

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

**FORM 10-K**

(Mark One)

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

For the fiscal year ended December 31, 2005

OR

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

Commission File Number 0-23827

**PC CONNECTION, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
incorporation or organization)

**02-0513618**

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

**Rt. 101A, 730 Milford Road  
Merrimack, New Hampshire**

(Address of principal executive offices)

**03054**

(Zip Code)

**(603) 683-2000**

Registrant's telephone number, including area code

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

Title of each class

Name of each exchange on which registered

None

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

**Common Stock, \$.01 par value**

(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

YES  NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

YES  NO

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES  NO

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

YES  NO

The aggregate market value of the registrant's voting shares of common stock held by non-affiliates of the registrant on June 30, 2005, based on \$6.21 per share, the last reported sale price on the NASDAQ National Market on that date, was \$48,601,422.

The number of shares outstanding of each of the registrant's classes of common stock, as of March 17, 2006:

Class	Number of Shares
Common Stock, \$.01 par value	25,259,261

The following documents are incorporated by reference into the Annual Report on Form 10-K: Portions of the registrant's definitive Proxy Statement for its 2006 Annual Meeting of Stockholders are incorporated by reference into Part III of this Report.

PC CONNECTION, INC. AND SUBSIDIARIES

FORM 10-K ANNUAL REPORT  
YEAR ENDED DECEMBER 31, 2005

TABLE OF CONTENTS

	<u>Page</u>
<b>PART I</b>	
ITEM 1. <a href="#">Business</a>	1
ITEM 1A. <a href="#">Risk Factors</a>	10
ITEM 1B. <a href="#">Unresolved Staff Comments</a>	15
ITEM 2. <a href="#">Properties</a>	15
ITEM 3. <a href="#">Legal Proceedings</a>	16
ITEM 4. <a href="#">Submission of Matters to a Vote of Security Holders</a>	16
<b>PART II</b>	
ITEM 5. <a href="#">Market for the Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities</a>	18
ITEM 6. <a href="#">Selected Financial Data</a>	19
ITEM 7. <a href="#">Management's Discussion and Analysis of Financial Condition and Results of Operations</a>	20
ITEM 7A. <a href="#">Quantitative and Qualitative Disclosure About Market Risk</a>	37
ITEM 8. <a href="#">Consolidated Financial Statements and Supplementary Data</a>	37
ITEM 9. <a href="#">Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</a>	37
ITEM 9A. <a href="#">Controls and Procedures</a>	37
ITEM 9B. <a href="#">Other Information</a>	38
<b>PART III</b>	
ITEM 10. <a href="#">Directors and Executive Officers of the Registrant</a>	39
ITEM 11. <a href="#">Executive Compensation</a>	39
ITEM 12. <a href="#">Security Ownership of Certain Beneficial Owners and Management and Related Shareholder Matters</a>	39
ITEM 13. <a href="#">Certain Relationships and Related Transactions</a>	39
ITEM 14. <a href="#">Principal Accountant Fees and Services</a>	39
<b>PART IV</b>	
ITEM 15. <a href="#">Exhibits and Financial Statement Schedules</a>	40
<a href="#">SIGNATURES</a>	45

**PART I**

**Item 1. Business**

**GENERAL**

We are a national direct marketer of a wide range of information technology products and services, including computer systems, software and peripheral equipment, networking communications, and other products and accessories that we purchase from manufacturers, distributors, and other suppliers. We operate through three primary business segments: (1) consumers and small- to medium-sized businesses, or SMB, through our PC Connection Sales subsidiaries, (2) federal, state, and local government and educational institutions, or Public Sector, through our GovConnection subsidiary, and (3) large corporate accounts, or Large Account, through our MoreDirect subsidiary. Our principal customers are SMBs (comprised of 20 to 1,000 employees), governmental agencies and educational organizations, and medium-to-large corporate accounts. We sell products through a combination of outbound telemarketing, field sales, targeted direct mail catalogs, our Internet Web sites, Internet advertising, and in selected computer magazines. We offer a broad selection of over 100,000 products targeted for business use at competitive prices, including products from Acer, Apple Computer, Cisco Systems, Hewlett-Packard, IBM, Lenovo, Microsoft, Sony, Symantec, and Toshiba. Our most frequently ordered products are carried in inventory and are typically shipped to customers the same day the order is received.

We are subject to the informational requirements of the Exchange Act, and accordingly, we file reports, proxy and information statements, and other information with the Securities and Exchange Commission, or SEC. Such reports and information can be read and copied at the public reference facilities maintained by the SEC at the Public Reference Room, 100 F Street, NE, Washington, D.C. 20549. Information regarding the operation at the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330. The SEC maintains a web site (<http://www.sec.gov>) that contains such reports and information regarding issuers that file electronically with the SEC. We maintain a Web site with the address [www.pcconnection.com](http://www.pcconnection.com). We are not including the information contained in our Web site as part of, or incorporating it by reference into, this annual report on Form 10-K. We make available free of charge through our Web site our annual reports on Form 10-K, quarterly reports on Form 10-Q, and current reports on Form 8-K, and amendments to these reports, as soon as reasonably practicable after we electronically file these materials with, or otherwise furnish them to, the SEC.

Since our founding in 1982, we have consistently served our customers' needs by providing innovative, reliable, and timely service and technical support, and by offering an extensive assortment of branded products through knowledgeable, well-trained sales and support teams. Our strategy's effectiveness is reflected in the recognition we have received, including being named to the Fortune 1000 and the VARBusiness 500 for the last five years.

We believe that our consistent customer focus has also resulted in strong brand name recognition and a broad and loyal customer base. At December 31, 2005, our mailing list consisted of approximately 3,600,000 customers, of which approximately 444,000 had purchased products from us within the last twelve months. Approximately 88% of our net sales in the year ended December 31, 2005 were made to customers who had previously purchased products from us. We believe we also have strong relationships with vendors, resulting in favorable product allocations and marketing assistance.

Our business-to-business marketing efforts are targeted to SMBs, government and educational organizations, and medium-to-large corporate accounts. As of December 31, 2005, we employed 618 account managers, including 186 new account managers with less than 12 months of outbound telemarketing experience with us. Account managers are responsible for managing corporate accounts and focus on outbound sales calls to prospective customers. We believe that increasing our sales representatives' productivity is critical to our future success, and we have increased our investments in this area accordingly.

## [Table of Contents](#)

We publish several catalogs, including PC Connection®, focusing on PCs and compatible products, and MacConnection®, focusing on Apple personal computers and compatible products. We also issue, from time to time, specialty catalogs, including GovConnection catalogs directed to government and education organizations. With colorful illustrations, concise product descriptions, relevant technical information, along with toll-free telephone numbers for ordering, our catalogs are recognized as a leading source for personal computer hardware, software, and other related products. We distributed approximately 27 million catalogs during the year ended December 31, 2005.

We also market our products and services through our Web sites: [www.pcconnection.com](http://www.pcconnection.com), [www.govconnection.com](http://www.govconnection.com), [www.macconnection.com](http://www.macconnection.com), and [www.moredirect.com](http://www.moredirect.com). Our Web sites provide customers and prospective customers with product information and enable customers to place electronic orders for products. For the fiscal year 2005, Internet sales processed directly online were \$382.9 million, or 26.5% of net sales, compared to 20.3% in 2004. These sales during the fourth quarter of 2005 were \$123.7 million, or 31.0% of that quarter's net sales, compared to 22.0% for the fourth quarter of 2004.

The Internet supports three key business initiatives for us:

- **Customer choice** — We have built our business on the premise that our customers should be able to choose how they interact with us, be it by mail, telephone, fax, e-mail, or over the Internet.
- **Lowering transactions costs** — Our Web site tools, including robust product search features and Internet Business Accounts, allow customers to quickly and easily find information about products of interest to them. If customers still have questions, they may call into our Telesales Representatives or Account Managers. Such phone calls are typically shorter and have higher close rates than calls from customers who have not first visited our Web sites.
- **Leveraging the time of experienced Account Managers** — Our investments in technology-based sales and service programs allow our Account Managers more time to build and maintain relationships with our customers and help them to solve their business problems.

Additional financial information regarding our business segments is contained in Management's Discussion and Analysis of Financial Condition and Results of Operations in Item 7 of Part II, and Note 16 to our Consolidated Financial Statements included in Item 8 of Part II of this Annual Report on Form 10-K.

## MARKET AND COMPETITION

We generate approximately 58% of our sales from the SMB market, 24% from medium-to-large corporate accounts (Fortune 1000), and 18% from governmental agencies and educational organizations. We estimate the overall U.S. Information Technology market that we serve to be in excess of \$200 billion. The largest segment of the market is served by local and regional "value added resellers," or VARs, many of whom we believe are transitioning from the hardware and software business to IT services, which generally have higher margins.

We have transitioned from an end-user or desktop-centric computing supplier to a network or enterprise-wide computing supplier. We have also partnered with third-party technology and telecommunications service providers. We now offer access to the same services and technical expertise to our customers as local and regional VARs, but with more extensive product selection at lower prices.

Intense competition for customers has led manufacturers of PCs and related products to use all available channels, including direct marketers, to distribute products. Certain manufacturers who have traditionally used resellers to distribute their products have established or attempted to establish their own direct marketing operations, including sales through the Internet. Accordingly, we believe that these manufacturers of PCs and related products will continue to provide us and other third-party direct marketers favorable product allocations and marketing support.

## [Table of Contents](#)

We believe new entrants to the direct marketing channel must overcome a number of obstacles, including:

- the substantial time and resources required to build a customer base of meaningful size, quality, and responsiveness for cost-effective circulation;
- the high costs of developing the information and operating infrastructure required by direct marketers;
- the advantages enjoyed by larger and more established competitors in terms of purchasing and operating efficiencies;
- the difficulty of building relationships with manufacturers to achieve favorable product allocations and attractive pricing terms; and
- the difficulty of identifying and recruiting management personnel with significant direct marketing experience in the industry.

### **BUSINESS STRATEGIES**

Our objective is to become the principal supplier of information technology products and solutions, including personal computers and related products and services, to our customers. The key elements of our business strategies include:

- ***Providing consistent customer service before, during, and after the sale.*** We believe that we have earned a reputation for providing superior customer service by consistently focusing on our customers' needs. We deliver value to our customers through high-quality service and technical support provided by our knowledgeable, well-trained personnel. We also have efficient delivery programs and offer our customers reasonable return policies.
- ***Offering a broad product selection at competitive prices.*** We offer our customers a wide assortment of information technology products and solutions, including personal computers and related products and networking products, at competitive prices. Our merchandising programs feature products that provide customers with aggressive price and performance and the convenience of one-stop shopping for their personal computer and related needs.
- ***Maintaining a strong brand name and customer awareness.*** Since our founding in 1982, we have built a strong brand name and customer awareness. We have been named to the Fortune 1000 and the VARBusiness 500 for the last five years. Our mailing list includes approximately 3,600,000 names, of which approximately 444,000 have purchased products from us during the last 12 months.
- ***Maintaining long-standing vendor relationships.*** We have a history of strong relationships with vendors, and were among the first direct marketers qualified by manufacturers to market computer systems to end users. We provide our vendors with both information concerning customer preferences and an efficient channel for the advertising and distribution of their products.

### **GROWTH STRATEGIES**

Our growth strategies are to increase revenues derived from our penetration of our existing customers, broaden our product offerings, and expand our customer base. The key elements of our growth strategies include:

- ***Expanding product and service offerings.*** We continually evaluate information technology products and services focused on business users, adding new products and services as they become available or in response to customer demand. We work closely with vendors to identify and source first-to-market product offerings at aggressive prices, and believe that the expansion of our corporate outbound marketing program will enhance our access to such product offerings. In addition to using our own inventories, we utilize our distribution and manufacturing suppliers to drop ship products directly to our customers. We drop shipped 44% of our net sales in 2005, compared to 38% in 2004.

## [Table of Contents](#)

- **Increasing outbound telemarketing productivity.** We believe that higher sales productivity is the key to leveraging our expense structure and driving future profitability improvements. We plan to expand and focus our training and evaluation programs, system enhancements, and sales tools more towards assisting our sales personnel in improving their productivity. As we increase our productivity, we plan to increase the number of our corporate account managers and assign them a greater number of our customers.
- **Expanding electronic commerce channel.** Our Web-based catalog provides detailed product descriptions, product search capabilities, and online order processing. This channel provides our customers with a convenient means of shopping with us, and it also allows us to leverage our account managers more effectively. The number of Internet Business Account users grew from 138,000 at December 31, 2004 to approximately 168,000 at December 31, 2005. We plan to further improve online sales capabilities, including product information and customer service and support available on our Web site.
- **Targeting customer segments.** Through targeted marketing, we seek to expand the number of our active customers and generate additional sales from these existing customers. We have developed specialty catalogs, as well as standard catalogs with special cover pages, featuring product offerings designed to address the needs of specific customer populations, including new product inserts targeted to purchasers of graphics, server, and networking products.
- **Pursuing strategic acquisitions and alliances.** We seek acquisitions and alliances that add new customers, strengthen our product offerings, add management talent, and produce operating results which are accretive to our core business earnings. In 2002, we acquired MoreDirect, a premier e-procurement supplier of IT products for medium-to-large corporate organizations nationwide. In October 2005, we acquired selected assets of Amherst Technologies, and as a result, we added approximately 40 former Amherst sales representatives in the fourth quarter of 2005.

## **SERVICE AND SUPPORT**

Since our founding in 1982, our primary objective has been to provide products that meet the demands and needs of customers and to supplement those products with up-to-date product information and excellent customer service and support. We believe that offering our customers superior value, through a combination of product knowledge, consistent and reliable service, and leading products at competitive prices, differentiates us from other direct marketers and provides the foundation for developing a broad and loyal customer base.

We invest in training programs for our service and support personnel, with an emphasis on putting customer needs and service first. We provide toll-free technical support from 9:00 a.m. through 5:30 p.m. Eastern Time, Monday through Friday. Product support technicians assist callers with questions concerning compatibility, installation, determination of defects, and more difficult questions relating to product use. The product support technicians authorize customers to return defective or incompatible products to either the manufacturer or to us for warranty service. In-house technicians perform both warranty and non-warranty repair on most major systems and hardware products.

Using our customized information system, we send our customer orders to our distribution center for processing immediately after a customer receives credit approval. Through our Everything Overnight® service, orders accepted up until 2:00 a.m. Eastern Time, (until midnight on most custom-configured systems) are generally shipped for overnight delivery via DHL Worldwide. We also configure approximately 20% of the computer systems we ship from our distribution center. Configuration typically consists of the installation of memory, accessories, and/or software.

## MARKETING AND SALES

We sell our products through our direct marketing channels to SMBs, government agencies and educational organizations, and medium-to-large corporate accounts. We seek to be the primary supplier of information technology products and solutions, including personal computers and related products, to our existing customers and to expand our customer base. We use multiple marketing approaches to reach existing and prospective customers, including:

- outbound telemarketing and field sales;
- Web and print media advertising;
- marketing programs targeted to specific customer populations; and
- catalogs and inbound telesales.

All of our marketing approaches emphasize our broad product offerings, fast delivery, customer support, competitive pricing, and our increasing range of service solutions.

We believe that our ability to establish and maintain long-term customer relationships and to encourage repeat purchases is largely dependent on the strength of our telemarketing personnel and programs. Because our customers' primary contact with us is through our telemarketers, we are committed to maintaining a qualified, knowledgeable, and motivated sales staff with its principal focus on customer service.

**Sales Channels.** The following table sets forth our percentage of net sales by sales channel:

Sales Channel	Years Ended December 31,		
	2005	2004	2003
Outbound Telemarketing and Field Sales	69%	74%	77%
Online Internet	26	20	16
Inbound Telesales	5	6	7
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>

**Outbound Telemarketing and Field Sales.** We seek to build loyal relationships with our potential high-volume customers by assigning them to individual account managers. We believe that customers respond favorably to a one-on-one relationship with personalized, well-trained account managers. Once established, these one-on-one relationships are maintained and enhanced through frequent telecommunications and targeted catalogs and other marketing materials designed to meet each customer's specific IT needs. We pay most of our account managers a base annual salary plus incentive compensation. Incentive compensation is tied to gross profit dollars produced by the individual account manager. Account managers historically have significantly increased productivity after approximately twelve months of training and experience. At December 31, 2005, we employed 618 sales representatives, including 186 with less than twelve months of outbound telemarketing experience with us.

**Online Internet.** ([www.pcconnection.com](http://www.pcconnection.com), [www.govconnection.com](http://www.govconnection.com), [www.macconnection.com](http://www.macconnection.com), and [www.moredirect.com](http://www.moredirect.com)) We provide product descriptions and prices of all products online. Our PC Connection Web site also provides updated information for over 90,000 items and on-screen images for more than 58,000 items. We offer, and continuously update, selected product offerings and other special buys. We believe that our Web sites will be an increasingly important sales source and communication tool for improving customer service.

**Inbound Telesales.** Our inbound sales representatives answer customer telephone calls generated by our catalogs and other advertising programs. These representatives also assist customers in making purchasing decisions, process product orders, and respond to customer inquiries on order status, product

## [Table of Contents](#)

pricing, and availability. Using our proprietary information systems, sales representatives can quickly access customer records which detail purchase history and billing and shipping information, expediting the ordering process. Our two principal catalogs are PC Connection® for the PC market and MacConnection® for the Apple market. In 2005, we published twelve editions of each. We distribute catalogs to purchasers on our in-house mailing list as well as to other prospective customers. In addition, we distribute specialty catalogs to educational and governmental customers and prospects on a periodic basis. We also distribute our monthly catalogs customized with special covers and inserts, offering a wider assortment of special offers on products in specific areas such as graphics, server/netcom, and mobile computing, or for specific customers, such as developers.

**Business Segments.** We conduct our business operations through three primary business segments: (1) SMB, (2) Large Account, and (3) Public Sector.

**SMB Segment.** While we continue to generate credit card sales to consumers, our principal target customers in this segment are small-to-medium-sized business customers with 20 to 1,000 employees. Our primary means of marketing to this segment incorporate all three sales channels—outbound telemarketing, primarily to our business customers; inbound telesales, particularly to our consumer group; and online Internet sales to both consumer and business customers.

**Large Account Segment.** Through our MoreDirect subsidiary's custom designed Web-based system, we are able to offer our larger corporate customers an efficient and effective method of sourcing, evaluating, purchasing, and tracking a wide variety of IT products and services. MoreDirect's account managers typically have ten to twenty years of experience and are located strategically across the United States. This allows them to work directly with customers, often on site. MoreDirect generally places all product orders with manufacturers and/or distribution companies for drop shipment directly to its customers.

**Public Sector Segment.** We use a combination of outbound telemarketing, including some on-site sales solicitation by field sales account managers, and online Internet sales through Internet Business Accounts, to reach these customers. Through our GovConnection subsidiary, we target each of the four distinct market sectors within this segment—federal government, higher educational institutions, school grades K through 12, and state and local governments.

The following table sets forth the relative distribution of our net sales by business segment:

Business Segment	Years Ended December 31,		
	2005	2004	2003
SMB	58%	59%	57%
Large Account	24	22	19
Public Sector	18	19	24
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>

**Specialty Marketing.** Our specialty marketing activities include direct mail, other inbound and outbound telemarketing services, bulletin board services, package inserts, fax broadcasts, and electronic mail. We also market call-answering and fulfillment services to certain of our product vendors.

**Customers.** We maintain an extensive database of customers and prospects currently aggregating approximately 3,600,000 names. Approximately 88% of our net sales in the year ended December 31, 2005 were made to customers who had previously purchased products from us. Except for sales to the federal government, no single customer accounted for more than 2% of our consolidated revenue in 2005. The loss of any single customer will not have a material adverse effect on any of our business segments. In addition, we do not have individual orders in our backlog that are material to our business.



## PRODUCTS AND MERCHANDISING

We continuously focus on expanding the breadth of our product offerings. We currently offer our customers over 100,000 information technology products designed for business applications from more than 1,000 manufacturers, including hardware and peripherals, accessories, networking products, and software. We select the products that we sell based upon their technology and effectiveness, market demand, product features, quality, price, margins, and warranties. As part of our merchandising strategy, we also offer products related to PCs, such as digital cameras.

The following table sets forth our percentage of net sales (in dollars) of notebooks and personal digital assistants (“PDAs”), desktops and servers, storage devices, software, networking communications products, printers and printer supplies, video, imaging, and sound, memory and system enhancements, and accessories and other products during the years ended December 31, 2005, 2004, and 2003.

	PERCENTAGE OF NET SALES		
	Years Ended December 31,		
	2005	2004	2003
Notebooks and PDAs	18%	21%	20%
Desktops/Servers	14	14	15
Storage Devices	9	8	9
Software	12	12	11
Net/Com Products	8	7	8
Printers and Printer Supplies	11	11	11
Video, Imaging, and Sound	12	12	12
Memory and System Enhancements	5	5	5
Accessories/Other	11	10	9
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>

We offer a 30-day right of return generally limited to defective merchandise. Returns of non-defective products are subject to restocking fees. Substantially all of the products marketed by us are warranted by the manufacturer. We generally accept returns directly from the customer and then either credit the customer’s account or ship the customer a similar product from our inventory.

## PURCHASING AND VENDOR RELATIONS

During the year ended December 31, 2005, we purchased approximately 61% of our products from distributors and aggregators and the balance directly from manufacturers. We ship the majority of our purchases directly to our distribution facility in Wilmington, Ohio. During the years ended December 31, 2005, 2004, and 2003, product purchases from Ingram Micro, Inc., our largest vendor, accounted for approximately 26%, 27%, and 22%, respectively, of our total product purchases. Purchases from Tech Data Corporation comprised 19%, 14%, and 15% of our total product purchases in the years ended December 31, 2005, 2004, and 2003, respectively. Purchases from HP constituted 11%, 11%, and 15% of our total product purchases in 2005, 2004, and 2003, respectively. No other vendor accounted for more than 10% of our total product purchases in the years ended December 31, 2005, 2004, and 2003. We believe that alternative sources for products obtained from Ingram Micro, Tech Data, and HP are available to us.

Many product suppliers reimburse us for advertisements or other cooperative marketing programs in our catalogs or advertisements in personal computer magazines that feature a manufacturer’s product. Reimbursements may be in the form of discounts, advertising allowances, and/or rebates. We also receive reimbursements from certain vendors based upon the volume of purchases or sales of the vendors’ products by us.

Some of our vendors offer limited price protection in the form of rebates or credits against future purchases. We may also participate in end-of-life-cycle and other special purchases which may not be eligible for price protection.

## [Table of Contents](#)

We believe that we have excellent relationships with vendors. We generally pay vendors within stated terms and take advantage of all appropriate discounts. We believe that because of our volume purchases we are able to obtain product pricing and terms that are competitive with those available to other major direct marketers. Although brand names and individual product offerings are important to our business, we believe that competitive products are available in substantially all of the merchandise categories offered by us.

### **DISTRIBUTION**

At our approximately 205,000 square foot distribution and fulfillment complex in Wilmington, Ohio, we receive and ship inventory, configure computer systems, and process returned products. Orders are transmitted electronically from our Connecticut, Maryland, Massachusetts, New Hampshire, and Texas sales facilities to our Wilmington distribution center after credit approval, where packing documentation is printed automatically and order fulfillment takes place. Through our Everything Overnight<sup>®</sup> service, orders accepted up until 2:00 a.m. Eastern time, (until midnight on custom-configured systems) are generally shipped for overnight delivery via DHL Worldwide Express. We ship approximately 50% of our orders through DHL. Upon request, orders may also be shipped by other common carriers.

We also place product orders directly with manufacturers and/or distribution companies for drop shipment by those manufacturers and/or suppliers directly to customers. Our MoreDirect subsidiary generally places all product orders with manufacturers and/or distribution companies for drop shipment directly to customers. Order status with distributors is tracked online and in all circumstances, a confirmation of shipment from manufacturers and/or distribution companies is received prior to initial recording of the transaction. At the end of each financial reporting period, revenue is adjusted pursuant to Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements" to reflect the anticipated receipt of products by the customers in the period. Products dropped shipped by suppliers increased from 38% of net sales in 2004 to 44% of net sales in 2005. In future years, we expect that products drop shipped from suppliers will continue to increase, both in dollars and as a percentage of net sales, as we seek to lower our overall inventory and distribution costs while maintaining excellent customer service.

### **MANAGEMENT INFORMATION SYSTEMS**

All of our subsidiaries, except for MoreDirect, use management information systems, principally comprised of applications software running on IBM AS/400 and RS6000 computers and Microsoft Windows 2003-based servers, which we have customized for our use. These systems permit centralized management of key functions, including order taking and processing, inventory and accounts receivable management, purchasing, sales, and distribution, and the preparation of daily operating control reports on key aspects of the business. We also operate advanced telecommunications equipment to support our sales and customer service operations. Key elements of the telecommunications systems are integrated with our computer systems to provide timely customer information to sales and service representatives, and to facilitate the preparation of operating and performance data.

MoreDirect has developed a custom designed Internet-based system, Traxx<sup>®</sup>, which comprises applications software running on Linux and Sun Solaris servers. This system is an integrated application of sales order processing, integrated supply chain visibility, and full EDI links with major manufacturers' distribution partners for product information, availability, pricing, ordering, delivery, and tracking, including related accounting functions.

We believe that our customized information systems enable us to improve our productivity, ship customer orders on a same-day basis, respond quickly to changes in our industry, and provide high levels of customer service.

Our success is dependent in large part on the accuracy and proper use of our information systems, including our telephone systems, to manage our inventory and accounts receivable collections, to purchase, sell, and ship

## [Table of Contents](#)

our products efficiently and on a timely basis, and to maintain cost-efficient operations. We have undertaken a significant upgrade of our sales processing systems and expect to continually upgrade our information systems to more effectively manage our operations and customer database.

### **COMPETITION**

The direct marketing and sale of information technology products, including personal computers and related products, is highly competitive. We compete with other direct marketers of IT products, including CDW Corporation and Insight Enterprises, Inc., who are much larger than we are. We also compete with:

- certain product manufacturers that sell directly to customers, such as Dell Inc. and Gateway, Inc., as well as some of our own suppliers, such as HP, Lenovo, and Apple;
- distributors that sell directly to certain customers;
- various cost-plus aggregators, franchisers, and national computer retailers; and
- companies with more extensive Web sites and commercial online networks.

Additional competition may arise if other new methods of distribution, such as broadband electronic software distribution, emerge in the future.

We compete not only for customers, but also for favorable product allocations and cooperative advertising support from product manufacturers. Several of our competitors are larger and have substantially greater financial resources than we have.

We believe that price, product selection and availability, and service and support are the most important competitive factors in our industry.

### **INTELLECTUAL PROPERTY RIGHTS**

Our trademarks include PC Connection<sup>®</sup>, GovConnection<sup>®</sup>, MacConnection<sup>®</sup>, and MoreDirect<sup>®</sup>, and their related logos; Everything Overnight<sup>®</sup>, The Connection<sup>®</sup>, Raccoon Character<sup>®</sup>, Service Connection<sup>®</sup>, HealthConnection<sup>™</sup>, Graphics Connection<sup>®</sup>, and Education Connection<sup>®</sup>, Your Brands, Your Way, Next Day<sup>®</sup>, and Epiq PC Systems<sup>®</sup>. We intend to use and protect these and our other marks, as we deem necessary. We believe our trademarks have significant value and are an important factor in the marketing of our products. We do not maintain a traditional research and development group, but we work closely with computer product manufacturers and other technology developers to stay abreast of the latest developments in computer technology, both with respect to the products we sell and use.

### **WORK FORCE**

As of December 31, 2005, we employed 1,571 persons, of whom 801 were engaged in sales related activities, 165 were engaged in providing IT services and customer service and support, 288 were engaged in purchasing, marketing, and distribution related activities, 95 were engaged in the operation and development of management information systems, and 222 were engaged in administrative and accounting functions. We consider our employee relations to be good. Our employees are not represented by a labor union, and we have never experienced a work stoppage since our inception.

## [Table of Contents](#)

### **Item 1A. Risk Factors**

Statements contained or incorporated by reference in this Annual Report on Form 10-K that are not based on historical fact are “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Exchange Act. These forward-looking statements regarding future events and our future results are based on current expectations, estimates, forecasts, and projections and the beliefs and assumptions of our management including, without limitation, our expectations with regard to the industry’s rapid technological change and exposure to inventory obsolescence, availability and allocations of goods, reliance on vendor support and relationships, competitive risks, pricing risks, and the overall level of economic activity and the level of business investment in information technology products. Forward-looking statements may be identified by the use of forward-looking terminology such as “may,” “could,” “will,” “expect,” “estimate,” “anticipate,” “continue,” or similar terms, variations of such terms or the negative of those terms.

We cannot assure investors that our assumptions and expectations will prove to have been correct. Important factors could cause our actual results to differ materially from those indicated or implied by forward-looking statements. Such factors that could cause or contribute to such differences include those factors discussed below. We undertake no intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. If any of the following risks actually occur, our business, financial condition or results of operations would likely suffer.

### **FACTORS THAT MAY AFFECT FUTURE RESULTS AND FINANCIAL CONDITION**

#### **We have experienced variability in sales, and there is no assurance that we will be able to maintain profitable operations.**

Several factors have caused our sales and results of operations to fluctuate and we expect these fluctuations to continue on a quarterly basis. Causes of these fluctuations include:

- changes in the overall level of economic activity;
- the condition of the personal computer industry in general;
- changes in the level of business investment in information technology products;
- shifts in customer demand for hardware and software products;
- variations in levels of competition;
- industry shipments of new products or upgrades;
- the timing of new merchandise and catalog offerings;
- fluctuations in response rates;
- fluctuations in postage, paper, shipping, and printing costs and in merchandise returns;
- adverse weather conditions that affect response, distribution, or shipping;
- changes in our product offerings;
- changes in consumer demand for information technology products; and
- changes in vendor distribution of products.

Our results also may vary based on our success of integrating acquisitions into our business, the impact of the costs of acquisitions and integration, and our ability to hire and retain sales representatives and other essential personnel. In addition, customer response rates for our catalogs and other marketing vehicles are subject to variations. The first and last quarters of the year generally have higher response rates while the two middle quarters typically have lower response rates.

## [Table of Contents](#)

We base our operating expenditures on sales forecasts. If our revenues do not meet anticipated levels in the future, we may not be able to reduce our staffing levels and operating expenses in a timely manner to avoid significant losses from operations.

**Despite our August 2004 award of an authorization to sell to the federal government under a new General Services Administration (“GSA”) schedule, our sales to that organization may not regain prior years’ sales levels, which would negatively impact our business.**

In November 2003, we were advised that the GSA canceled its contract with our subsidiary, GovConnection, following a review of its contract management system and procedures and the possibility of the sale of unqualified items or underpayment of required fees. The matter has been referred to the Department of Justice for review, and we are cooperating in that review. While we were awarded authorization in August 2004 to resume selling to the federal government under a new GSA schedule, we experienced significant declines in our 2004 and 2005 federal government sales from 2003 levels. Accordingly, our revenues may continue to be adversely impacted as we attempt to regain this business.

**We are exposed to inventory obsolescence due to the rapid technological changes occurring in the personal computer industry.**

The market for personal computer products is characterized by rapid technological change and the frequent introduction of new products and product enhancements. Our success depends in large part on our ability to identify and market products that meet the needs of customers in that marketplace. In order to satisfy customer demand and to obtain favorable purchasing discounts, we have and may continue to carry increased inventory levels of certain products. By so doing, we are subject to the increased risk of inventory obsolescence. Also, in order to implement our business strategy, we intend to continue, among other things, placing larger than typical inventory stocking orders and increasing our participation in first-to-market purchase opportunities. We may also participate in end-of-life-cycle purchase opportunities and market products on a private-label basis, which would increase the risk of inventory obsolescence. In addition, we sometimes acquire special purchase products without return privileges. There can be no assurance that we will be able to avoid losses related to obsolete inventory. In addition, manufacturers are limiting return rights and are taking steps to reduce their inventory exposure by supporting “build-to-order” programs authorizing distributors and resellers to assemble computer hardware under the manufacturers’ brands. These trends reduce the costs to manufacturers and shift the burden of inventory risk to resellers like us, which could negatively impact our business.

**We acquire products for resale from a limited number of vendors. The loss of any one of these vendors could have a material adverse effect on our business.**

We acquire products for resale both directly from manufacturers and indirectly through distributors and other sources. The five vendors supplying the greatest amount of goods to us constituted 67%, 63%, and 63% of our total product purchases in the years ended December 31, 2005, 2004, and 2003, respectively. Among these five vendors, purchases from Ingram represented 26%, 27%, and 22% of our total product purchases in the years ended December 31, 2005, 2004, and 2003, respectively. Purchases from Tech Data comprised 19%, 14%, and 15% of our total product purchases in the years ended December 31, 2005, 2004, and 2003, respectively. Purchases from HP represented 11%, 11%, and 15% of our total product purchases in the years ended December 31, 2005, 2004, and 2003, respectively. No other vendor supplied more than 10% of our total product purchases in the years ended December 31, 2005, 2004, and 2003, respectively. If we were unable to acquire products from Ingram, HP, or Tech Data, we could experience a short-term disruption in the availability of products, and such disruption could have a material adverse effect on our results of operations and cash flows.

Substantially all of our contracts and arrangements with our vendors that supply significant quantities of products are terminable by such vendors or us without notice or upon short notice. Most of our product vendors provide us with trade credit, of which the net amount outstanding at December 31, 2005 was \$114.4 million.

## [Table of Contents](#)

Termination, interruption, or contraction of relationships with our vendors, including a reduction in the level of trade credit provided to us, could have a material adverse effect on our financial position.

Some product manufacturers either do not permit us to sell the full line of their products or limit the number of product units available to direct marketers such as us. An element of our business strategy is to continue increasing our participation in first-to-market purchase opportunities. The availability of certain desired products, especially in the direct marketing channel, has been constrained in the past. We could experience a material adverse effect to our business if we are unable to source first-to-market purchase or similar opportunities, or if we face the reemergence of significant availability constraints.

### **We may experience a reduction in the incentive programs offered to us by our vendors.**

Some product manufacturers and distributors provide us with incentives such as supplier reimbursements, payment discounts, price protection, rebates, and other similar arrangements. The increasingly competitive computer hardware market has already resulted in the following:

- reduction or elimination of some of these incentive programs;
- more restrictive price protection and other terms; and
- reduced advertising allowances and incentives, in some cases.

Many product suppliers provide us with co-op advertising support, and in exchange, we feature their products in our catalogs. This support significantly defrays our catalog production expense. In the past, we have experienced a decrease in the level of co-op advertising support available to us from certain manufacturers. The level of co-op advertising support we receive from some manufacturers may further decline in the future. Such a decline could decrease our gross margin and increase our SG&A expenses as a percentage of sales and have a material adverse effect on our cash flows.

### **We face many competitive risks.**

The direct marketing industry and the computer products retail business, in particular, are highly competitive. We compete with consumer electronics and computer retail stores, including superstores. We also compete with other direct marketers of hardware and software and computer related products, including CDW Corporation, Insight Enterprises, Inc., and Dell Inc., who are much larger than we are. Certain hardware and software vendors, such as HP, Lenovo, and Apple, who provide products to us, are also selling their products directly to end users through their own catalogs and over the Internet. We compete not only for customers, but also for co-op advertising support from personal computer product manufacturers. Some of our competitors have larger catalog circulations and customer bases and greater financial, marketing, and other resources than we do. In addition, some of our competitors offer a wider range of products and services than we do and may be able to respond more quickly to new or changing opportunities, technologies, and customer requirements. Many current and potential competitors also have greater name recognition, engage in more extensive promotional activities, and adopt pricing policies that are more aggressive than ours. We expect competition to increase as retailers and direct marketers who have not traditionally sold computers and related products enter the industry.

In addition, product resellers and direct marketers are combining operations or acquiring or merging with other resellers and direct marketers to increase efficiency. Moreover, current and potential competitors have established or may establish cooperative relationships among themselves or with third parties to enhance their products and services. Accordingly, it is possible that new competitors or alliances among competitors may emerge and acquire significant market share.

We cannot assure you that we can continue to compete effectively against our current or future competitors. If we encounter new competition or fail to compete effectively against our competitors, our business may be harmed.

**We face and will continue to face significant price competition.**

Generally, pricing is very aggressive in the personal computer industry, and we expect pricing pressures to continue. An increase in price competition could result in a reduction of our profit margins. There can be no assurance that we will be able to offset the effects of price reductions with an increase in the number of customers, higher sales, cost reductions, or otherwise. Also, our sales of personal computer hardware products are generally producing lower profit margins than those associated with software products. Such pricing pressures could result in an erosion of our market share, reduced sales, and reduced operating margins, any of which could have a material adverse effect on our business.

**The methods of distributing personal computers and related products are changing, and such changes may negatively impact us and our business.**

The manner in which personal computers and related products are distributed and sold is changing, and new methods of distribution and sale, such as online shopping services, have emerged. Hardware and software manufacturers have sold, and may intensify their efforts to sell, their products directly to end users. From time to time, certain manufacturers have instituted programs for the direct sales of large order quantities of hardware and software to certain major corporate accounts. These types of programs may continue to be developed and used by various manufacturers. Some of our vendors, including Apple, HP, and Lenovo, currently sell some of their products directly to end users and have stated their intentions to increase the level of such direct sales. In addition, manufacturers may attempt to increase the volume of software products distributed electronically to end users. An increase in the volume of products sold through or used by consumers of any of these competitive programs or distributed electronically to end users could have a material adverse effect on our results of operations.

**We could experience system failures which would interfere with our ability to process orders.**

We depend on the accuracy and proper use of our management information systems, including our telephone system. Many of our key functions depend on the quality and effective utilization of the information generated by our management information systems, including:

- our ability to manage inventory and accounts receivable collection;
- our ability to purchase, sell, and ship products efficiently and on a timely basis; and
- our ability to maintain operations.

Our management information systems require continual upgrades to most effectively manage our operations and customer database. We are currently in the midst of a major upgrade to our sales processing system. Although we maintain some redundant systems, with full data backup, a substantial interruption in management information systems or in telephone communication systems, including those resulting from natural disasters as well as power loss, telecommunications failure, and similar events, would substantially hinder our ability to process customer orders and thus could have a material adverse effect on our business.

**We rely on the continued development of electronic commerce and Internet infrastructure development.**

We have had an increasing level of sales made over the Internet in part because of the growing use and acceptance of the Internet by end users. No one can be certain that acceptance and use of the Internet will continue to develop or that a sufficiently broad base of consumers will adopt and continue to use the Internet and other online services as a medium of commerce. Sales of computer products over the Internet represent a significant and increasing portion of overall computer product sales. Growth of our Internet sales is dependent on potential customers using the Internet in addition to traditional means of commerce to purchase products. We cannot accurately predict the rate at which they will do so.

Our success in growing our Internet business will depend in large part upon the development of an infrastructure for providing Internet access and services. If the number of Internet users or their use of Internet

## [Table of Contents](#)

resources continues to grow rapidly, such growth may overwhelm the existing Internet infrastructure. Our ability to increase the speed with which we provide services to customers and to increase the scope of such services ultimately is limited by, and reliant upon, the speed, reliability, and cost-effectiveness of the networks operated by third parties, and these networks may not continue to be developed or be available at prices consistent with our required business model.

### **We depend heavily on third-party shippers to deliver our products to customers.**

We ship approximately 50% of our products to customers by DHL Worldwide Express (“DHL”), with the remainder being shipped by United Parcel Service, Inc. and other overnight delivery and surface services. A strike or other interruption in service by these shippers could adversely affect our ability to market or deliver products to customers on a timely basis.

### **We may experience potential increases in shipping, paper, and postage costs, which may adversely affect our business if we are not able to pass such increases on to our customers.**

Shipping costs are a significant expense in the operation of our business. Increases in postal or shipping rates and paper costs could significantly impact the cost of producing and mailing our catalogs and shipping customer orders. Postage prices and shipping rates increase periodically, and we have no control over future increases. We have a long-term contract with DHL whereby DHL ships products to our customers. We believe that we have negotiated favorable shipping rates with DHL. We generally invoice customers for shipping and handling charges. There can be no assurance that we will be able to pass on to our customers the full cost, including any future increases in the cost, of commercial delivery services such as DHL.

We also incur substantial paper and postage costs related to our marketing activities, including producing and mailing our catalogs. Paper prices historically have been cyclical, and we have experienced substantial increases in the past. Significant increases in postal or shipping rates and paper costs could adversely impact our business, financial condition, and results of operations, particularly if we cannot pass on such increases to our customers or offset such increases by reducing other costs.

### **Privacy concerns with respect to list development and maintenance may materially adversely affect our business.**

We mail catalogs and send electronic messages to names in our proprietary customer database and to potential customers whose names we obtain from rented or exchanged mailing lists. World-wide public concern regarding personal privacy has subjected the rental and use of customer mailing lists and other customer information to increased scrutiny. Any domestic or foreign legislation enacted limiting or prohibiting these practices could negatively affect our business.

### **We face many uncertainties relating to the collection of state sales and use tax.**

We presently collect sales and use tax on sales of products to residents in many states. During the year ended December 31, 2005, we collected sales and use tax on approximately 19% of our net sales. Various states have sought to impose on direct marketers the burden of collecting state sales and use taxes on the sales of products shipped to their residents. In 1992, the United States Supreme Court affirmed its position that it is unconstitutional for a state to impose sales or use tax collection obligations on an out-of-state mail-order company whose only contacts with the state are limited to the distribution of catalogs and other advertising materials through the mail and the subsequent delivery of purchased goods by United States mail or by interstate common carrier. However, legislation that would expand the ability of states to impose sales and use tax collection obligations on direct marketers has been introduced in Congress on many occasions. Additionally, certain states have adopted rules that require companies and their affiliates to register in those states as a condition of doing business within those states. Moreover, due to our presence on various forms of electronic



## [Table of Contents](#)

media and other operational factors, our contacts with many states may exceed the limited contacts involved in the Supreme Court case. We cannot predict the level of contacts that is sufficient to permit a state to impose on us a sales or use tax collection obligation. Two of our competitors have elected to collect sales and use taxes in all states. If the Supreme Court changes its position, or if legislation is passed to overturn the Supreme Court's decision, or if a court were to determine that our contacts with a state exceed the constitutionality permitted contacts, the imposition of a sales or use tax collection obligation on us in states to which we ship products would result in additional administrative expenses to us, could result in tax liability for past sales as well as price increases to our customers, and could reduce demand for our product.

### **We are dependent on key personnel.**

Our future performance will depend to a significant extent upon the efforts and abilities of our senior executives. The competition for qualified management personnel in the computer products industry is very intense, and the loss of service of one or more of these persons could have an adverse effect on our business. Our success and plans for future growth will also depend on our ability to hire, train, and retain skilled personnel in all areas of our business, including sales account managers and technical support personnel. There can be no assurance that we will be able to attract, train, and retain sufficient qualified personnel to achieve our business objectives.

### **We are controlled by two principal stockholders.**

Patricia Gallup and David Hall, our two principal stockholders, beneficially own or control, in the aggregate, approximately 68% of the outstanding shares of our common stock. Because of their beneficial stock ownership, these stockholders can continue to elect the members of the Board of Directors and decide all matters requiring stockholder approval at a meeting or by a written consent in lieu of a meeting. Similarly, such stockholders can control decisions to adopt, amend, or repeal our charter and our bylaws, or take other actions requiring the vote or consent of our stockholders and prevent a takeover of us by one or more third parties, or sell or otherwise transfer their stock to a third party, which could deprive our stockholders of a control premium that might otherwise be realized by them in connection with an acquisition of us. Such control may result in decisions that are not in the best interest of our public stockholders. In connection with our initial public offering, the principal stockholders placed substantially all shares of common stock beneficially owned by them into a voting trust, pursuant to which they are required to agree as to the manner of voting such shares in order for the shares to be voted. Such provisions could discourage bids for our common stock at a premium as well as have a negative impact on the market price of our common stock.

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

None.

### **Item 2. Properties**

In November 1997, we entered into a fifteen year lease for our corporate headquarters and telemarketing center located at 730 Milford Road, Merrimack, New Hampshire 03054-4631, with an affiliated entity, G&H Post, which is related to us through common ownership. The total lease is valued at approximately \$7.0 million, based upon an independent property appraisal obtained at the date of lease, and interest is calculated at an annual rate of 11%. The lease requires us to pay our proportionate share of real estate taxes and common area maintenance charges as additional rent and also to pay insurance premiums for the leased property. We have the option to renew the lease for two additional terms of five years each. The lease has been recorded as a capital lease in the financial statements.

We also lease 205,000 square feet in two facilities in Wilmington, Ohio, which houses our distribution and order fulfillment operations. The leases governing these two facilities expire in the first quarter of 2007 and the fourth quarter of 2009, respectively. We also operate telemarketing centers in Keene and Portsmouth, New Hampshire; Marlborough, Massachusetts; Rockville, Maryland; Fairfield, Connecticut; and Boca Raton, Florida. We also opened a new sales office in Addison, Texas during the first quarter of 2006. Leasehold improvements

## [Table of Contents](#)

associated with these properties are amortized over the terms of the leases or their useful lives, whichever is shorter. We believe that existing distribution facilities in Wilmington, Ohio will be sufficient to support our anticipated needs through the next twelve months and beyond.

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

On March 20, 2002, The Lemelson Medical, Education & Research Foundation, L.P. filed a complaint in U.S. District Court for the District of Arizona naming us as an additional defendant in the so-called "Federal Express" case. The Federal Express case involves approximately eighty-eight defendants and pertains to claims made by the foundation relating to its right to royalties for the use of bar code scanners that allegedly utilize technology covered by patents now owned by the foundation. The foundation had previously filed claims against manufacturers of bar code scanners in U.S. District Court for the District of Nevada alleging patent infringement. The manufacturers of bar code scanners prevailed on most points in litigation in the Nevada action relating to the validity of the patents at issue. However, Lemelson has appealed to the U.S. Court of Appeals for the Ninth Circuit. The defendants in the Arizona litigation have requested the U.S. District Court to stay the proceedings pending the outcome of the Nevada litigation, which the Court granted. Until the Nevada patent litigation is resolved, we will expend little, if any, legal fees in the Arizona case. If the bar code manufacturers are successful in the Nevada case, we expect the Arizona court to dismiss the action against us.

The foundation has not specified the amount of damages it seeks in its complaint, but such damages may be material. If the foundation ultimately prevails in the Arizona litigation, the damages assessed against us may be material and may have a material adverse effect on our financial condition. In addition, we may be required to modify the methods by which we track inventories and ship products that may have a material adverse effect on our results of operations. We intend to vigorously defend this claim and, to the extent we are found liable, we believe we have indemnification claims against certain manufacturers of bar code scanners.

While we may ultimately decide to seek indemnity from certain manufacturers of bar code scanners, we can provide no assurance that we would be successful in obtaining such indemnity. At a minimum, if the Nevada or Arizona litigation proceeds, we may incur material legal fees in the defense of the foundation's claims or in seeking indemnity from certain manufacturers of bar code scanners.

On October 7, 2003, Commissariat A L'Energie Atomique filed a complaint in the U.S. District Court for the District of Delaware, naming us as a defendant, along with several other computer-related resellers, in a patent infringement case. We are attempting under contract provision and the Uniform Commercial Code to be defended and indemnified by the manufacturers of the allegedly infringing products. In the event that the manufacturers do not agree to indemnify us, we may have to expend some defense costs and we may be liable for some amount of damages. No specific amount has been claimed as damages.

We are subject to various legal proceedings and claims which have arisen during the ordinary course of business. In the opinion of management, the outcome of such matters is not expected to have a material effect on our financial position, results of operations, and cash flows.

### **Item 4. Submission of Matters to a Vote of Security Holders**

There were no matters submitted during the fourth quarter of 2005 to a vote of security holders.

### **Executive Officers of PC Connection**

The executive officers of PC Connection and their ages as of March 17, 2006 are as follows:

<u>Name</u>	<u>Age</u>	<u>Position</u>
Patricia Gallup	51	Chairman, President, and Chief Executive Officer
Robert F. Wilkins	44	Executive Vice President
Peter J. Cannone	40	Senior Vice President, Sales Subsidiaries
Jack L. Ferguson	67	Vice President, Treasurer and Chief Financial Officer
Bradley G. Mousseau	54	Vice President, Human Resources

## [Table of Contents](#)

**Patricia Gallup** is a co-founder of PC Connection and has served as Chief Executive Officer and Chairman of the Board since September 2002. Ms. Gallup also assumed the role of President of PC Connection upon the resignation of its former president on March 21, 2003. Ms. Gallup served as Chairman from June 2001 to August 2002. Ms. Gallup has served as a member of our executive management team since its inception in 1982.

**Robert F. Wilkins** has served as Executive Vice President of PC Connection since January 2000. Mr. Wilkins served as President of PC Connection Sales Corporation from January 2000 to December 2001. Mr. Wilkins served as Senior Vice President of Sales and Marketing from January 1999 to January 2000 and Senior Vice President of Merchandising and Product Management from January 1998 to January 1999. From December 1995 to January 1998, Mr. Wilkins served as Vice President of Merchandising and Product Management. On March 30, 2006, Mr. Wilkins resigned from the Company.

**Peter J. Cannone** has served as Senior Vice President, Sales Subsidiaries since August 2005. Mr. Cannone served as President of our subsidiary, PC Connection Sales Corporation, from January 2004 to August 2005 and served as Vice President of PC Connection Sales Corporation from April 2003 to January 2004. Mr. Cannone served as President of AAI Distribution from February 2002 to November 2002. Mr. Cannone served as Vice President of PC Connection Sales Corporation from August 1999 to February 2002.

**Jack L. Ferguson** has served as Vice President and Chief Financial Officer since December 2005 and as Treasurer since November 1997. Mr. Ferguson served as Interim Chief Financial Officer from October 2004 to December 2005 and as Director of Finance from December 1992 to November 1997. Prior to joining PC Connection, Mr. Ferguson was a partner with Deloitte & Touche LLP.

**Bradley G. Mousseau** has served as Vice President, Human Resources since January 2000. Prior to joining PC Connection, Mr. Mousseau served as Vice President of Global Workforce Strategies for Systems & Computer Technology Corporation (SCT) from April 1997 to January 2000.

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

PC Connection's Common Stock commenced trading on March 3, 1998 on the Nasdaq National Market under the symbol "PCCC." As of March 17, 2006, there were 25,259,261 shares outstanding of our common stock held by approximately 115 stockholders of record and 2,991 beneficial holders.

The following table sets forth for the fiscal periods indicated the range of high and low sales prices for our common stock on the Nasdaq National Market.

<u>2005</u>	<u>High</u>	<u>Low</u>
Quarter Ended:		
December 31	\$ 6.70	\$5.10
September 30	7.19	5.05
June 30	8.60	4.95
March 31	10.17	5.52
<u>2004</u>		
Quarter Ended:		
December 31	\$10.00	\$6.66
September 30	7.74	6.21
June 30	8.64	6.52
March 31	10.90	6.45

We have never declared or paid cash dividends on our capital stock. We anticipate that we will retain all future earnings, if any, to fund the development and growth of our business, and we do not anticipate paying any cash dividends on our Common Stock in the foreseeable future. Our secured credit agreement contains restrictions that may limit our ability to pay dividends in the future.

*Share Repurchase Authorization*

We announced on March 28, 2001, that our Board of Directors authorized the spending of up to \$15.0 million to repurchase our common stock. Share purchases will be made in the open market from time to time depending on market conditions. We have repurchased an aggregate of 362,267 shares for \$2.3 million as of December 31, 2005, which are reflected as treasury stock on the consolidated balance sheet. Our current bank line of credit dated June 29, 2005, however, limits additional repurchases to \$10 million without bank approval of higher amounts. We did not repurchase any shares of our common stock in the year ended December 31, 2005.

[Table of Contents](#)

**Item 6. Selected Financial Data**

The following selected financial and operating data should be read in conjunction with the Company's Consolidated Financial Statements and the Notes thereto, and "Management's Discussion and Analysis of Financial Condition and Results of Operations" and other financial information included elsewhere in this Form 10-K.

	Years Ended December 31,				
	2005	2004	2003	2002	2001
	(dollars in thousands, except per share and selected operating data)				
<b>Statement of Operations Data:</b>					
Net sales	\$ 1,444,297	\$ 1,353,834	\$ 1,312,891	\$ 1,191,497	\$ 1,186,217
Cost of sales	1,280,701	1,201,780	1,175,212	1,062,311	1,054,631
Gross profit	163,596	152,054	137,679	129,186	131,586
Selling, general, and administrative expenses	151,981	132,729	124,824	121,964	117,610
Special charges <sup>(1)</sup>	2,127	5,232	1,929	1,636	2,204
Income from operations	9,488	14,093	10,926	5,586	11,772
Interest expense	(1,447)	(1,385)	(1,305)	(1,152)	(1,179)
Other, net	89	152	117	513	1,307
Income before income taxes	8,130	12,860	9,738	4,947	11,900
Income tax provision	(3,683)	(4,556)	(3,850)	(1,700)	(4,521)
Net income	\$ 4,447	\$ 8,304	\$ 5,888	\$ 3,247	\$ 7,379
Basic net income per share	\$ .18	\$ .33	\$ .24	\$ .13	\$ .30
Diluted net income per share	\$ .18	\$ .33	\$ .23	\$ .13	\$ .30
<b>Selected Operating Data:</b>					
Catalogs distributed	27,467,000	31,125,000	31,525,000	28,765,000	41,683,000
Orders entered <sup>(2)</sup>	1,439,000	1,281,000	1,333,000	1,243,000	1,265,000
Average order size <sup>(2)</sup>	\$ 1,166	\$ 1,230	\$ 1,169	\$ 1,119	\$ 1,116
<b>Balance Sheet Data:</b>					
Working capital	\$ 100,893	\$ 103,637	\$ 96,883	\$ 91,289	\$ 120,442
Total assets	337,705	286,542	310,605	268,682	243,645
Short-term debt:					
Current maturities of capital lease obligations:					
To affiliate	416	373	334	200	171
To third party	412	391	—	—	—
Notes payable	19,975	4,810	5,614	—	1,000
Long-term debt:					
Capital lease obligations, less current maturities:					
To affiliate	5,299	5,715	6,088	6,421	6,621
To third party	396	841	—	—	—
Total stockholders' equity	171,399	166,158	157,189	150,144	146,762

<sup>(1)</sup> Our 2005 special charges consist of \$1,071 for the cost of workforce reductions and \$1,056 incurred related to the temporary retention of certain Amherst employees and facilities subsequent to the purchase of certain assets of Amherst Technologies. Our 2004 special charges consist of \$860 for the cost of workforce reductions, \$101 for the remaining uninsured portion of a 2003 employee defalcation, \$3,559 related to our review of the 2003 General Services Administration ("GSA") contract cancellation and costs related to securing a new schedule, \$512 in professional fees related to a review of certain prior year rebate-related transactions, and \$200 related to a proposed litigation settlement. Our 2003 special charges consist of \$407 for the cost of workforce reductions, \$1,130 for an uninsured portion of an employee defalcation, and \$392 for an internal review of GovConnection's GSA contract cancellation. Our 2002 special charges consist of \$886 for the cost of workforce reductions and \$750 for costs relating to the Microsoft settlement. Our 2001 special charges consist of \$1,510 for the cost of workforce reductions and \$694 for costs relating to a proposed acquisition that was abandoned.

<sup>(2)</sup> Does not reflect cancellations or returns.

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

*Our management’s discussion and analysis of our financial condition and results of operations include the identification of certain trends and other statements that may predict or anticipate future business or financial results that are subject to important factors that could cause our actual results to differ materially from those indicated. See “Factors That May Affect Future Results and Financial Condition.”*

**OVERVIEW**

PC Connection is a national direct marketer of a wide range of IT products and services—including computer systems, software and peripheral equipment, networking communications, and other products, and accessories that we purchase from manufacturers, distributors, and other suppliers. We also offer a growing range of repair, configuration, installation, and other services performed by our personnel and third-party providers. We operate through three primary business segments: (a) consumers and small- to medium-sized businesses, or SMBs, through our PC Connection Sales subsidiaries, (b) large corporate accounts, or Large Account, through our MoreDirect subsidiary, and (c) federal, state, and local government and educational institutions, or Public Sector, through our GovConnection subsidiary.

We generate sales through (i) outbound telemarketing and field sales contacts by account managers focused on the business, education, and government markets, (ii) our Web sites, and (iii) inbound calls from customers responding to our catalogs and other advertising media.

The primary challenges we face in effectively managing our business are (1) increasing our revenues while improving our gross profit margins in all three business segments, (2) recruiting, retaining, and improving the productivity of our sales personnel, and (3) effectively managing and leveraging our selling, general, and administrative (“SG&A”) expenses over a higher sales base. With only moderate growth projected in the overall IT industry, any significant sales growth for us must come through increased market share. Competition is expected to be even more intense in the future, which could put more pressure on margins.

We enjoyed a modest improvement in sales productivity (average annualized sales per sales representative) in 2005 compared to the prior year and have made significant investments in our sales training programs and information systems in anticipation of further productivity gains in the latter half of 2006. We also launched in the fourth quarter of 2005 our “Core 1” sales training program with the goal of improving sales representatives’ retention and productivity. Increasing our sales representatives’ productivity will remain a key corporate challenge for the upcoming year. We also invested in our services business in 2005 in anticipation of migrating our business from a product-centered to solution-oriented model.

As previously reported, the General Services Administration, or GSA, cancelled its contract with GovConnection in November 2003, following its review of that subsidiary’s contract management system and procedures and the possibility of the sale of unqualified items and underpayment of required fees. Although we were awarded a new GSA contract in August 2004, we have experienced significant declines in our 2004 and 2005 federal government sales from 2003 levels. Our federal government revenues may continue to be negatively impacted as GovConnection seeks to regain sales under the new GSA contract. This matter is further discussed in the section entitled “Factors That May Affect Future Results and Financial Condition” in Item 1A of Part I of this Annual Report on Form 10-K.

**RESULTS OF OPERATIONS**

The following table sets forth for the periods indicated information derived from our statements of income expressed as a percentage of net sales.

	Years Ended December 31,		
	2005	2004	2003
Net sales (in millions)	<u>\$1,444.3</u>	<u>\$1,353.8</u>	<u>\$1,312.9</u>
Net sales	100.0%	100.0%	100.0%
Gross profit	11.3	11.2	10.5
Selling, general, and administrative expenses	10.5	9.8	9.5
Special charges	0.1	0.4	0.2
Income from operations	0.7	1.0	0.8

Our overall increase in 2005 net sales resulted from year-over-year sales growth achieved in all three business segments. The year-over-year increases in our gross margin and SG&A expenses as a percentage of net sales are attributable largely to the inclusion of additional vendor consideration amounts as reductions to cost of sales. Most product manufacturers provide us with co-op advertising support in exchange for product coverage in our catalogs as well as other advertising promotions. As noted in our Annual Report on Form 10-K for the year ended December 31, 2004, we revised our estimates in the third quarter of 2004 relating to vendor consideration as a result of Emerging Issues Task Force Issue No. 02-16, "Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor" ("EITF 02-16"). This pronouncement requires that such consideration be recorded as a reduction of cost of sales unless the consideration represents reimbursement for costs incurred for a specific advertising program funded by an individual vendor. In the years ended December 31, 2005 and 2004, we recorded \$14.5 million and \$5.4 million, respectively, of additional advertising reimbursements in excess of advertising costs incurred as reductions to cost of sales and inventory. We recorded \$14.3 million and \$4.9 million of these respective amounts as offsets to cost of sales, and the respective balances reduced inventory. Such excess advertising reimbursements had previously been recorded as offsets to SG&A expense. This 2004 revision resulted in increases, on a consolidated basis, of 1.0% and 0.4% in both gross margin and SG&A expenses as a percentage of net sales for 2005 and 2004, respectively. SG&A expenses also increased as a result of increased investments in 2005 related to our improvements to our sales systems and our service-related business. As a result of these investments, we expect to see increases in both retention and productivity in our sales representatives in the latter half of 2006.

## [Table of Contents](#)

### **Sales Distribution**

The following table sets forth our percentage of net sales by business segment, sales channel, and product mix:

Business Segment	Years Ended December 31,		
	2005	2004	2003
SMB	58%	59%	57%
Large Account	24	22	19
Public Sector	18	19	24
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>
Sales Channel			
Outbound Telemarketing and Field Sales	69%	74%	77%
Online Internet	26	20	16
Inbound Telesales	5	6	7
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>
Product Mix			
Notebooks and PDAs	18%	21%	20%
Desktop/Servers	14	14	15
Storage Devices	9	8	9
Software	12	12	11
Net/Com Products	8	7	8
Printers and Printer Supplies	11	11	11
Video, Imaging, and Sound	12	12	12
Memory and System Enhancements	5	5	5
Accessories/Other	11	10	9
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>

### **Gross Profit Margins**

The following table summarizes our overall gross profit margins, as a percentage of net sales, for the last three years:

Segment	Years Ended December 31,		
	2005	2004	2003
SMB	12.4%	12.2%	11.2%
Large Account	10.0	10.2	11.3
Public Sector	9.6	9.4	8.2
Total	11.3%	11.2%	10.5%

Consolidated gross margin increased modestly year over year in 2005 due to the gross margin gain realized in our SMB and Public Sector segments, as the Large Account segment experienced a slight year-over-year gross margin decline. Our increase in gross margin rate for the year ended December 31, 2005 was primarily the result of our revised estimates relating to EITF 02-16, as discussed previously. Specifically, on a segment basis for the year ended December 31, 2005, our revised estimates relating to EITF 02-16 resulted in increases of 1.4% and 1.1%, respectively, in our SMB and Public Sector gross margin rates. We continue to focus on improving product margins by increasing add-on sales of accessories and other companion products to system sales and by increasing sales of third-party warranty, installation, and other services. Excluding the effect of EITF 02-16, gross margins decreased in 2005 primarily as the result of increased competitive pressures, as described more fully below.



## [Table of Contents](#)

We continue to focus on generating more gross profit dollars per transaction and on increasing gross margin. Our efforts to preserve and improve product margins include:

- Increasing our higher-margin sales of third-party warranty, installation, and other services;
- Maximizing higher-valued vendor incentive programs; and
- Increasing sales productivity.

Gross margin on sales to corporate accounts that purchase at volume discounts is generally lower than gross margins on consumer or smaller business sales. Gross margin on sales to Public Sector customers has historically been lower than that for commercial sales. However, the gross profit dollar contribution per Public Sector and Large Account order is generally higher as average order sizes are usually larger. We believe that sales to Large Account and Public Sector customers will continue to represent a growing portion of our business mix in future periods. We also expect the increasing migration of customers to our web sites to continue the increase in the percentage of online Internet sales, which generally have higher margins.

Gross margins also vary by product mix. Sales of notebooks and PDAs accounted for 18% of our overall sales in 2005, a decrease from 21% in 2004. The decrease in these two product lines served to increase our overall gross margin rates. Sales of computer systems (including desktops, servers, and notebooks) result in a relatively high dollar sales order and generally provide the largest gross profit dollar contribution per order of all our products. However they usually yield the lowest gross margin percentage.

### **Cost of Sales and Certain Other Costs**

Cost of sales includes the invoice cost of the product, packaging, inbound and outbound freight, and provisions for inventory obsolescence, adjusted for discounts, rebates, and other vendor consideration adjustments, including those pursuant to EITF 02-16. Direct operating expenses relating to our purchasing function and receiving, inspection, internal transfer, warehousing, packing and shipping, and other expenses of our distribution center are included in selling, general, and administrative expenses. Accordingly, our gross margins may not be comparable to those of other entities who include all of the costs related to their distribution network in cost of goods sold. Such costs, as a percentage of net sales for the years reported, are as follows:

	Years Ended December 31,		
	2005	2004	2003
	0.62%	0.64%	0.69%

### **Operating Expenses**

The following table breaks out our more significant operating expenses for the last three years (in millions of dollars):

	Years Ended December 31,		
	2005	2004	2003
Personnel costs	\$100.6	\$ 93.5	\$ 89.7
Advertising, net	11.4	0.9	(4.4)
Facilities operations	8.4	9.3	9.4
Credit card fees	7.8	7.4	7.6
Depreciation and amortization	7.2	7.1	8.4
Bad debts	2.7	2.4	3.1
Other—net	13.9	12.1	11.0
Total	<u>\$152.0</u>	<u>\$132.7</u>	<u>\$124.8</u>
Percentage of net sales	<u>10.5%</u>	<u>9.8%</u>	<u>9.5%</u>

## [Table of Contents](#)

We have concentrated our efforts on managing our overall operating costs. While we plan to continue our focus on controlling discretionary expenditures, we expect that our SG&A expense may vary depending on changes in sales volume, as well as the levels of continued investments in key growth initiatives such as enhancing our sales training, improving marketing programs, and deploying next generation technology to support the sales organization.

Personnel costs continue to represent the majority of our operating expenses, with sales personnel representing the largest portion of these costs. Our other operating costs, except for credit card fees and bad debts, tend to be relatively fixed over changing sales levels. Total operating expenses increased year over year in 2005 partly as a result of investments in our sales systems and our service-related business; these included incremental expenditures related to training, customer acquisition programs, and other marketing initiatives.

Most product manufacturers provide us with co-op advertising support in exchange for product coverage in our catalogs as well as other advertising promotions. EITF 02-16, which addresses the income classification of vendor consideration, became effective for the periods beginning January 1, 2003. This pronouncement requires that such consideration be recorded as a reduction of cost of sales unless the consideration represents reimbursement for costs incurred for a specific advertising program funded by an individual vendor. For the years ended December 31, 2005, 2004, and 2003, we recorded advertising expense of \$23.2 million, \$22.5 million, and \$22.8 million, respectively. For the years ended December 31, 2005, 2004, and 2003, we received total vendor advertising funding of \$28.6 million, \$29.1 million, and \$29.4 million, respectively. We recorded \$16.7 million, \$7.5 million, and \$2.2 million of these reimbursements as reductions to cost of sales and inventory in 2005, 2004, and 2003, respectively. As discussed earlier, we revised our estimates used to determine excess vendor advertising in 2004, and accordingly, \$14.5 million and \$5.4 million of the respective 2005 and 2004 amounts referred to above relates to this revision in our estimates. Our net advertising expense was accordingly higher in those two years. Although the level of vendor co-op advertising support available to us from certain manufacturers has declined, and may decline further in the future, the overall level of co-op advertising support has remained consistent with our levels of spending for catalog and other advertising programs. We believe that the overall levels of co-op advertising support available over the next twelve months will be consistent with our planned advertising programs.

**YEAR-OVER-YEAR COMPARISONS**

*Year Ended December 31, 2005 Compared to Year Ended December 31, 2004*

Net sales increased 6.7% to \$1,444.3 million in 2005 from \$1,353.8 million in 2004 as we experienced increases in all three business segments. Changes in net sales and gross profit by business segment are shown in the following table (dollars in millions):

	Years Ended December 31,				% Change
	2005		2004		
	Amount	% of Net Sales	Amount	% of Net Sales	
<b>Sales:</b>					
SMB	\$ 834.6	57.8%	\$ 802.3	59.3%	4.0%
Large Account	347.5	24.1	298.5	22.0	16.4
Public Sector	262.2	18.1	253.0	18.7	3.6
Total	<u>\$1,444.3</u>	<u>100.0%</u>	<u>\$1,353.8</u>	<u>100.0%</u>	6.7%
<b>Gross Profit:</b>					
SMB	\$ 103.7	12.4%	\$ 98.0	12.2%	5.8%
Large Account	34.6	10.0	30.3	10.2	14.2
Public Sector	25.3	9.6	23.8	9.4	6.3
Total	<u>\$ 163.6</u>	<u>11.3%</u>	<u>\$ 152.1</u>	<u>11.2%</u>	7.6%

- Net sales for our SMB segment increased due to a modest increase in the number of sales representatives employed in 2005 while maintaining sales productivity. Sales representatives for the SMB segment totaled 411 at December 31, 2005, up from 405 at December 31, 2004. Net sales for our SMB segment also increased due the implementation of customer acquisition initiatives, including increased Internet advertising, which contributed to our 25% year-over-year increase in SMB Internet sales in 2005.
- Net sales for our Large Account segment increased due to an improvement in average sales productivity per account manager and as a result of our acquisition in October 2005 of certain assets of Amherst Technologies LLC, or the Amherst Transaction. Our fourth quarter sales of 2005 included \$25 million of revenues generated by former Amherst sales representatives who joined this segment. Sales representatives for the Large Account segment totaled 100 at December 31, 2005, up from 69 at the end of 2004. This segment's productivity increase resulted from increased penetration of our existing customer base, as well as the addition of new accounts.
- Net sales for our Public Sector segment increased due to a 6.2% year-over-year increase in our federal government revenues, as our sales to state and local government units and educational organizations were level year over year. During the year ended December 31, 2005, we added several new vendors to our GSA contract, which was awarded in the third quarter of 2004 and therefore not in effect for most of the prior year. Sales representatives for our Public Sector segment totaled 107 at December 31, 2005 and 2004.

Gross profit increased in all three business segments as shown by the above, whereas the gross margin percentage of net sales improved for our SMB and Public Sector segments.

- Gross profit for our SMB segment increased primarily due to a refinement of estimates, made in the third quarter of 2004, pursuant to EITF 02-16, which required the transfer of additional vendor consideration from SG&A to cost of sales. For the year ended December 31, 2005, we recorded \$11.4 million of additional vendor consideration as a reduction to cost of sales, compared to \$4.7 million in 2004. These offsets resulted in gross margin increases of 1.4% and 0.6% of net sales for 2005 and 2004, respectively. Gross margins were otherwise negatively impacted by increased shipping costs and tighter competitive pricing pressures, which partly offset the increased vendor consideration.

## [Table of Contents](#)

- Gross profit for our Large Account segment increased due to an increase in sales as explained above. Gross margin rates decreased modestly in this highly competitive large enterprise segment. We targeted a select group of high-value customers in the latter half of 2005, which partly accounted for the sales increase but also adversely impacted gross margin rates.
- Gross profit for our Public Sector segment increased in both dollars and as a percentage of sales due primarily to our recording additional vendor consideration, pursuant to EITF 02-16, as a reduction to cost of sales in 2005 compared to the prior year. For the year ended December 31, 2005, we recorded \$2.9 million of additional vendor consideration as a reduction to cost of sales, compared to \$0.2 million in 2004. These offsets resulted in gross margin increases of 1.1% and 0.1% of net sales for 2005 and 2004, respectively. Similar to SMB, increased shipping costs and tighter competitive pricing pressures negatively impacted this segment's gross margin rates.

*Selling, general, and administrative expenses* increased in both dollars and as a percentage of sales in 2005 from 2004.

SG&A expenses attributable to our operating segments are summarized below (dollars in millions):

	Years Ended December 31,				% Change
	2005		2004		
	Amount	% of Net Sales	Amount	% of Net Sales	
SMB	\$ 98.8	11.8%	\$ 85.3	10.6%	15.8%
Large Account	17.9	5.2	15.5	5.2	15.5
Public Sector	35.3	13.5	31.9	12.6	10.7
Total	<u>\$152.0</u>	10.5%	<u>\$132.7</u>	9.8%	14.5%

- SG&A expenses for our SMB segment increased year over year, and were higher as a percentage of net sales in 2005 compared to 2004, primarily due to an increase in net advertising expense. Net advertising expense increased as a result of the previously discussed change in estimates for vendor consideration as well as increased Internet advertising costs. Our investments in making our sales support systems more responsive and flexible also contributed to this segment's SG&A expenses.
- SG&A expenses for our Large Account segment increased year over year, but remained flat as a percentage of net sales in 2005 compared to the prior year. The dollar increase resulted partly from the additional sales representatives added from our Amherst Transaction. SG&A expenses for this segment represent the lowest of the three segments as a percentage of net sales, reflecting the nature and efficiency of this segment's variable cost field sales and drop-shipping operating model.
- SG&A expenses for our Public Sector segment increased year over year, and were higher as a percentage of net sales in 2005 compared to 2004. Net advertising expense increased as a result of the previously discussed change in estimates for vendor consideration. This segment's SG&A expenses as a percentage of net sales also continue to be higher than its historical trend due to our retention of experienced federal sales personnel while we continue to rebuild our federal business. (See "*Factors That May Affect Future Results and Financial Condition*" for further discussion of this topic.) Our investments in making our sales support systems more responsive and flexible also contributed to this segment's SG&A expenses.

## [Table of Contents](#)

*Special charges* totaled \$2.1 million and \$5.2 million for the years ended December 31, 2005 and 2004, respectively. A roll forward of special charges for the two years ended December 31, 2005 is shown below (in thousands of dollars). There were no significant changes in estimates in any of the periods presented.

	<u>Workforce Reductions</u>	<u>Amherst Transaction</u>	<u>Employee Defalcation</u>	<u>GSA Review</u>	<u>Other</u>	<u>Total</u>
Balance December 31, 2003	\$ 113	\$ —	\$ —	\$ 237	\$ —	\$ 350
Charges	860	—	101	3,559	712	5,232
Cash payments	(724)	—	(101)	(3,072)	(497)	(4,394)
Balance December 31, 2004	249	—	—	724	215	1,188
Charges	1,071	1,056	—	—	—	2,127
Cash payments	(454)	(924)	—	(724)	(200)	(2,302)
Adjustments	—	—	—	—	(15)	(15)
Balance December 31, 2005	<u>\$ 866</u>	<u>\$ 132</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 998</u>

The 2005 Amherst Transaction charges relate primarily to the temporary retention of certain Amherst employees and facilities while we integrated this business. The 2004 charges for the employee defalcation represent the loss sustained by one of our commercial subsidiaries in excess of the amount covered by insurance. The 2004 charges for the GSA contract review represent costs of our review relating to the cancellation by the GSA in late 2003 of its contract with our subsidiary, GovConnection, and costs related to securing a new GSA schedule, which was awarded in August 2004. The other charges in 2004 include \$200 accrued as an estimated liability in a patent infringement case, which we settled in 2005, and \$512 in professional fees relating to our review of certain calendar year 2000 and 2003 transactions.

*Income from operations* decreased by \$4.6 million to \$9.5 million for the year ended December 31, 2005 from \$14.1 million compared to 2004. MoreDirect, our Large Account segment, accounted for \$16.8 million and \$14.6 million of our income from operations in 2005 and 2004, respectively. Excluding MoreDirect, we incurred a loss from operations of \$7.3 million for 2005 and \$0.5 million for 2004, primarily as the result of the losses incurred in our Public Sector segment and the lower gross margin in our SMB segment, after excluding the effect of EITF 02-16.

Income from operations as a percentage of net sales decreased from 1.0% in 2004 to 0.7% in 2005. This decrease was attributable to the changes in net sales, gross margin, and SG&A expenses as discussed above.

*Interest expense* was \$1.4 million in both 2005 and 2004. Interest expense was unchanged in 2005 as higher interest rates in 2005 were offset by lower borrowings as compared to 2004.

Our effective tax rate was 45.3% for 2005 and 35.4% for 2004. This year-over-year increase was due primarily to the tax benefits of state tax loss carryforwards in certain jurisdictions not recognizable as offsets to state tax charges in other jurisdictions, and to certain non-deductible expenses. We anticipate that our effective tax rate will be approximately 39% in 2006 due to anticipated changes in mix of state income taxes to which we are subject.

*Net income* decreased by \$3.9 million to \$4.4 million in 2005 from \$8.3 million in 2004, principally as a result of the decrease in income from operations.

[Table of Contents](#)

**Year Ended December 31, 2004 Compared to Year Ended December 31, 2003**

Net sales increased 3.1% to \$1,353.8 million in 2004 from \$1,312.9 million in 2003. Our SMB and Large Account segments both increased, offsetting the decrease in our Public Sector's sales. Changes in net sales and gross profit by business segment are shown in the following table (dollars in millions):

	Years Ended December 31,				% Change
	2004		2003		
	Amount	% of Net Sales	Amount	% of Net Sales	
<b>Sales:</b>					
SMB	\$ 802.3	59.3%	\$ 744.4	56.7%	7.8%
Large Account	298.5	22.0	247.9	18.9	20.4
Public Sector	253.0	18.7	320.6	24.4	(21.1)
Total	<u>\$1,353.8</u>	<u>100.0%</u>	<u>\$1,312.9</u>	<u>100.0%</u>	3.1%
<b>Gross Profit:</b>					
SMB	\$ 98.0	12.2%	\$ 83.4	11.2%	17.5%
Large Account	30.3	10.2	28.0	11.3	8.2
Public Sector	23.8	9.4	26.3	8.2	(9.5)
Total	<u>\$ 152.1</u>	<u>11.2%</u>	<u>\$ 137.7</u>	<u>10.5%</u>	10.5%

- Net sales for our SMB segment increased due to the increase in the number of sales account managers employed in 2004 while maintaining sales productivity. Sales representatives for the SMB segment totaled 405 at December 31, 2004, up from 378 at December 31, 2003. Sales productivity was flat in 2004 compared to 2003 because we implemented company-wide gross margin improvement initiatives in early 2004. As discussed below, these initiatives inhibited our sales growth as we refrained from low-margin sales but resulted in improved over-all operating margins.
- Net sales for our Large Account segment increased due to an improvement in average sales productivity per account manager. IT spending grew at a faster pace for our large Fortune 1000 customers than those of our other two business segments. Sales account managers for the Large Account segment totaled 69 at December 31, 2004, down from 85 at the end of 2003. This reduction in headcount resulted from a planned reduction in under-performing sales representatives.
- Net sales for our Public Sector segment decreased due primarily to a 58.5% decrease in sales to the federal government. Our federal government sales decreased from the prior year due to the late 2003 cancellation of our GSA contract described previously. Although we were issued a new GSA contract in August 2004, it was too late into the federal buying season to recover this business. However, sales to state and local governmental and educational institutions ("SLED") increased 14.7% due to improvement in average sales productivity per account manager. Sales account managers for the Public Sector segment totaled 107 at December 31, 2004, up from 104 at December 31, 2003. The headcount mix between our federal and SLED account managers was unchanged from year to year due to our investment decision to maintain our federal account managers despite the nine month absence of our GSA contract.

Gross profit increased in our SMB and Large Account areas as shown by the above, whereas the gross margin percentage of net sales improved for our SMB and Public Sector segments.

- Gross profit for the SMB segment improved due to increases in both net sales and gross margin rate. We were able to improve gross margin rates by increasing add-on sales of accessories and other companion products to our system sales, as well increasing sales of third-party warranty, installation, and other services. These initiatives were implemented in both our SMB and Public Sector segments in early 2004. Additionally,

## [Table of Contents](#)

as discussed earlier, our revised estimates of advertising reimbursements in excess of costs incurred accounted for 60 basis points of our 1.0% increase in gross margin rate in the SMB segment.

- Gross profit for the Large Account segment increased due to the increase in sales explained earlier, despite a decrease in the gross margin rate. Changes in customer mix and continuing competitive pressures caused gross margin rates to decrease on a year-over-year basis.
- Despite an increase in gross margin rate, gross profit for the Public Sector segment decreased due to the decline in federal sales discussed above. Similar to our SMB segment, we were able to improve margin rates by increasing add-on sales of accessories and other companion products to our system sales, as well as increasing sales of third-party warranty, installation, and other services. As a result of losing its GSA contract in late 2003, the Public Sector increased its agency revenues from sales through third-party GSA schedules in 2004, which contributed to its improved gross margin rate. Revising our estimates used in EITF 02-16 led to an impact of less than 0.1% on this segment's gross margin rate.

*Selling, general, and administrative expenses* increased in both dollars and as a percentage of sales in 2004 from 2003.

We have concentrated our efforts on managing our overall operating costs. Personnel costs generally account for approximately two-thirds of our SG&A expenses, as shown earlier in the table of SG&A expenses. While we plan to continue our focus on controlling discretionary expenditures, we expect that our SG&A expense may vary depending on changes in sales volume, as well as the levels of continued investments in key growth initiatives such as hiring more experienced outbound sales account managers, improving marketing programs, and deploying next generation technology to support the sales organization.

SG&A expenses attributable to our operating segments are summarized below (dollars in millions):

	Year Ended December 31,				
	2004		2003		% Change
	Amount	% of Net Sales	Amount	% of Net Sales	
SMB	\$ 85.3	10.6%	\$ 82.3	11.1%	3.6%
Large Account	15.5	5.2	14.0	5.6	10.7
Public Sector	31.9	12.6	28.5	8.9	11.9
Total	<u>\$ 132.7</u>	9.8%	<u>\$ 124.8</u>	9.5%	6.3%

- SG&A expenses for the SMB segment increased slightly in 2004, while decreasing as a percentage of net sales from 2003. This segment has a relatively fixed cost structure, and the increase in its 2004 net sales resulted in a lower expense rate for this year. As discussed earlier, in 2004 we revised our estimates relating to vendor consideration as a result of EITF 02-16 and reclassified in our SMB segment \$5.4 million of advertising reimbursements in excess of advertising costs from SG&A expense to cost of goods sold and inventory. The resulting net increase in advertising expenses was the primary reason for our increased expense on a dollar basis but was partially offset by decreases in depreciation expense and bad debt expense.
- SG&A expenses for the Large Account segment increased on a dollar basis but decreased as a percentage of net sales. SG&A expenses for this segment represent the lowest of the three segments as a percentage of net sales, reflecting the nature and efficiency of this segment's variable cost field sales and drop-shipping operating model.
- The Public Sector segment's SG&A expenses increased in 2004 but were significantly higher as a percentage of net sales from 2003. The significant decrease in our federal sales described above accounted for the increase in this segment's SG&A expense as a percentage of sales. We retained our experienced sales personnel in anticipation of our new GSA contract, which was awarded in August 2004.

## [Table of Contents](#)

*Special charges* totaled \$5.2 million and \$1.9 million for the years ended December 31, 2004 and 2003, respectively. A roll forward of special charges for the two years ended December 31, 2004 is shown below (in thousands of dollars). There were no changes in estimates in any of the periods presented.

	<u>Workforce Reductions</u>	<u>Employee Defalcation</u>	<u>GSA Review</u>	<u>Other</u>	<u>Total</u>
Balance December 31, 2002	\$ 208	\$ —	\$ —	\$ —	\$ 208
Charges	407	1,130	392	—	1,929
Cash payments	(502)	(1,130)	(155)	—	(1,787)
Balance December 31, 2003	113	—	237	—	350
Charges	860	101	3,559	712	5,232
Cash payments	(724)	(101)	(3,072)	(497)	(4,394)
Balance December 31, 2004	<u>\$ 249</u>	<u>\$ —</u>	<u>\$ 724</u>	<u>\$ 215</u>	<u>\$ 1,188</u>

The charges for the employee defalcation represent the loss sustained by one of our commercial subsidiaries in excess of the amount covered by insurance. The charges for the GSA contract review represent costs of our review relating to the GSA contract cancellation in late 2003 and costs related to securing a new GSA schedule, which was awarded in August 2004. The other charges in 2004 include \$200 accrued as an estimated liability in a patent infringement case currently in litigation and \$512 in professional fees relating to our review of certain calendar year 2000 and 2003 transactions. We concluded our review of these transactions in October 2004.

*Income from operations* increased by \$3.2 million, or 29.4%, to \$14.1 million for the year ended December 31, 2004 from \$10.9 million compared to 2003. MoreDirect, our Large Account segment, accounted for \$14.6 million and \$12.9 million of our income from operations in 2004 and 2003, respectively. Excluding MoreDirect, we incurred a loss from operations of \$0.5 million for 2004 and \$2.0 million in 2003.

Income from operations as a percentage of net sales increased from 0.8% in 2003 to 1.0% in 2004. This increase was attributable to the changes in net sales, gross margin, and SG&A expenses as discussed above.

*Interest expense* was \$1.4 million in 2004 and \$1.3 million in 2003. Interest expense increased due to slightly higher average borrowings outstanding and slightly higher interest rates in 2004 as compared to 2003.

Our effective tax rate was 35.4% for 2004 and 39.5% for 2003. This year-over-year decrease was due to a decrease in our accrual for state tax contingencies in certain states in which we operate.

*Net income* increased by \$2.4 million, or 40.7%, to \$8.3 million in 2004 from \$5.9 million in 2003, principally as a result of the increase in income from operations.

## LIQUIDITY AND CAPITAL RESOURCES

### *Liquidity Overview*

Our primary sources of liquidity have historically been internally generated funds from operations and borrowings under our bank line of credit. We have used those funds to meet our capital requirements, which consist primarily of working capital for operational needs, capital expenditures for computer equipment and software used in our business, and recently the Amherst Transaction.

We believe that funds generated from operations, together with available credit under our bank line of credit and inventory trade credit agreements, will be sufficient to finance our working capital, capital expenditure, and other requirements for at least the next twelve calendar months. We expect our capital needs for 2006 to consist primarily of capital expenditures of \$4.0 to \$5.0 million and payments on capital and operating lease obligations of approximately \$5.0 million. We expect to meet our cash requirements for 2006 through a combination of cash on hand, cash generated from operations and, if necessary, additional borrowings on our bank line of credit, as follows:

- *Cash on Hand.* At December 31, 2005 we had approximately \$9.8 million in unrestricted accounts.



## [Table of Contents](#)

- *Cash Generated from Operations.* We expect to generate cash flows from operations in excess of operating cash needs by generating earnings and balancing net changes in inventories and receivables with compensating changes in payables to generate a positive cash flow. Historically, we have consistently generated positive cash flows from operations.
- *Credit Facilities.* As of December 31, 2005, we had drawn \$20.0 million of our \$50.0 million bank line of credit. This line of credit can be increased, at our option, to \$70.0 million for approved acquisitions or other uses authorized by the bank. Borrowings are, however, limited by certain minimum collateral and earnings requirements, as described more fully below.

Our ability to continue funding our planned growth, both internally and externally, is dependent upon our ability to generate sufficient cash flow from operations or to obtain additional funds through equity or debt financing, or from other sources of financing, as may be required. While at this time we do not anticipate needing any additional sources of financing to fund our operations, if demand for information technology products declines, our cash flows from operations may be substantially affected. See also related risks listed below under “Factors That May Affect Future Results and Financial Condition.”

### **Summary Sources and Uses of Cash**

The following table summarizes our sources and uses of cash over the last three years (in millions):

	Years Ended December 31,		
	2005	2004	2003
Net cash provided by operating activities	\$ 9.6	\$13.3	\$ 3.3
Net cash used for investing activities	(21.7)	(8.9)	(8.3)
Net cash provided by (used for) financing activities	15.0	(0.5)	6.2
Increase in cash and cash equivalents	<u>\$ 2.9</u>	<u>\$ 3.9</u>	<u>\$ 1.2</u>

*Cash provided by operating activities* decreased in 2005 but increased in 2004. The primary reasons for the decrease in 2005 were a decrease in net earnings before depreciation and an increase in receivables, partially offset by an increase in payables. The increase in 2004 resulted primarily from an increase in net earnings before depreciation and a decrease in receivables, partially offset by a decrease in payables.

At December 31, 2005, we had \$114.4 million in outstanding accounts payable. Such accounts are generally paid within 30 days of incurrence and will be financed by cash flows from operations or short-term borrowings under the line of credit. This amount includes \$12.3 million payable to two financial institutions under inventory trade credit agreements we use to finance our purchase of certain inventory, secured by the inventory so financed. We believe we will be able to meet our obligations under our accounts payable with cash flows from operations and our existing line of credit.

*Cash used for investing activities* increased significantly in 2005. These activities include our capital expenditures in the three years presented, primarily for computer equipment and capitalization of internally-developed software. Our 2002 acquisition of MoreDirect required earn-out payments due to the former shareholder of MoreDirect. These payments totaled \$6.9 million, \$11.1 million, and \$10.8 million in 2005, 2004 and 2003, respectively. Additionally, in October 2005 we consummated the Amherst Transaction, which accounted for \$7.8 million of the use of cash in 2005.

*Cash provided by financing activities* in 2005 related to an increase in our net borrowings of \$15.2 million under our bank line of credit, whereas there was a decrease in our net borrowings by \$0.8 million in 2004. Our 2003 financing activities consisted primarily of an increase in net borrowings of \$5.6 million.

**Debt Instruments, Contractual Agreements, and Related Covenants**

Below is a summary of certain provisions of our credit facilities and other contractual obligations. It is qualified in its entirety by the terms of the actual agreements, which are on file with the Securities and Exchange Commission. For more information about the restrictive covenants in our debt instruments and inventory financing agreements, see “Factors Affecting Sources of Liquidity.” For more information about our obligations, commitments, and contingencies, see our consolidated financial statements and the accompanying notes included in this annual report.

**Bank Line of Credit.** We secured from our current bank an increased line of credit in June 2005 to provide us with a borrowing capacity of up to \$50.0 million. In addition, we have the option to increase the facility an additional \$20.0 million, based on sufficient levels of trade receivables to meet borrowing base requirements, and depending on meeting minimum EBITDA (earnings before interest, taxes, depreciation, and amortization) and equity requirements, described below under “Factors Affecting Sources of Liquidity.” Amounts outstanding under this facility were \$20.0 million at December 31, 2005. Approximately \$17.0 million of this amount bear interest at Eurodollar Rates (\$10.0 million at 5.11% and \$7.0 million at 5.36%). The balance bears interest at the prime rate (7.25% at December 31, 2005). Substantially all of our assets are collateralized as security for this facility, and all of our subsidiaries are guarantors under the line of credit. Borrowing availability under the line was \$30.0 million at December 31, 2005.

This facility, which matures in June 2008, operates under an automatic cash management program whereby disbursements in excess of available cash are added as borrowings at the time disbursement checks clear the bank, and available cash receipts are first applied against any outstanding borrowings and then invested in short-term qualified cash investments. Accordingly, borrowings under the line are classified as current.

**Inventory Trade Credit Agreements.** We have security agreements with two financial institutions to facilitate the purchase of inventory from various suppliers under certain terms and conditions. These agreements allow a collateralized first position in certain branded products inventory financed by these financial institutions. Although the agreements provide for up to 100% financing on the purchase price, up to an aggregate of \$45.0 million, any outstanding financing must be fully secured by available inventory. We do not pay any interest or discount fees on such inventory financing; such costs are borne by the suppliers as an incentive for us to purchase their products. Amounts outstanding under such facilities, equal to \$12.3 million as of December 31, 2005, are recorded in accounts payable, and the inventory financed is classified as inventory on the consolidated balance sheet.

**Contractual Obligations.** The following table sets forth information with respect to our long-term obligations payable in cash as of December 31, 2005 (in thousands):

	Payments Due By Period				
	Total	Less Than 1 Year	1 – 3 Years	3 – 5 Years	More Than 5 Years
<b>Contractual Obligations:</b>					
Capital lease obligations <sup>(1)</sup>	\$ 9,533	\$ 1,467	\$2,464	\$2,279	\$ 3,323
Operating lease obligations	7,742	3,172	3,551	1,019	—
Total	<u>\$17,275</u>	<u>\$ 4,639</u>	<u>\$6,015</u>	<u>\$3,298</u>	<u>\$ 3,323</u>

<sup>(1)</sup> Including interest, excluding taxes, insurance, and common area maintenance charges.

We do not have any other off-balance sheet arrangements that have or are reasonably likely to have, a current or future material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources.

**Capital Leases.** We have a 15-year lease for our corporate headquarters with an affiliated company related through common ownership. We also have a three-year lease for certain computer equipment with an unrelated

## [Table of Contents](#)

party. We are required to make lease payments aggregating from \$1.0 million to \$1.5 million per year. In addition to the rent payable under the facility lease, we are required to pay real estate taxes, insurance, and common area maintenance charges.

*Operating Leases.* We also lease facilities from our principal stockholders and facilities and equipment from third parties under non-cancelable operating leases. See “Contractual Obligations” above for lease commitments under these leases.

*Earn-out Provisions of MoreDirect Merger Agreement.* We completed the acquisition of MoreDirect in April 2002. Under the terms of this agreement, we were required to make additional payments to the MoreDirect shareholder if certain earnings levels were achieved through December 31, 2004. Earn-out payments aggregating \$6.9 million, \$11.1 million, and \$10.8 million were made in 2005, 2004, and 2003, respectively, based on MoreDirect’s 2004, 2003, and 2002 earnings, respectively.

### **Factors Affecting Sources of Liquidity**

*Internally Generated Funds.* The key factors affecting our internally generated funds are our ability to minimize costs and fully achieve our operating efficiencies, timely collection of our customer receivables, and management of our inventory levels.

*Bank Line of Credit.* Our credit facility contains certain financial ratios and operational covenants and other restrictions (including restrictions on additional debt, guarantees, stock repurchases, dividends and other distributions, investments, and liens) with which the Company and all of its subsidiaries must comply. Any failure to comply with these covenants would not only prevent us from borrowing additional funds under this line of credit, but would also constitute a default. This credit facility contains two financial tests:

- The funded debt ratio (defined as the average outstanding advances under the line for the quarter, divided by the consolidated EBITDA for the four quarters) must not be more than 2.0 to 1.0. Our actual funded debt ratio at December 31, 2005 was 1.2 to 1.0.
- Minimum Consolidated Net Worth must be at least \$150.0 million, plus 50% of consolidated net income for each quarter, beginning with the quarter ending March 31, 2006 (loss quarters not counted). Our actual consolidated stockholders’ equity at December 31, 2005 was \$171.4 million.

The borrowing base under this facility is set at 80% of qualified commercial receivables, plus 50% of qualified government receivables, less \$5 million of the formula availability which must be held in reserves. As of December 31, 2005, \$30.0 million of the facility was available for additional borrowings.

*Inventory Trade Credit Agreements.* These agreements contain similar financial ratios and operational covenants and restrictions as those contained in our bank line of credit described above. Such agreements also contain cross-default provisions whereby a default under the bank agreement would also constitute a default under these agreements. Financing under these agreements is limited to the purchase of specific branded products from authorized suppliers, and amounts outstanding must be fully collateralized by inventories of those products on hand.

*Capital Markets.* Our ability to raise additional funds in the capital market depends upon, among other things, general economic conditions, the condition of the information technology industry, our financial performance and stock price, and the state of the capital markets.

### **APPLICATION OF CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

The SEC requires that all registrants disclose their most “critical accounting policies” in “Management’s Discussion of Financial Condition and Results of Operations.” A “critical accounting policy” has been defined as one that is both important to the portrayal of the registrant’s financial condition and results and requires

## [Table of Contents](#)

management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Further, "critical accounting policies" are those that are reflective of significant judgments and uncertainties, and potentially result in materially different results under different assumptions and conditions.

We believe that our accounting policies described below fit the definition of "critical accounting policies." We have reviewed our policies for the year ended December 31, 2005 and determined that they remain our most critical accounting policies.

### **Revenue Recognition**

Revenue on product sales is recognized at the point in time when persuasive evidence of an arrangement exists, the price is fixed and final, delivery has occurred, and there is a reasonable assurance of collection of the sales proceeds. We generally obtain oral or written purchase authorizations from our customers for a specified amount of product at a specified price. Because we either (i) have a general practice of covering customer losses while products are in transit despite title transferring to the customer at the point of shipment or (ii) have FOB – destination specifically set out in our arrangements with federal agencies, delivery is deemed to have occurred at the point in time when the product is received by the customer. We provide our customers with a limited thirty-day right of return generally limited to defective merchandise. Revenue is recognized at delivery and a reserve for sales returns is recorded. We have demonstrated the ability to make reasonable and reliable estimates of product returns in accordance with Statement of Financial Accounting Standards No. 48, "Revenue Recognition When Right of Return Exists," based on significant historical experience. Should such returns no longer prove estimable, we believe that the impact on our financials would not necessarily be significant, since the return privilege expires 30 days after shipment.

Revenue for third party service contracts are recorded on a net sales recognition basis because we do not assume the risks and rewards of ownership in these transactions. For such contracts, we evaluate whether the sales of such services should be recorded as gross sales or net sales as required under the guidelines described in Staff Accounting Bulletin No. 104, "Revenue Recognition" and EITF Issue No. 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent." Under gross sales recognition, we are the primary obligor, and the entire selling process is recorded in sales with our cost to the third party service provider recorded as a cost of sales. Under net sales recognition, we are not the primary obligor, and the cost to the third party service provider is recorded as a reduction to sales, with no cost of goods sold, thus leaving the entire gross profit as the reported net sale for the transaction.

Similarly, we recognize revenue from agency sales transactions on a net sales basis. In agency sales transactions, we facilitate product sales by equipment manufacturers directly to our customers and receive agency fees for such transactions. We do not take title to the products or assume any maintenance or return obligations in these transactions; title is passed directly from the supplier to our customer.

Net amounts included in revenue for such service contracts and agency sales transactions were \$7.3 million, \$5.8 million, and \$5.0 million for the years ended December 31, 2005, 2004, and 2003, respectively.

### **Accounts Receivable**

We perform ongoing credit evaluations of our customers and adjust credit limits based upon payment history and customers' current credit worthiness. Our allowance is generally computed by (1) applying specific percentage reserves on accounts that are past due; and (2) specifically reserving for customers known to be in financial difficulty. Therefore, if the financial condition of certain of our customers were to deteriorate, or if we noted there was a lengthening of the timing of the settlement of receivables that was symptomatic of a general deterioration in the ability of our customers to pay, we would have to increase our allowance for doubtful accounts. This would negatively impact our earnings. Our cash flows would be impacted to the extent that receivables could not be collected.

## [Table of Contents](#)

In addition to accounts receivable from customers, we record receivables from our vendors/suppliers for cooperative advertising, price protection, supplier reimbursements, rebates, and other similar arrangements. A portion of such receivables is estimated based on information available from our vendors at discrete points in time. While such estimates have historically approximated actual cash received, an unanticipated change in a promotional program could give rise to a reduction in the receivable. This could negatively impact our earnings and our cash flows.

Considerable judgment is used in assessing the ultimate realization of customer receivables and vendor/supplier receivables, including reviewing the financial stability of a customer, vendor information, and gauging current market conditions. If our evaluations are incorrect, we may incur future charges to our income statement.

### **Vendor Consideration**

We receive allowances from merchandise vendors for price protections, discounts, product rebates, and other programs. These allowances are treated as a reduction of the vendor's prices and are recorded as adjustments to cost of sales or inventory, as applicable. We also receive vendor co-op advertising funding for our catalogs and other programs. Vendors have the ability to place advertisements in the catalogs for which we receive advertising allowances. These vendor allowances, to the extent that they represent specific reimbursements of the underlying specific, incremental, and identifiable costs, are offset against selling, general, and administrative expense on the consolidated statements of income. Advertising reimbursements that cannot be associated with a specific program funded by an individual vendor or that exceed the fair value of advertising expense associated with that program are recorded as reductions to cost of inventory purchases in accordance with EITF 02-16. The level of allowances received from certain merchandise vendors has declined in past years and may do so again. Such a decline could have a material impact on gross margin and operating income.

### **Inventories – Merchandise**

Inventories (all finished goods) consisting of software packages, computer systems, peripheral equipment, and consumer electronics are stated at cost (determined under the first-in, first-out method) or market, whichever is lower. Inventory quantities on hand are reviewed regularly, and provisions are made for obsolete, slow moving, and non-salable inventory, based primarily on management's forecast of customer demand for those products in inventory. The IT industry is characterized by rapid technological change and new product development that could result in increased obsolescence of inventory on hand. Increased obsolescence or decreased customer demand beyond management's expectations could require additional provisions. This could negatively impact our earnings. Our obsolescence charges have historically ranged between \$6.0 million and \$7.0 million per annum. Historically, there have been no unusual charges precipitated by specific technological or forecast issues.

### **Contingencies**

From time to time we are subject to potential claims and assessments from third parties. We continually assess whether or not such claims have merit and warrant accrual under the "probable and estimable" criteria of Statement of Financial Accounting Standard No. 5, "Accounting for Contingencies." In 2003, we were subject to audit by the GSA. While we have accrued an estimate of our anticipated liability in the financial statements, such estimate is subject to change based on incremental findings by the government auditors. Any such change in estimate will impact both our results of operations and our cash flows.

### **Value of Long-Lived Assets, Including Intangibles**

We carry a variety of long-lived assets on our balance sheet. These are all currently classified as held for use. These include property and equipment, identifiable intangibles, and goodwill. An impairment review is undertaken on (1) an annual basis for assets such as goodwill and indefinite lived intangible assets; and (2) on an event-driven basis for all long-lived assets (including indefinite lived intangible assets and goodwill) when facts and circumstances suggest that cash flows emanating from such assets may be diminished. We may review the

## [Table of Contents](#)

carrying value of all these assets based partly on our projections of anticipated cash flows – projections which are, in part, dependent upon anticipated market conditions, operational performance, and legal status. Any impairment charge that is recorded negatively impacts our earnings. Cash flows are generally not impacted.

Over the last several years, we have incurred no impairment charges. While we believe that our future estimates are reasonable, different assumptions regarding items such as future cash flows and the volatility inherent in markets which we serve could materially effect our valuations and result in impairment charges against the carrying value of those assets.

### **Employee Compensation and Benefits**

Our employee compensation model has several elements that we consider variable. These include our obligation to our employees for health care. We have selected a plan that results in our being self-insured up to certain stop-loss limits. Accordingly, we have to estimate the amount of health care claims outstanding at a given point in time. These estimates are based on historical experience and could be subject to change. Such change could negatively impact both our earnings and our cash flows.

We also have granted stock options to our employees. In general, such grants since 1998 have been made at the current fair value of our stock and accordingly, given that we account for option awards under APB Opinion 25, “Accounting for Stock Issued to Employees” (“APB 25”), no compensation charge has been recorded. In previous years, most specifically those years prior to our initial public offering, there was a difference between the strike price of the option and the then current fair value of the stock. This difference resulted in a fixed and determinable compensation charge. In December 2005, we accelerated the vesting of certain stock options. This acceleration was undertaken to minimize recognition of compensation expense in future years in anticipation of the adoption of SFAS 123(R) in 2006, as discussed below. (See “*Note 11—Stockholders’ Equity*” of our “*Notes to Consolidated Financial Statements*” for further discussion.) We did not, however, modify option grants in a manner that would cause either re-measurement of the awards or the commencement of variable accounting.

As described in the notes to the financial statements, pro-forma disclosure has been provided as if we applied the fair value methodology to option awards. The recognition of compensation for awards, as will be required upon the adoption of Statement of Financial Accounting Standard No. 123(R), “Share-Based Payment” (“SFAS 123(R)”) for our interim quarter ending March 31, 2006, will have an adverse effect on our earnings. For the years 2006 through 2009, we expect to record \$0.6 million, \$0.5 million, \$0.3 million, and \$0.1 million, respectively, for the remaining unvested options held by officers from grants greater than 20,000 shares.

We have also engaged in workforce reduction actions in each of the last three years. These actions included formula driven termination benefits. These benefits were or are being paid relatively quickly and have not been subject to change. We do not foresee a circumstance where there could be significant variability in our workforce reduction estimates. However, if we did experience significant variability, such change could negatively impact our cash flows.

### **RECENTLY ISSUED FINANCIAL ACCOUNTING STANDARDS**

In December 2004, the Financial Accounting Standards Board issued SFAS No. 123(R). This Statement is a revision of SFAS No. 123, “Accounting for Stock-Based Compensation,” and supersedes APB 25 and its related implementation guidance. SFAS 123(R) requires a company to measure the grant date fair value of equity awards given to employees in exchange for services and recognize that cost over the period that such services are performed. SFAS 123(R) is effective for the beginning of the first fiscal year after June 15, 2005 and will be effective for our interim quarter ending March 31, 2006. SFAS 123(R) allows the choice between two methods of adoption: the modified-prospective transition method and the modified-retrospective transition method. Adoption of SFAS 123(R) may materially increase stock compensation expense and decrease net income. In addition, SFAS 123(R) requires that the excess tax benefits related to stock compensation be reported as a cash inflow

## [Table of Contents](#)

from financing activities rather than as a reduction of taxes paid in cash from operations. We have adopted the provisions of SFAS 123(R) effective January 1, 2006, using the modified prospective approach.

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections," ("SFAS 154") which is a replacement of APB Opinion No. 20, "Accounting Changes," and FASB Statement No. 3, "Reporting Accounting Changes in Interim Financial Statements." SFAS 154 changes the requirements for the accounting and reporting of accounting changes by requiring retrospective application to prior period financial statements unless impracticable. This statement is effective in fiscal years beginning after December 15, 2005.

### **INFLATION**

We have historically offset any inflation in operating costs by a combination of increased productivity and price increases, where appropriate. We do not expect inflation to have a significant impact on our business in the foreseeable future.

### **Item 7A. Quantitative and Qualitative Disclosure About Market Risk**

We invest cash balances in excess of operating requirements in short-term securities, generally with maturities of 90 days or less. In addition, our unsecured credit agreement provides for borrowings which bear interest at variable rates based on the prime rate. We had \$20.0 million in borrowings outstanding pursuant to the credit agreement as of December 31, 2005. We believe the effect, if any, of reasonably possible near-term changes in interest rates on our financial position, results of operations, and cash flows should not be material. Our credit agreement exposes earnings to changes in short-term interest rates since interest rates on the underlying obligations are variable. However, as noted above, \$20.0 million in borrowings were outstanding on the credit agreement at December 31, 2005, and the average outstanding borrowings during the year were \$7.5 million. Accordingly, the change in earnings resulting from a hypothetical 10% increase or decrease in interest rates is not material.

### **Item 8. Consolidated Financial Statements and Supplementary Data**

The information required by this Item is included in this Report beginning at page F-1.

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

Not applicable.

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

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of December 31, 2005. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Our disclosure controls

## [Table of Contents](#)

and procedures are designed to provide reasonable assurance of achieving their objectives as described above. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were effective at the reasonable assurance level.

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the fiscal quarter ended December 31, 2005 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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

On November 11, 2005, our subsidiary Merrimack Services Corporation entered into a four-year amendment to its lease with EWE Warehouse Investments V, LTD. for property located in Wilmington, Ohio. The lease, one of two that we have for our Wilmington distribution center, was effective December 1, 2005 and requires a monthly payment of \$40,533.

On December 12, 2005, our subsidiary GovConnection, Inc. entered into a three-year amendment with Metro Park I, LLC for office property located in Rockville, Maryland. The lease commences April 1, 2006 and requires a monthly payment of \$16,781 in year one of the lease, \$17,284 in year two, and \$17,803 in year three.

On March 30, 2006, Robert F. Wilkins, Executive Vice President, resigned from the Company. The Company intends to enter into a separation agreement under which Mr. Wilkins will receive a total of \$430,000, payable in equal bi-weekly payments over a period of 52 weeks. A copy of Mr. Wilkins's employment agreement was filed previously by the Company with the Securities and Exchange Commission.

Mr. Wilkins will be retained as a consultant by the Company following his separation. Under the terms of the consulting agreement, Mr. Wilkins will earn between \$264,000 and \$304,000 over a period of one year.



**PART III**

**Item 10. Directors and Executive Officers of the Registrant**

The information included under the headings, “Executive Officers of PC Connection” in Item 4 of Part I hereof and “Information Concerning Directors, Nominees, and Executive Officers,” “Section 16(a) Beneficial Ownership Reporting Compliance” and “Code of Business Conduct” in our definitive Proxy Statement for our 2006 Annual Meeting of Stockholders to be held on May 24, 2006 (the “Proxy Statement”) is incorporated herein by reference. We anticipate filing the Proxy Statement within 120 days after December 31, 2005. With the exception of the foregoing information and other information specifically incorporated by reference into this Form 10-K, the Proxy Statement is not being filed as a part hereof.

**Item 11. Executive Compensation**

The information included under the heading “Executive Compensation” in the Proxy Statement is incorporated herein by reference.

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

The information included under the heading “Security Ownership of Certain Beneficial Owners and Management” and “Equity Compensation Plan Information” in the Proxy Statement is incorporated herein by reference.

**Item 13. Certain Relationships and Related Transactions**

The information included under the heading “Certain Transactions and Relationships” in the Proxy Statement is incorporated herein by reference.

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

The information included under the heading “Principal Accountant Fees and Services” in the Proxy Statement is incorporated herein by reference.

**PART IV**

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

(a) List of Documents Filed as Part of this Report:

(1) Consolidated Financial Statements

The consolidated financial statements listed below are included in this document.

<u>Consolidated Financial Statements</u>	<u>Page References</u>
Report of Management	F-2
Report of Independent Registered Public Accounting Firm	F-3
Consolidated Balance Sheets	F-4
Consolidated Statements of Income	F-5
Consolidated Statement of Changes in Stockholders' Equity	F-6
Consolidated Statements of Cash Flows	F-7
Notes to Consolidated Financial Statements	F-8

(2) Consolidated Financial Statement Schedule:

The following Consolidated Financial Statement Schedule, as set forth below, is filed with this report:

<u>Schedule</u>	<u>Page Reference</u>
<a href="#">Schedule II—Valuation and Qualifying Accounts</a>	F-28

All other schedules have been omitted because they are either not applicable or the relevant information has already been disclosed in the financial statements.

(3) Supplementary Data

Not applicable.

## Table of Contents

### (b) Exhibits

The exhibits listed below are filed herewith or are incorporated herein by reference to other filings.

#### EXHIBIT INDEX

<u>Exhibits</u>	
3.2(1)	Amended and Restated Certificate of Incorporation of Registrant.
3.4(1)	Bylaws of Registrant.
4.1(1)	Form of specimen certificate for shares of Common Stock, \$0.01 par value per share, of the Registrant.
9.1(1)	Form of 1998 PC Connection Voting Trust Agreement among the Registrant, Patricia Gallup individually and as a trustee, and David Hall individually and as trustee.
10.1(1)	Form of Registration Rights Agreement among the Registrant, Patricia Gallup, David Hall, and the 1998 PC Connection Voting Trust.
10.2(1)	1993 Incentive and Non-Statutory Stock Option Plan, as amended.
10.3(1)	1997 Stock Incentive Plan.
10.4	Amended and Restated 1997 Employee Stock Purchase Plan, as amended
10.5(18)	PC Connection, Inc. Discretionary Bonus Plan.
10.6(1)	Employment Agreement between the Registrant and Robert F. Wilkins, dated December 23, 1995.
10.7(4)	Amendment to Employment Agreement between the Registrant and Robert F. Wilkins dated December 23, 1995.
10.8(1)	Employment Agreement, dated as of January 1, 1998, between the Registrant and Patricia Gallup.
10.9	Separation Agreement by and between PC Connection, Inc. and Kenneth A. Grady, dated November 28, 2005.
10.10(1)	Agreement between the Registrant and Ingram Micro, Inc., dated October 30, 1997, as amended.
10.11(11)	Agreement for Inventory Financing, dated as of October 31, 2002, by and among the Registrant, Merrimack Services Corporation, GovConnection, Inc., MoreDirect, Inc., and IBM Credit Corporation.
10.12(11)	Guaranty, dated as of November 14, 2002, entered into by Registrant in connection with the Agreement for Inventory Financing, dated as of October 31, 2002, by and among the Registrant, Merrimack Services Corporation, GovConnection, Inc., MoreDirect, Inc., and IBM Credit Corporation.
10.13(11)	Guaranty, dated as of November 14, 2002, entered into by PC Connection Sales Corporation in connection with the Agreement for Inventory Financing, dated as of October 31, 2002, by and among the Registrant, Merrimack Services Corporation, GovConnection, Inc., MoreDirect, Inc., and IBM Credit Corporation.
10.14(11)	Acknowledgement, Waiver and Amendment to Agreement for Inventory Financing, dated as of November 25, 2003, by and among the Registrant, Merrimack Services Corporation, GovConnection, Inc., MoreDirect, Inc. and IBM Credit LLC.
10.15	Second Amendment, dated May 9, 2004, to the Agreement for Inventory Financing between the Registrant and its subsidiaries Merrimack Services Corporation, GovConnection, Inc., and MoreDirect, Inc. and IBM Credit LLC.
10.16	Third Amendment, dated May 27, 2005, to the Agreement for Inventory Financing between the Registrant and its subsidiaries Merrimack Services Corporation, Inc., GovConnection, Inc., and MoreDirect, Inc. and IBM Credit LLC.
10.17(15)	Second Amended and Restated Credit and Security Agreement, dated June 29, 2005, among Citizens Bank of Massachusetts, as lender and as agent, other financial institutions party thereto from time to time, as lenders, PC Connection, Inc., as borrower, GovConnection, Inc., Merrimack Services Corporation, PC Connection Sales Corporation, PC Connection Sales of Massachusetts, Inc. and MoreDirect, Inc., each as guarantors
10.18(6)	Agreement and Plan of Merger, dated March 25, 2002, by and among PC Connection, Inc., Boca Acquisition Corp., MoreDirect, Inc. and the stockholders of MoreDirect, Inc. set forth on Schedule 1 thereto.

## Table of Contents

<u>Exhibits</u>	
10.19(7)	Amendment No. 1 to the Agreement and Plan of Merger, dated April 5, 2002, by and among PC Connection, Inc., Boca Acquisition Corp., MoreDirect, Inc., Russell Madris, the sole stockholder of MoreDirect, Inc. and Michael Diamant, James Garrity, and Scott Madris.
10.20(16)	Bill of Sale, dated October 21, 2005, between PC Connection, Inc. and IBM Credit, LLC.
10.21(10)(+)	National Account Agreement between Airborne Express, Inc. and Merrimack Services Corporation d/b/a PC Connection Services, dated June 2, 2003.
10.22(17)	Amendment to agreement with DHL Express, Inc., dated July 30, 2004.
10.23(1)	Lease between the Registrant and Gallup & Hall partnership, dated June 1, 1987, as amended, for property located in Marlow, New Hampshire.
10.24(4)	Amendment, dated January 1, 1999, to the Lease Agreement between the Registrant and Gallup & Hall Partnership, dated June 1, 1987, as amended for property located in Marlow, New Hampshire.
10.25(8)	Lease between Merrimack Services Corporation and Audio Accessories, Inc., dated November 1, 2002, for property located at Mill Street, Marlow, New Hampshire.
10.26(1)	Lease between the Registrant and Gallup & Hall partnership, dated May 1, 1997, for property located at 442 Marlboro Street, Keene, New Hampshire.
10.27(8)	Amendment, dated June 1, 2002, to the Lease Agreement between Merrimack Services Corporation and Gallup & Hall, dated May 1, 1997, for property located at 442 Marlboro Street, located in Keene, New Hampshire.
10.28(1)	Amended and Restated Lease between the Registrant and G&H Post, LLC, dated December 29, 1997, for property located at Route 101A, Merrimack, New Hampshire.
10.29(2)	Amendment No. 1 to Amended and Restated Lease between the Registrant and G&H Post, LLC, dated December 29, 1998, for property located at Route 101A, Merrimack, New Hampshire.
10.30(1)	Lease between the Registrant and Gallup & Hall partnership, dated July 22, 1998, for property located at 450 Marlboro Street, Keene, New Hampshire.
10.31(4)	Lease between PC Connection, Inc. and The Hillsborough Group, dated January 5, 2000, for property located at 706 Route 101A, Merrimack, New Hampshire.
10.32(12)	Amendment, dated September 7, 2004, to the Lease Agreement between Merrimack Services Corporation and The Hillsborough Group, dated January 5, 2000, for property located at 706 Route 101A, Merrimack, New Hampshire.
10.33(1)	Lease between the Registrant and Miller-Valentine Partners, dated September 24, 1990, as amended, for property located at Old State Route 73, Wilmington, Ohio.
10.34(4)	Third Amendment, dated June 26, 2000, to the Lease Agreement between Merrimack Services Corporation and EWE Warehouse Investments V, LTD., dated July 31, 1998, for property located at 2840 Old State Route 73, Wilmington, Ohio.
10.35(8)	Fourth Amendment, dated July 31, 2002, to the Lease Agreement between Merrimack Services and EWE Warehouse Investments V, LTD, dated June 26, 2000, for property located at Old State Route 73, Wilmington, Ohio.
10.36(13)	Fifth Amendment, dated February 28, 2005, to the Lease Agreement between Merrimack Services Corporation and EWE Warehouse Investments V, LTD., for property located at 2780-2880 Old State Route 73, Wilmington, Ohio.
10.37(3)	Assignment of Lease Agreements, dated December 13, 1999, between Micro Warehouse, Inc. (assignor) and the Registrant (assignee), for property located at Old State Route 73, Wilmington, Ohio.
10.38(5)	Amendment, dated June 19, 2001, to the Assignment of Lease Agreements, dated as of December 13, 1999, between Micro Warehouse Inc. (assignor) and Merrimack Services Corporation for property located at Old State Route 73, Wilmington, Ohio.
10.39(11)	Second Amendment, dated April 24, 2003, to the Lease Agreement between Merrimack Services and EWE Warehouse Investments V, LTD, as amended June 19, 2001, for property located at Old State Route 73, Wilmington, Ohio.
10.40	Third Amendment, dated November 11, 2005, to the Lease Agreement between Merrimack Services and EWE Warehouse Investments V, LTD, as amended April 24, 2003, for property located at Old State Route 73, Wilmington, Ohio.

## Table of Contents

<u>Exhibits</u>	
10.41(4)	Lease between ComTeq Federal, Inc. and Rockville Office/Industrial Associates dated December 14, 1993, for property located at 7503 Standish Place, Rockville, Maryland.
10.42(4)	Amendment, dated November 1, 1996, to the Lease Agreement between ComTeq Federal, Inc. and Rockville Office/Industrial Associates for property located in Rockville, Maryland.
10.43(4)	Second Amendment, dated March 31, 1998, to the Lease Agreement between ComTeq Federal, Inc. and Rockville Office/Industrial Associates, dated November 1, 1996, as amended for property located in Rockville, Maryland.
10.44(4)	Third Amendment, dated August 31, 2000, to the Lease Agreement between ComTeq Federal, Inc. and Rockville Industrial Associates, dated March 31, 1998, as amended for property located in Rockville, Maryland.
10.45(8)	Fourth Amendment, dated November 20, 2002, to the Lease Agreement between GovConnection (formerly known as ComTeq Federal, Inc.) and Rockville Office/Industrial Associates, dated March 31, 1998, as amended for property located in Rockville, Maryland.
10.46	Fifth Amendment, dated December 12, 2005, to the Lease Agreement between GovConnection, Inc. Metro Park I, LLC, dated December 14, 2003, for property located in Rockville, Maryland.
10.47(4)	Lease between Merrimack Services Corporation and Schleicher & Schuell, Inc., dated November 16, 2000, for property located at 10 Optical Avenue, Keene, New Hampshire.
10.48(9)	Lease between GovConnection, Inc. and Fairhaven Investors Limited Partnership, dated April 30, 2003, for property located at 2150 Post Road, Fairfield, Connecticut.
10.49(14)	Amendment, dated April 14, 2005, to the Lease Agreement between GovConnection, Inc. and Fairhaven Investors Limited Partnership, dated May 1, 2003, for property located in Fairhaven, Connecticut.
10.50(12)	Amendment, dated September 24, 2004, to the Lease Agreement between Merrimack Services Corporation and Bronx II, LLC, dated October 27, 1988, as amended for property located in Marlborough, MA.
10.51(13)	Lease between MoreDirect, Inc. and Boca Technology Center, LLC, dated February 14, 2005, for property located in Boca Raton, Florida.
10.52(13)	Sublease between Merrimack Services Corporation and 222 International, LP, dated March 4, 2005, for property located in Portsmouth, New Hampshire.
10.53	Lease between MoreDirect, Inc. and RMC Midway Walnut, LP, dated January 06, 2006, for property located at 14295 Midway Road, Addison, Texas.
10.54	Lease between PC Connection Sales of Massachusetts, Inc. and RMC Midway Walnut, LP, dated January 06, 2006, for property located at 14295 Midway Road, Addison, Texas.
10.55	Summary of Compensation for Executive Officers.
10.56	Summary of Compensation for Non-Employee Directors.
21.1	Subsidiaries of Registrant.
23.1	Consent of Deloitte & Touche LLP.
31.1	Certification of the Company's President and Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of the Company's Vice President, Treasurer and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of the Company's President and Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of the Company's Vice President, Treasurer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
(1)	Incorporated by reference from the exhibits filed with the Company's registration statement (333-41171) on Form S-1 filed under the Securities Act of 1933.
(2)	Incorporated by reference from exhibits filed with the Company's annual report on Form 10-K, File Number 0-23827, filed on March 31, 1999.
(3)	Incorporated by reference from exhibits filed with the Company's annual report on Form 10-K/A Amendment No. 1, File Number 0-23827, filed on April 4, 2000.

## Table of Contents

- (4) Incorporated by reference from exhibits filed with the Company's annual report on Form 10-K, File Number 0-23827, filed on March 30, 2001.
- (5) Incorporated by reference from exhibits filed with the Company's quarterly report on Form 10-Q, File Number 0-23827, filed on August 14, 2001.
- (6) Incorporated by reference from exhibits filed with the Company's annual report on Form 10-K, File Number 0-23827, filed on April 1, 2002.
- (7) Incorporated by reference from exhibits filed with the Company's current report on Form 8-K, dated April 5, 2002.
- (8) Incorporated by reference from exhibits filed with the Company's annual report on Form 10-K, File Number 0-23827, filed on March 31, 2003.
- (9) Incorporated by reference from exhibits filed with the Company's quarterly report on Form 10-Q, File Number 0-23827, filed on August 13, 2003.
- (10) Incorporated by reference from exhibits filed with the Company's quarterly report on Form 10-Q, File number 0-23827, filed November 20, 2003.
- (11) Incorporated by reference from exhibits filed with the Company's annual report on Form 10-K, File Number 0-23827, filed on March 30, 2004.
- (12) Incorporated by reference from exhibits filed with the Company's quarterly report on Form 10-Q, File Number 0-23827, filed November 15, 2004.
- (13) Incorporated by reference from exhibits filed with the Company's annual report on Form 10-K, File Number 0-23827, filed on March 31, 2005.
- (14) Incorporated by reference from exhibits filed with the Company's quarterly report on Form 10-Q, filed on May 16, 2005.
- (15) Incorporated by reference from exhibits filed with the Company's current report on Form 8-K, filed on July 6, 2005.
- (16) Incorporated by reference from exhibits filed with the Company's current report on Form 8-K, filed on October 27, 2005.
- (17) Incorporated by reference from exhibits filed with the Company's quarterly report on Form 10-Q, filed on November 14, 2005.
- (18) Incorporated by reference from exhibits filed with the Company's current report on Form 8-K, filed on December 30, 2005.
- (+) Confidential treatment requested for this agreement.



[Table of Contents](#)

**PC CONNECTION, INC. AND SUBSIDIARIES**  
**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

	<u>Page</u>
<a href="#">Report of Management</a>	F-2
<a href="#">Report of Independent Registered Public Accounting Firm</a>	F-3
<a href="#">Consolidated Balance Sheets as of December 31, 2005 and 2004</a>	F-4
<a href="#">Consolidated Statements of Income for the years ended December 31, 2005, 2004, and 2003</a>	F-5
<a href="#">Consolidated Statement of Changes in Stockholders' Equity for the years ended December 31, 2005, 2004, and 2003</a>	F-6
<a href="#">Consolidated Statements of Cash Flows for the years ended December 31, 2005, 2004, and 2003</a>	F-7
<a href="#">Notes to Consolidated Financial Statements</a>	F-8



## REPORT OF MANAGEMENT

Responsibility for the integrity and objectivity of the financial information presented in this Annual Report on Form 10-K rests with PC Connection, Inc. and its subsidiaries (“the Company”) management. The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America, applying certain estimates and judgments as required.

While we have not performed our first formal assessment of internal control over financial reporting called for by the Public Company Accounting Oversight Board Standard No. 2, we believe the Company maintains an effective internal control structure. It consists, in part, of an organization with clearly defined lines of responsibility and delegation of authority, comprehensive systems, and control procedures. We believe that this structure provides reasonable assurance that transactions are executed in accordance with management authorization and accounting principles generally accepted in the United States of America.

To assure the effective administration of internal control, we carefully select and train our employees, develop and disseminate written policies and procedures, provide appropriate communication channels, and foster an environment conducive to the effective functioning of controls. We believe that it is essential for the Company to conduct its business affairs in accordance with the highest ethical standards.

Deloitte & Touche LLP, an independent registered public accounting firm, is retained to audit the Company’s consolidated financial statements. Its accompanying report is based on an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States).

The Audit Committee of the Board of Directors is composed solely of outside directors and is responsible for recommending to the Board of Directors the independent accounting firm to be retained for the coming year. The Audit Committee meets periodically and privately with the independent auditors, as well as with Company management, to review accounting, auditing, internal control structure, and financial reporting matters.

Patricia Gallup  
President and  
Chief Executive Officer

Jack L. Ferguson  
Vice President, Treasurer and  
Chief Financial Officer

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors of  
PC Connection, Inc.  
Merrimack, New Hampshire

We have audited the accompanying consolidated balance sheets of PC Connection, Inc. and subsidiaries (the “Company”) as of December 31, 2005 and 2004, and the related consolidated statements of income, changes in stockholders’ equity, and cash flows for each of the three years in the period ended December 31, 2005. Our audits also included the financial statement schedule listed in the Index at Item 15. These financial statements and financial statement schedule are the responsibility of the Company’s management. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of PC Connection, Inc. and subsidiaries as of December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2005, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly in all material respects the information set forth therein.

Deloitte & Touche LLP  
Boston, Massachusetts  
March 30, 2006

## PC CONNECTION, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS  
(amounts in thousands, except per share data)

	December 31,	
	2005	2004
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 9,770	\$ 6,829
Accounts receivable, net	162,525	120,752
Inventories—merchandise	75,374	78,390
Deferred income taxes	3,769	3,039
Income taxes receivable	1,742	1,325
Prepaid expenses and other current assets	4,219	3,644
<b>Total current assets</b>	<b>257,399</b>	<b>213,979</b>
Property and equipment, net	17,700	17,647
Goodwill, net	56,820	51,687
Other intangibles, net	5,427	3,040
Other assets	359	189
<b>Total Assets</b>	<b>\$337,705</b>	<b>\$286,542</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities:		
Current maturities of capital lease obligations:		
To affiliate	\$ 416	\$ 373
To third party	412	391
Note payable—bank	19,975	4,810
Accounts payable	114,413	79,709
Accrued expenses and other liabilities	21,290	18,138
Acquisition earn-out obligation	—	6,921
<b>Total current liabilities</b>	<b>156,506</b>	<b>110,342</b>
Capital lease obligations, less current maturities:		
To affiliate	5,299	5,715
To third party	396	841
Deferred income taxes	4,105	3,486
<b>Total Liabilities</b>	<b>166,306</b>	<b>120,384</b>
Commitments and Contingencies (Note 14)		
Stockholders' Equity:		
Preferred Stock, \$.01 par value, 10,000 shares authorized, none issued	—	—
Common Stock, \$.01 par value, 100,000 shares authorized, 25,622 and 25,462 issued, 25,259 and 25,100 outstanding at December 31, 2005 and December 31, 2004, respectively	256	255
Additional paid-in capital	77,884	77,091
Retained earnings	95,545	91,098
Treasury stock at cost	(2,286)	(2,286)
<b>Total Stockholders' Equity</b>	<b>171,399</b>	<b>166,158</b>
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$337,705</b>	<b>\$286,542</b>

See notes to consolidated financial statements.

## PC CONNECTION, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF INCOME

*(amounts in thousands, except per share data)*

	Years Ended December 31,		
	2005	2004	2003
Net sales	\$ 1,444,297	\$ 1,353,834	\$ 1,312,891
Cost of sales	1,280,701	1,201,780	1,175,212
Gross profit	163,596	152,054	137,679
Selling, general, and administrative expenses	151,981	132,729	124,824
Special charges	2,127	5,232	1,929
Income from operations	9,488	14,093	10,926
Interest expense	(1,447)	(1,385)	(1,305)
Other, net	89	152	117
Income before taxes	8,130	12,860	9,738
Income tax provision	(3,683)	(4,556)	(3,850)
Net income	\$ 4,447	\$ 8,304	\$ 5,888
Earnings per common share:			
Basic	\$ .18	\$ .33	\$ .24
Diluted	\$ .18	\$ .33	\$ .23
Shares used in computation of earnings per common share:			
Basic	25,184	25,028	24,713
Diluted	25,281	25,269	25,114

See notes to consolidated financial statements.

## PC CONNECTION, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

*(amounts in thousands)*

	Common Stock		Additional Paid-In Capital	Retained Earnings	Treasury Shares		Total
	Shares	Amount			Shares	Amount	
<b>Balance, January 1, 2003</b>	<b>24,997</b>	<b>\$ 250</b>	<b>\$ 75,274</b>	<b>\$ 76,906</b>	<b>(362)</b>	<b>\$ (2,286)</b>	<b>\$ 150,144</b>
Exercise of stock options, including income tax benefits	257	2	728	—	—	—	730
Issuance of stock under employee stock purchase plan	88	1	426	—	—	—	427
Net income and comprehensive income	—	—	—	5,888	—	—	5,888
<b>Balance, December 31, 2003</b>	<b>25,342</b>	<b>253</b>	<b>76,428</b>	<b>82,794</b>	<b>(362)</b>	<b>(2,286)</b>	<b>157,189</b>
Exercise of stock options, including income tax benefits	47	1	259	—	—	—	260
Issuance of stock under employee stock purchase plan	73	1	404	—	—	—	405
Net income and comprehensive income	—	—	—	8,304	—	—	8,304
<b>Balance, December 31, 2004</b>	<b>25,462</b>	<b>255</b>	<b>77,091</b>	<b>91,098</b>	<b>(362)</b>	<b>(2,286)</b>	<b>166,158</b>
Exercise of stock options, including income tax benefits	96	1	447	—	—	—	448
Issuance of stock under employee stock purchase plan	64	—	312	—	—	—	312
Acceleration of certain stock options	—	—	34	—	—	—	34
Net income and comprehensive income	—	—	—	4,447	—	—	4,447
<b>Balance, December 31, 2005</b>	<b>25,622</b>	<b>\$ 256</b>	<b>\$ 77,884</b>	<b>\$ 95,545</b>	<b>(362)</b>	<b>\$ (2,286)</b>	<b>\$ 171,399</b>

See notes to consolidated financial statements.

**PC CONNECTION, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
*(amounts in thousands)*

	Years Ended December 31,		
	2005	2004	2003
<b>Cash Flows from Operating Activities:</b>			
Net income	\$ 4,447	\$ 8,304	\$ 5,888
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	7,197	7,127	8,363
Deferred income taxes	(111)	632	(888)
Provision for doubtful accounts	3,993	4,280	2,953
Loss on disposal of fixed assets	43	8	41
Acceleration of certain stock options	34	—	—
Changes in assets and liabilities:			
Accounts receivable	(45,766)	19,305	(11,976)
Inventories	3,016	1,750	(27,661)
Prepaid expenses and other current assets	(992)	870	(1,267)
Other non-current assets	(170)	19	126
Accounts payable	34,704	(32,829)	27,045
Income tax benefits from exercise of stock options	82	97	349
Accrued expenses and other liabilities	3,152	3,755	328
Net cash provided by operating activities	<u>9,629</u>	<u>13,318</u>	<u>3,301</u>
<b>Cash Flows from Investing Activities:</b>			
Purchases of property and equipment	(6,572)	(2,804)	(2,517)
Purchase of intangible asset	(475)	—	—
Proceeds from sale of property and equipment	13	3	2
Payments of acquisition earn-out obligations	(6,921)	(11,095)	(10,829)
Payment for acquisition	(7,779)	—	—
Cash escrow distributed for acquisition	—	5,000	5,000
Net cash used for investing activities	<u>(21,734)</u>	<u>(8,896)</u>	<u>(8,344)</u>
<b>Cash Flows from Financing Activities:</b>			
Proceeds from short-term borrowings	320,379	369,285	238,259
Repayment of short-term borrowings	(305,214)	(370,089)	(232,645)
Repayment of capital lease obligations	(797)	(334)	(199)
Exercise of stock options	366	163	381
Issuance of stock under employee stock purchase plan	312	405	427
Net cash provided by (used for) financing activities	<u>15,046</u>	<u>(570)</u>	<u>6,223</u>
Increase in cash and cash equivalents	2,941	3,852	1,180
Cash and cash equivalents, beginning of year	6,829	2,977	1,797
Cash and cash equivalents, end of year	<u>\$ 9,770</u>	<u>\$ 6,829</u>	<u>\$ 2,977</u>
<b>Supplemental Cash Flow Information:</b>			
Interest paid	\$ 1,188	\$ 1,155	\$ 899
Income taxes paid	3,960	2,819	6,065
Acquisition earn-out obligation, net of adjustments	—	6,423	11,560
Purchase of assets through capital lease obligation	—	1,232	—

See notes to consolidated financial statements.

**PC CONNECTION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
*(amounts in thousands, except per share data)*

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

PC Connection, Inc. is a national direct marketer of a wide range of information technology products and services—including computer systems, software and peripheral equipment, networking communications, and other products and accessories that we purchase from manufacturers, distributors, and other suppliers. We operate through three primary business segments: (1) consumers and small- to medium-sized businesses, or SMB, through our PC Connection Sales subsidiaries, (2) federal, state, and local government and educational institutions, or Public Sector, through our GovConnection subsidiary, and (3) large corporate accounts, or Large Account, through our MoreDirect subsidiary.

We generate sales through (i) outbound telemarketing and field sales contacts by account managers focused on the business, education, and government markets, (ii) our Web sites, and (iii) inbound calls from customers responding to our catalogs and other advertising media. The following is a summary of significant accounting policies.

***Principles of Consolidation***

The consolidated financial statements include the accounts of PC Connection, Inc. and subsidiaries. Intercompany transactions and balances are eliminated in consolidation.

***Use of Estimates in the Preparation of Financial Statements***

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These estimates and assumptions affect the amounts reported in the accompanying consolidated financial statements. Actual results could differ from those estimates.

***Revenue Recognition***

Revenue on product sales is recognized at the point in time when persuasive evidence of an arrangement exists, the price is fixed and final, delivery has occurred, and there is a reasonable assurance of collection of the sales proceeds. We generally obtain oral or written purchase authorizations from our customers for a specified amount of product at a specified price. Because we either (i) have a general practice of covering customer losses while products are in-transit despite title transferring at the point of shipment or (ii) have FOB—destination specifically set out in our arrangements with federal agencies and certain commercial customers, delivery is deemed to have occurred at the point in time when the product is received by the customer.

We provide our customers with a limited thirty-day right of return generally limited to defective merchandise. Revenue is recognized at delivery and a reserve for sales returns is recorded. We have demonstrated the ability to make reasonable and reliable estimates of product returns in accordance with Statement of Financial Accounting Standards (“SFAS”) No. 48, “Revenue Recognition When Right of Return Exists,” based on significant historical experience.

All amounts billed to a customer in a sale transaction related to shipping and handling, if any, represent revenues earned for the goods provided, and these amounts have been classified as “net sales.” Costs related to such shipping and handling billings are classified as “cost of sales.”

Revenue for third party service contracts is recorded on a net sales recognition basis because we do not assume the risks and rewards of ownership in these transactions. For such contracts, we evaluate whether the

## [Table of Contents](#)

sales of such services should be recorded as gross sales or net sales as required under the guidelines described in Staff Accounting Bulletin No. 104, "Revenue Recognition" and Emerging Issues Task Force ("EITF") Issue No. 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent." Under gross sales recognition, we are the primary obligor, and the entire selling process is recorded in sales with our cost to the third party service provider recorded as a cost of sales. Under net sales recognition, we are not the primary obligor, and the cost to the third party service provider is recorded as a reduction to sales, with no cost of goods sold, thus leaving the entire gross profit as the reported net sale for the transaction.

Similarly, we recognize revenue from agency sales transactions on a net sales basis. In agency sales transactions, we facilitate product sales by equipment manufacturers directly to our customers and receive agency fees for such transactions. We do not take title to the products in these transactions; title is passed directly from the supplier to our customer.

Net amounts included in revenue for such service contracts and agency sales transactions were \$7,279, \$5,797, and \$4,960 for the years ended December 31, 2005, 2004, and 2003, respectively.

### ***Cost of Sales and Certain Other Costs***

Cost of sales includes the invoice cost of the product, packaging, inbound and outbound freight, and provisions for inventory obsolescence, adjusted for discounts, rebates, and other vendor consideration adjustments, including those pursuant to EITF Issue No. 02-16, "Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor" ("EITF 02-16"). Direct operating expenses relating to our purchasing function and receiving, inspection, internal transfer, warehousing, packing and shipping, and other expenses of our distribution center are included in selling, general, and administrative expenses. Total direct operating expenses relating to these functions included in selling, general, and administrative expenses for the years ended December 31, 2005, 2004, and 2003 are shown below:

<b>Years Ended December 31,</b>		
<b>2005</b>	<b>2004</b>	<b>2003</b>
\$8,911	\$8,684	\$9,112

### ***Cash and Cash Equivalents***

We consider all highly liquid short-term investments with original maturities of 90 days or less to be cash equivalents. The carrying value of our cash equivalents approximates fair value. The majority of payments due from credit card processors and banks for third-party credit card and debit card transactions process within one to five business days. All credit card and debit card transactions that process in less than seven days are classified as cash and cash equivalents. Amounts due from banks for these transactions classified as cash totaled \$ 4,189 and \$2,845 at December 31, 2005 and 2004, respectively.

### ***Accounts Receivable***

We perform ongoing credit evaluations of our customers and adjust credit limits based on payment history and customer credit-worthiness. We maintain an allowance for estimated doubtful accounts based on our historical experience and the customer credit issues identified. We monitor collections regularly and adjust the allowance for doubtful accounts as necessary to recognize any changes in credit exposure.

### ***Inventories—Merchandise***

Inventories (all finished goods) consisting of software packages, computer systems, and peripheral equipment, are stated at cost (determined under the first-in, first-out method) or market, whichever is lower. Inventory quantities on hand are reviewed regularly, and allowances are maintained for obsolete, slow moving, and nonsalable inventory.



***Vendor Allowances***

We receive allowances from merchandise vendors for price protections, discounts, product rebates, and other programs. These allowances are treated as a reduction of the vendor's prices and are recorded as adjustments to cost of sales or inventory, as applicable. Allowances from product rebates that require certain volumes of product sales or purchases are recorded only after the related milestones are met.

***Advertising Costs and Reimbursements***

Costs of producing and distributing catalogs are deferred and charged to expense over the period that each catalog remains the most current selling vehicle (generally one to two months) which approximates the period of probable benefits. Other advertising costs are expensed as incurred. Vendors have the ability to place advertisements in the catalogs for which we receive advertising allowances. These vendor allowances, to the extent that they represent specific reimbursements of such specific, incremental, and identifiable costs, are offset against selling, general, and administrative expense on the consolidated statements of income. Advertising reimbursements that cannot be associated with a specific program funded by an individual vendor or that exceed the fair value of advertising expense associated with that program are included in the cost of inventory purchases in accordance with EITF 02-16.

Advertising costs charged to expense were \$23,207, \$22,494, and \$22,764 for the respective years ended December 31, 2005, 2004, and 2003. Total advertising reimbursements received from vendors were \$28,582, \$29,119, and \$29,430 for the respective years ended December 31, 2005, 2004, and 2003. We recorded \$16,725, \$7,498, and \$2,247 of these reimbursements as reductions to cost of sales or inventory in the respective years ended December 31, 2005, 2004, and 2003.

***Property and Equipment***

Property and equipment are stated at cost, net of accumulated depreciation and amortization. Depreciation and amortization is provided for both financial and income tax reporting purposes over the estimated useful lives of the assets ranging from three to seven years. Computer software, including licenses and internally developed software, is capitalized and amortized over lives ranging from three to five years, except that certain capitalized internally developed software is expensed for income tax reporting purposes. Depreciation is provided using the straight-line method for property. Leasehold improvements and facilities under capital leases are amortized over the terms of the related leases or their useful lives, whichever is shorter, whereas for income tax reporting purposes, they are amortized over the applicable tax lives. We periodically evaluate the carrying value of property and equipment based upon current and anticipated undiscounted cash flows, and recognize an impairment when it is probable that such estimated future cash flows will be less than the asset carrying value. We did not recognize any impairments in 2005, 2004, or 2003.

***Goodwill and Other Intangible Assets***

Our intangible assets consist of (1) goodwill, which is not amortized; (2) indefinite lived intangibles, which consist of certain trademarks that are not subject to amortization; and (3) amortizing intangibles, which consist of customer lists and a licensing agreement, which are being amortized over their useful lives. All intangible assets are subject to impairment tests on a periodic basis.

Note 2 describes SFAS No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"), and the annual impairment methodology that we employ on January 1 of each year in calculating the recoverability of goodwill. This same impairment test will be performed at other times during the course of a year should an event occur which suggests that the recoverability of goodwill should be challenged. Non-amortizing intangibles are also subject to annual impairment tests.

Amortizing intangibles are evaluated for impairment using the methodology set forth in SFAS No. 144, "Accounting for the Impairment or Disposal of Long-lived Assets." Recoverability of these assets is assessed only when events have occurred that may give rise to an impairment. When a potential impairment has been identified, forecasted undiscounted net cash flows of the operations to which the asset relates are compared to the current

## [Table of Contents](#)

carrying value of the long-lived assets present in that operation. If such cash flows are less than such carrying amounts, long-lived assets including such intangibles, are written down to their respective fair values.

### **Income Taxes**

Deferred income tax assets and liabilities are computed for differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future, based on anticipated tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount that is more likely than not to be realized.

Accruals for tax contingencies are recorded when certain positions taken in filed tax returns, although supported, are probable of being successfully challenged, resulting in additional tax liabilities. Accruals are not recorded for tax contingencies not likely to be successfully challenged. Such accruals are adjusted as necessary in light of changing facts and circumstances.

### **Concentrations**

Concentrations of credit risk with respect to trade account receivables are limited due to the large number of customers comprising our customer base. Ongoing credit evaluations of customers' financial condition are performed by management on a regular basis.

During the years ended December 31, 2005, 2004, and 2003, product purchases from Ingram Micro, Inc., our largest vendor, accounted for approximately 26%, 27%, and 22%, respectively, of our total product purchases. Purchases from Tech Data Corporation comprised 19%, 14%, and 15% of our total product purchases in 2005, 2004, and 2003, respectively. Purchases from Hewlett-Packard Company constituted 11%, 11%, and 15% of our total product purchases in 2005, 2004, and 2003, respectively. No other vendor supplied more than 10% of our total product purchases in 2005, 2004, or 2003.

No single customer, other than the federal government, accounted for more than 2% of total net sales in 2005. Net sales to the federal government in 2005, 2004, and 2003 were \$68,924, \$64,900, and \$156,600, or 4.8%, 4.8%, and 11.9% of total net sales, respectively.

### **Earnings Per Share**

Basic earnings per common share is computed using the weighted average number of shares outstanding. Diluted earnings per share is computed using the weighted average number of shares outstanding adjusted for the incremental shares attributed to options outstanding to purchase common stock, if dilutive.

The following table sets forth the computation of basic and diluted earnings per share:

	2005	2004	2003
<b>Numerator:</b>			
Net income	<u>\$ 4,447</u>	<u>\$ 8,304</u>	<u>\$ 5,888</u>
<b>Denominator:</b>			
Denominator for basic earnings per share	25,184	25,028	24,713
Dilutive effect of employee stock options	<u>97</u>	<u>241</u>	<u>401</u>
Denominator for diluted earnings per share	<u>25,281</u>	<u>25,269</u>	<u>25,114</u>
<b>Earnings per share:</b>			
Basic	<u>\$ .18</u>	<u>\$ .33</u>	<u>\$ .24</u>
Diluted	<u>\$ .18</u>	<u>\$ .33</u>	<u>\$ .23</u>

## [Table of Contents](#)

The following unexercised stock options were excluded from the computation of diluted earnings per share for years ended December 31, 2005, 2004, and 2003 because the exercise prices of the options were generally greater than the average market price of the common shares during the respective periods:

	2005	2004	2003
Anti-dilutive stock options	1,830	1,426	1,516

### **Stock-Based Compensation**

Compensation expense associated with awards of stock or options to employees and directors is measured using the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"). The intrinsic value method requires that compensation expense, if any, be measured by the difference between the fair value of our common stock and the strike price of the option as of a measurement date. This measurement date is generally when both the number of shares and the strike price of the options are determined. Information concerning the impact of the utilization of the fair market value model prescribed by SFAS 123, "Accounting for Stock-Based Compensation" ("SFAS 123") is shown below.

We recorded \$34 of compensation expense in 2005 under the intrinsic value method, but did not record any compensation expense in 2004 or 2003. The 2005 expense resulted from the acceleration of vesting of certain options discussed in Note 11. Had we recorded compensation expense using the fair value method under SFAS 123, pro forma net income and diluted net income per share for the years ended December 31 would have been as shown below. Of the 2005 pro forma compensation expense, approximately \$1,211, net of taxes, resulted from this vesting acceleration.

	2005	2004	2003
Net income, as reported	\$4,447	\$8,304	\$5,888
Compensation expense, net of taxes, included in net income as reported	19	—	—
Compensation expense, net of taxes, under SFAS 123	2,310	1,110	1,877
Net income, under SFAS 123	2,156	7,194	4,011
Basic net income per share, as reported	.18	.33	.24
Basic net income per share, under SFAS 123	.09	.29	.16
Diluted net income per share, as reported	.18	.33	.23
Diluted net income per share, under SFAS 123	.09	.28	.16

We measured the fair value of options on their grant date using the Black/Scholes option-pricing model. The key weighted-average assumptions we used to apply this pricing model were as follows:

	2005	2004	2003
Risk-free interest rates	3.99%	3.08%	3.20%
Volatility	81.0%	94.5%	68.6%
Expected life of option grants	5.0 years	4.0 years	4.0 years
Dividend yield	0%	0%	0%

### **Share Repurchase Authorization**

We announced on March 28, 2001, that our Board of Directors authorized the spending of up to \$15,000 to repurchase our common stock. Share purchases will be made in the open market from time to time depending on market conditions. We have repurchased an aggregate of 362,267 shares for \$2,286 as of December 31, 2005, which are reflected as treasury stock on the consolidated balance sheet. Our current bank line of credit dated June 29, 2005 limits additional repurchases to \$10,000 without bank approval of higher amounts.

### **Recently Issued Financial Accounting Standards**

In December 2004, the Financial Accounting Standards Board ("FASB") issued SFAS 123(R), "Share-Based Payment" ("SFAS 123(R)"). This Statement is a revision of SFAS 123 and supersedes APB 25 and its

## [Table of Contents](#)

related implementation guidance. SFAS 123(R) requires a company to measure the grant date fair value of equity awards given to employees in exchange for services and recognize that cost over the period that such services are performed. SFAS 123(R) is effective for the beginning of the first fiscal year after June 15, 2005 and will be effective for our interim quarter ending March 31, 2006. SFAS 123(R) allows the choice between two methods of adoption: the modified-prospective transition method and the modified-retrospective transition method. Adoption of SFAS 123(R) may materially increase stock compensation expense and decrease net income. In addition, SFAS 123(R) requires that the excess tax benefits related to stock compensation be reported as a cash inflow from financing activities rather than as a reduction of taxes paid in cash from operations. We have adopted the provisions of SFAS 123(R) effective January 1, 2006, using the modified prospective approach. See Note 11.

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections," ("SFAS 154") which is a replacement of APB Opinion No. 20, "Accounting Changes," and FASB Statement No. 3, "Reporting Accounting Changes in Interim Financial Statements." SFAS 154 changes the requirements for the accounting and reporting of accounting changes by requiring retrospective application to prior period financial statements unless impracticable. This statement is effective in fiscal years beginning after December 15, 2005.

## 2. GOODWILL AND OTHER INTANGIBLE ASSETS

We apply the provisions of SFAS 142 which required, among other things, the discontinuance of the amortization of goodwill and indefinite lived intangibles. SFAS 142 also includes provisions for the assessment of the value and useful lives of existing recognized intangibles (including goodwill), reclassification of certain intangibles both in and out of previously reported goodwill and the identification of reporting units for purposes of assessing potential future impairments of goodwill and other intangibles. We perform the assessment annually on January 1. We completed the impairment review required by SFAS 142 on January 1, 2006 and 2005, and determined that our goodwill and intangible assets were not impaired.

Intangible assets not subject to amortization are as follows:

	December 31,	
	2005	2004
Goodwill	\$ 56,820	\$ 51,687
Trademarks	1,190	1,190

A rollforward of goodwill is as follows:

Balance, January 1, 2003	\$33,704
Adjustment to MoreDirect acquisition	(62)
Adjustment to 2002 contingent consideration	29
MoreDirect contingent consideration	11,593
Balance, December 31, 2003	45,264
Adjustment to 2003 contingent consideration	(498)
MoreDirect contingent consideration	6,921
Balance, December 31, 2004	51,687
Amherst Technologies acquisition, October 21, 2005	5,133
Balance, December 31, 2005	<u>\$56,820</u>

Intangible assets subject to amortization at December 31, 2005 consisted of customer lists of \$3,815 and a licensing agreement of \$422 (net of accumulated amortization of \$1,405 and \$53, respectively). Intangible assets subject to amortization at December 31, 2004 consisted of customer lists of \$1,850 (net of accumulated amortization of \$970). The weighted-average amortization period of the customer list and licensing agreement acquired in the year ended December 31, 2005 was four years. For the years ended December 31, 2005, 2004, and 2003, we recorded amortization expense of \$489, \$353, and \$353, respectively.

## [Table of Contents](#)

The estimated amortization expense relating to customer lists and licensing agreements for each of the five succeeding years and thereafter is as follows:

<u>For the Year Ended December 31,</u>	
2006	\$ 1,065
2007	1,071
2008	1,071
2009	942
2010	88
2011 and thereafter	—

### 3. ACQUISITION OF MOREDIRECT, INC.

On April 5, 2002, we completed the acquisition of MoreDirect, Inc. Under the terms of the agreement, MoreDirect's shareholder continued to be eligible to earn additional consideration based upon MoreDirect achieving targeted levels of annual earnings before income taxes through December 31, 2004. For the years ended December 31, 2004, 2003, and 2002, we paid earn-out consideration owed to MoreDirect's shareholder of \$6,921, \$11,095, and \$10,829, respectively. The payment for the year ended December 31, 2004, made in April 2005, was the final payment required under this agreement.

### 4. PURCHASE OF CERTAIN ASSETS OF AMHERST TECHNOLOGIES, LLC

On October 21, 2005, we completed the acquisition of certain assets of Amherst Technologies, LLC and certain other parties (collectively, "Amherst") from IBM Credit, LLC ("IBM") for \$7,751 in cash. Prior to this transaction, IBM was granted a security interest by Amherst covering the acquired assets. The assets we acquired include customer relationships and related intangibles; intellectual property; and miscellaneous furniture, fixtures, and equipment. The acquired assets were combined with our MoreDirect, Inc. subsidiary to expand its reach into the medium-to-large corporate customer segment and enhance its sales efforts. We incurred an additional \$28 of costs directly related to the transaction.

The transaction was accounted for by the purchase method, and accordingly, any sales generated by former Amherst Technologies' sales representatives are included in our consolidated financial statements only for periods after October 21, 2005.

The following table summarizes the estimated fair values of the assets acquired at the date of acquisition. We did not assume any liabilities in this transaction. The fair values of certain intangible assets were determined by management, utilizing in part a third party valuation.

<u>At October 21, 2005</u>	
Intangible assets	\$2,400
Property, plant and equipment and other assets	246
Goodwill	5,133
Purchase price of selected assets	<u>\$7,779</u>

The \$2,400 of acquired intangible assets represents customer relationships (four-year weighted-average useful life). Goodwill of \$5,133 was assigned to our Large Account segment. All of this goodwill is expected to be deductible for income tax purposes as a result of this transaction.

## [Table of Contents](#)

### 5. ACCOUNTS RECEIVABLE

Accounts receivable consisted of the following:

	December 31,	
	2005	2004
Trade	\$ 160,058	\$ 119,797
Co-op advertising	3,086	2,837
Vendor returns, rebates, and other	5,065	3,579
Due from employees	209	165
Due from affiliates	23	—
Total	168,441	126,378
Less allowances for:		
Sales returns	2,288	1,493
Doubtful accounts	3,628	4,133
Accounts receivable, net	<u>\$ 162,525</u>	<u>\$ 120,752</u>

### 6. PROPERTY AND EQUIPMENT

Property and equipment consisted of the following:

	December 31,	
	2005	2004
Facilities and equipment under capital lease	\$ 8,447	\$ 8,447
Leasehold improvements	6,049	5,968
Furniture and equipment	27,815	25,415
Computer software, including licenses and internally-developed software	30,895	29,051
Automobiles	201	169
Total	73,407	69,050
Less accumulated depreciation and amortization	55,707	51,403
Property and equipment, net	<u>\$ 17,700</u>	<u>\$ 17,647</u>

We recorded depreciation and amortization expense, including capital lease amortization, of \$6,708, \$6,774, and \$8,074 for the years ended December 31, 2005, 2004, and 2003, respectively.

### 7. SPECIAL CHARGES

In 2005, we recorded a charge of \$1,056 related to the temporary retention of certain Amherst employees and facilities subsequent to the purchase of certain assets of Amherst Technologies. We also recorded in 2005 charges of \$1,071 related to management restructuring costs, classified as workforce reductions in the table below.

In 2004, we recorded a charge of \$3,559 related to our review of the General Services Administration (“GSA”) contract cancellation and costs related to securing a new schedule. We also recorded in 2004 a charge of \$860 related to staff reductions, a charge of \$512 for professional fees incurred relating to a review of certain calendar year 2000 and 2003 transactions, a charge of \$101 related to the remaining uninsured portion of a 2003 employee defalcation, and a charge of \$200 related to a proposed litigation settlement involving alleged patent infringement.

In 2003, we recorded a charge of \$407 related to staff reductions, a charge of \$392 related to the GSA contract cancellation, and a charge of \$1,130 related to the uninsured portion of an employee defalcation.

## [Table of Contents](#)

A rollforward of special charges for the three years in the period ended December 31, 2005 is shown below. There were no significant changes in estimates in the interim periods.

	<u>Workforce Reduction</u>	<u>Amherst Technologies</u>	<u>GSA Review</u>	<u>Employee Defalcation</u>	<u>Other</u>	<u>Total</u>
Balance, January 1, 2003	\$ 208	\$ —	\$ —	\$ —	\$ —	\$ 208
Charges	407	—	392	1,130	—	1,929
Cash Payments	(502)	—	(155)	(1,130)	—	(1,787)
Balance, December 31, 2003	113	—	237	—	—	350
Charges	860	—	3,559	101	712	5,232
Cash payments	(724)	—	(3,072)	(101)	(497)	(4,394)
Balance, December 31, 2004	249	—	724	—	215	1,188
Charges	1,071	1,056	—	—	—	2,127
Cash payments	(454)	(924)	(724)	—	(200)	(2,302)
Adjustments	—	—	—	—	(15)	(15)
Liabilities at December 31, 2005	<u>\$ 866</u>	<u>\$ 132</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 998</u>

Liabilities at December 31, 2005 and 2004 are included in accrued expenses and other liabilities on the balance sheet.

## 8. BANK BORROWINGS

On June 29, 2005, we secured from our current bank an increased \$50,000 credit facility collateralized by substantially all of our business assets. This facility also gives us the option of increasing the borrowing amount by an additional \$20,000 at substantially the same terms. Amounts outstanding under this facility bear interest at the prime rate (7.25% at December 31, 2005). The facility also gives us the option of obtaining Eurodollar Rate Loans in multiples of \$1,000 for durations of one, two, three, four, or six months. The credit facility includes various customary financial and operating covenants, including minimum net worth and maximum funded debt ratio requirements, and restrictions on the payment of dividends, repurchase of our common stock, and default acceleration provisions, none of which we believe significantly restricts our operations. The maximum allowable funded debt ratio under the agreement is 2.0 to 1.0; our actual funded debt ratio at December 31, 2005 was 1.2 to 1.0. Funded debt ratio is the ratio of average outstanding advances under the facility to EBITDA (Earnings Before Interest Expense, Taxes, Depreciation, and Amortization). Borrowing availability under the agreement was \$30,025 at December 31, 2005.

Borrowings of \$19,975 and \$4,810 were outstanding under this credit facility at December 31, 2005 and 2004, respectively. A total of \$17,000 of the December 31, 2005 outstanding borrowings consisted of three-month and one-month Eurodollar Rate Loans of \$10,000 at 5.11% interest and \$7,000 at 5.36% interest, respectively. The credit facility matures on June 29, 2008, at which time amounts outstanding become due.

Certain information with respect to short-term borrowings was as follows:

<u>Year ended December 31,</u>	<u>Weighted Average Interest Rate</u>	<u>Maximum Amount Outstanding</u>	<u>Average Amount Outstanding</u>
2005	6.5%	\$ 34,053	\$ 7,460
2004	4.3	22,441	9,447
2003	4.1	27,623	5,452

## 9. TRADE CREDIT AGREEMENTS

At December 31, 2005 and 2004, we had security agreements with two financial institutions to facilitate the purchase of inventory from various suppliers under certain terms and conditions. The agreements allow a collateralized position in inventory financed by the financial institutions up to an aggregated amount of \$45,000. The cost of such financing under these agreements is borne by the suppliers by discounting their invoices to the financial institutions as an incentive for us to purchase their products. We do not pay any interest or discount fees on such inventory financing. At December 31, 2005 and 2004, accounts payable included \$12,316 and \$8,215, respectively, owed to these financial institutions.

## 10. CAPITAL LEASE

In November 1997, we entered into a fifteen-year lease for our corporate headquarters with an affiliated company related to us through common ownership. We occupied the facility upon completion of construction in late November 1998, and the lease payments commenced in December 1998.

Annual lease payments under the terms of the lease, as amended, are approximately \$911 for the first five years of the lease, increasing to \$1,025 for years six through ten and \$1,139 for years eleven through fifteen. The lease requires us to pay our proportionate share of real estate taxes and common area maintenance charges as additional rent and also to pay insurance premiums for the leased property. We have the option to renew the lease for two additional terms of five years each. The lease has been recorded as a capital lease.

In December 2004, we entered into a sale-leaseback transaction with a three-year lease for certain computer equipment. The cost of the leased equipment included in furniture and equipment was approximately \$1,232. Annual lease payments under the terms of the lease are approximately \$442 for each of the three years. At the termination of the lease we have the option of either continuing the lease at the current rate, returning the equipment, or purchasing the equipment at fair market value.

The net book value of capital lease assets was \$4,655 and \$5,521 as of December 31, 2005 and 2004, respectively.

Future aggregate minimum annual lease payments under these leases at December 31, 2005 are as follows:

<u>Year Ending December 31</u>	<u>Payments</u>
2006	\$ 1,467
2007	1,430
2008	1,035
2009	1,139
2010	1,139
2011 and thereafter	3,323
Total minimum payments (excluding taxes, maintenance, and insurance)	9,533
Less amount representing interest	3,010
Present value of minimum lease payments	6,523
Less current maturities (excluding interest)	828
Long-term portion	<u>\$ 5,695</u>

## 11. STOCKHOLDERS' EQUITY

### *Preferred Stock*

Our Amended and Restated Certificate of Incorporation (the "Restated Certificate") authorized the issuance of up to 10,000 shares of preferred stock, \$.01 par value per share (the "Preferred Stock"). Under the terms of the Restated Certificate, the Board is authorized, subject to any limitations prescribed by law, without stockholder



## [Table of Contents](#)

approval, to issue by a unanimous vote such shares of Preferred Stock in one or more series. Each such series of Preferred Stock shall have such rights, preferences, privileges, and restrictions, including voting rights, dividend rights, redemption privileges, and liquidation preferences, as shall be determined by the Board. There were no preferred shares outstanding at 2005 and 2004.

### **Incentive and Non-Statutory Stock Option Plans**

In December 1993, the Board adopted and the stockholders approved the 1993 Incentive and Non-Statutory Stock Option Plan (the "1993 Plan"). Under the terms of the 1993 Plan, we are authorized to make awards of restricted stock and to grant incentive and non-statutory options to our employees, consultants, and advisors to purchase shares of our stock. A total of 1,686 shares of our Common Stock was authorized for issuance upon exercise of options granted or awards made under the 1993 Plan. Options vested over varying periods up to four years and had contractual lives up to ten years.

In November 1997, the Board adopted and the stockholders approved the 1997 Stock Incentive Plan (the "1997 Plan"), which became effective on the closing of our initial public offering in 1998. The 1997 Plan provides for the grant of incentive stock options, non-statutory stock options, stock appreciation rights, performance shares, and awards of restricted stock and unrestricted stock. A total of 3,600 shares have been reserved for issuance under this Plan.

Information regarding the 1993 and 1997 Plans is as follows:

	<u>Option Shares</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Fair Value</u>
Outstanding, January 1, 2003	2,550	\$ 12.29	
Granted	1,070	6.74	\$ 3.63
Exercised	(257)	8.59	
Forfeited and cancelled	(636)	13.56	
Outstanding, December 31, 2003	2,727	10.78	
Granted	260	7.85	4.55
Exercised	(46)	9.06	
Forfeited and cancelled	(594)	9.59	
Outstanding, December 31, 2004	2,347	10.90	
Granted	635	6.46	4.21
Exercised	(96)	6.76	
Forfeited and cancelled	(344)	13.25	
Outstanding, December 31, 2005	<u>2,542</u>	9.74	

The following table summarizes the status of outstanding stock options as of December 31, 2005:

Exercise Price Range	Options Outstanding			Options Exercisable	
	No. of Shares	Weighted Average Remaining Life (Years)	Weighted Average Exercise Price	No. of Shares	Weighted Average Exercise Price
\$3.81—\$6.95	871	8.06	\$ 5.35	629	\$ 5.31
\$7.10—\$9.98	877	6.55	7.97	674	8.02
\$10.01—\$14.35	588	4.01	11.21	563	11.26
\$15.25—\$34.83	132	4.21	19.89	132	19.89
\$51.81—\$52.75	74	4.56	52.02	74	52.02
<u>\$ 3.81—\$52.75</u>	<u>2,542</u>	<u>6.28</u>	<u>\$ 9.74</u>	<u>2,072</u>	<u>\$ 10.42</u>

## [Table of Contents](#)

Total exercisable options and their weighted average exercise price at December 31, 2004 and 2003 were 1,342 shares at \$13.65 and 1,204 shares at \$13.92, respectively.

The Board of Directors approved on December 30, 2005 the acceleration of the vesting of the following outstanding options: (1) all unvested options from grants of 20 shares or more held by officers that would otherwise vest in 2006, (2) all “market condition” options (those options whose vesting depends upon reaching certain stock prices), held by officers, and (3) all other options from grants of less than 20 shares held by directors, officers and other employees. The vesting of options to purchase approximately 743 shares of common stock with exercise prices ranging from \$4.73 to \$10.53 per share, with a weighted average exercise price of approximately \$6.98 per share, was accelerated. All other terms and conditions of the original option grants remain unchanged. Vesting was not accelerated for options held by officers to purchase approximately 470 shares. The primary purpose of this decision to accelerate vesting was to avoid recognizing stock-based compensation associated with these options that would be required under SFAS 123(R) when adopted in 2006, a substantial portion of which is “out-of-the-money.” This acceleration is consistent with expected changes to our overall compensation approach which going forward will rely less heavily on stock options.

We recorded compensation expense of \$34 related to this acceleration in the fourth quarter of 2005, which amount represents the additional intrinsic value under APB 25 of those options whose vesting was accelerated. The estimated future compensation expense for those options that would have been recorded had such vesting not been accelerated, based on adopting SFAS 123(R) on January 1, 2006, was approximately \$1,388. For the years 2006 through 2009, we expect to record \$562, \$474, \$341, and \$121, respectively, for the remaining unvested options held by officers from grants greater than 20 shares. If we should make any grants of stock options or of a similar type vehicle, we will, under SFAS 123(R), be required to recognize the expense associated with the vesting of the vehicles in the periods reported.

### **1997 Employee Stock Purchase Plan**

In November 1997, the Board adopted and the stockholders approved the 1997 Employee Stock Purchase Plan (the “Purchase Plan”), which became effective on February 1, 1999. The Purchase Plan authorizes the issuance of common stock to participating employees. On December 30, 2005, the Board modified the Purchase Plan after reviewing the impact of SFAS 123(R) on compensation expense related to the discounted purchase by employees of common stock. Previously under the Purchase Plan, employees were permitted to purchase company stock at a price of 85% of the lesser of the fair market value per share of common stock on either the first or last business day of the six-month offering period. Effective January 1, 2006, our employees may purchase company stock at 95% of the purchase price as of the last business day of the six-month period. This modification will permit us to avoid recognition of stock compensation expense associated with the purchase of common stock under our Purchase Plan. An aggregate of 838 shares of common stock has been reserved for issuance under the Purchase Plan, of which 645 shares were purchased.

## **12. INCOME TAXES**

The provision for income taxes consisted of the following:

	Years Ended December 31,		
	2005	2004	2003
<b>Paid or currently payable:</b>			
Federal	\$3,127	\$3,985	\$4,108
State	667	(60)	630
Total current	3,794	3,925	4,738
<b>Deferred:</b>			
Federal	(125)	600	(697)
State	14	31	(191)
Net deferred	(111)	631	(888)
Net provision	<u>\$3,683</u>	<u>\$4,556</u>	<u>\$3,850</u>

## Table of Contents

The components of the deferred taxes at December 31, 2005 and 2004 are as follows:

	<u>2005</u>	<u>2004</u>
<b>Current:</b>		
Provisions for doubtful accounts	\$ 1,419	\$ 1,571
Inventory costs capitalized for tax purposes	285	274
Inventory and sales returns reserves	773	556
Deductible expenses, primarily employee-benefit related	326	126
State tax contingency and other accruals	273	—
Other	693	512
Net deferred tax asset—current	<u>\$ 3,769</u>	<u>\$ 3,039</u>
<b>Non-Current:</b>		
Compensation under non-statutory stock option agreements	\$ 21	\$ 37
Tax effect of state tax loss carryforwards	1,032	834
State tax credit carryforwards	1,780	1,465
Excess of book value over the tax basis of goodwill and other intangibles	(4,006)	(2,528)
Excess of book value over the tax basis of property and equipment	(720)	(1,595)
Subtotal	<u>(1,893)</u>	<u>(1,787)</u>
Valuation allowance	<u>(2,212)</u>	<u>(1,699)</u>
Net deferred tax liability—non-current	<u>(4,105)</u>	<u>(3,486)</u>
Net deferred tax liability	<u>\$ (336)</u>	<u>\$ (447)</u>

The state tax credit carryforwards are available to offset future state income taxes in years with sufficient state income levels to create creditable tax and within the applicable carryforward period for these credits. Total tax credit carryforwards aggregated \$1,780 and \$1,465 at December 31, 2005 and 2004, respectively. These credits are subject to a five-year carryforward period, with \$150 expiring beginning in 2006 and \$450, \$415, \$450, and \$315 expiring respectively on an annual basis through 2010. Additionally, certain of our subsidiaries have operating loss carryforwards aggregating \$18,972 at December 31, 2005 and representing state tax benefits, net of federal taxes, of approximately \$1,032. These loss carryforwards are subject to five- and twenty-year carryforward periods, with \$191, \$134, \$151, \$64, and \$56 expiring from 2006 through 2010, respectively, and \$436 expiring after 2020. We have provided valuation allowances of \$2,212 and \$1,699 at December 31, 2005 and 2004, respectively, against the state tax credit and state tax loss carryforwards, representing the portion of carryforward credits that we believe is not likely to be realized due to these restrictions.

The reconciliation of our 2005, 2004, and 2003 income tax provision to the statutory federal tax rate is as follows:

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Statutory tax rate	35.0%	35.0%	35.0%
State income taxes, net of federal benefit	5.2	3.5	4.5
State tax loss carryforwards	(5.1)	(2.6)	(1.9)
Less valuation allowance	5.1	2.6	1.9
Prior year tax matters	—	(3.5)	—
Nondeductible expenses	3.2	0.4	0.1
Other—net	1.9	—	(0.1)
Effective income tax rate	<u>45.3%</u>	<u>35.4%</u>	<u>39.5%</u>

We have established accruals for certain state and federal tax contingencies when, despite our belief that our tax return positions are fully supported, we believe that certain positions are probable of being successfully challenged. These accruals relate primarily to various state tax jurisdictional issues concerning the nature and extent of our operations and activities in those states.

## [Table of Contents](#)

The tax contingency accruals are adjusted in light of changing facts and circumstances. Total tax contingency reserves were \$1,131 and \$1,197 at December 31, 2005 and 2004, respectively. These reserves were decreased in 2005 by \$66 due to the settlement of a federal income tax audit without assessment and by \$152 due to the reduced exposure to state transfer pricing taxes, partially offset by increases of \$152 due to other state tax exposures. The tax contingency reserves were decreased in 2004 by \$229 due to reduced state income tax jurisdictional exposures and by \$293 due to reduced federal income tax audit exposures for earlier tax years. The reserves were increased in 2003 by \$143 due to estimated increases in certain other state tax contingencies.

### 13. EMPLOYEE BENEFIT PLAN

We have a contributory profit-sharing and employee savings plan covering all qualified employees. No contributions to the profit-sharing element of the plan were made by us in 2005, 2004, or 2003. We made matching contributions to the employee savings element of the plan of \$662, \$653, and \$602 in 2005, 2004, and 2003, respectively.

### 14. COMMITMENTS AND CONTINGENCIES

#### *Operating Leases*

We lease certain office facilities from our principal stockholders under 20-year noncancelable operating leases. The lease agreement for one facility requires us to pay all real estate taxes and insurance premiums related thereto. We also lease several other buildings from our principal stockholders on a month-to-month basis.

In addition, we lease office, distribution facilities, and equipment from unrelated parties with remaining terms of one to six years.

Future aggregate minimum annual lease payments under these leases at December 31, 2005 are as follows:

<u>Year Ending December 31</u>	<u>Related Parties</u>	<u>Others</u>	<u>Total</u>
2006	\$ 158	\$2,441	\$2,599
2007	154	1,775	1,929
2008	89	1,457	1,546
2009	—	866	866
2010	—	154	154
2011 and thereafter	—	—	—

Total rent expense aggregated \$3,413, \$4,905, and \$4,952 for the years ended December 31, 2005, 2004, and 2003, respectively, under the terms of the leases described above. Such amounts included \$157, \$147, and \$147 in 2005, 2004, and 2003, respectively, paid to related parties.

#### *Contingencies*

We are subject to various legal proceedings and claims which have arisen during the ordinary course of business. These claims include certain patent infringement litigation naming us and several other resellers as well as certain manufacturers of products we sell or use in our business. No specific amounts have been claimed as damages. In the opinion of management, the outcome of such matters is not expected to have a material effect on our financial position, results of operations, and cash flows.

We are also subject to audit by various government agencies relating to sales under certain government contracts. An audit was conducted on our GSA contract for the period May 1, 1997 to March 31, 2002, and in November 2003, the GSA's contract with our subsidiary, GovConnection, was cancelled. Management has concluded that such cancellation was precipitated by an audit of contractual compliance, although we have not received an audit report or received a claim from the GSA concerning amounts that might be owed pursuant to this audit. A new GSA contract was awarded in August 2004.

## [Table of Contents](#)

Based on our own internal review of contractual compliance, we have noted that several internal control deficiencies have existed at GovConnection surrounding its compliance with the GSA contract. Actions have been taken to address these deficiencies. We believe that we have provided adequate reserves to cover any claims as they relate to payment of fees required under the contract or any penalties assessed. We have reserved \$1.1 million for such fees or any penalties assessed. However, we will continue to evaluate such reserves in light of additional information that comes to our attention.

We have been informally advised that audit matters related to GovConnection have been referred to the Department of Justice for its review. Such a referral exposes us to possible civil damages for non-compliance with the GSA contract. Such damages can be substantial. No reserves have been provided for such a claim because of the preliminary nature of this matter. We will continue to evaluate our reserves—as they relate both to the GSA audit and the Department of Justice investigation—in light of additional information that comes to our attention. The ultimate outcome of these matters cannot be determined. Future events may result in conclusions that could have a material impact, either positively or negatively, on our results of operations or financial condition. We have no indication of intentional wrongdoing by GovConnection regarding the GSA contract. In order to assist in this evaluation, we engaged outside counsel and an independent accounting firm to review our systems, policies, and procedures relative to our federal, state, and local government contracts and to assist us in resolving this matter.

### 15. OTHER RELATED-PARTY TRANSACTIONS

As described in Notes 10 and 14, we have leased certain facilities from related parties. Other related-party transactions include the transactions summarized below. Related parties consist primarily of affiliated companies related to us through common ownership.

	Years Ended December 31		
	2005	2004	2003
Revenue:			
Sales of services to affiliated companies	\$ 82	\$ 74	\$ 65

### 16. SEGMENT AND RELATED DISCLOSURES

SFAS No. 131, “Disclosures About Segments of an Enterprise and Related Information,” requires that public companies report profits and losses and certain other information on their “reportable operating segments” in their annual and interim financial statements. The internal organization used by our Chief Operating Decision Maker (CODM) to assess performance and allocate resources determines the basis for our reportable operating segments. Our CODM is our Chief Executive Officer.

Our operations are organized under three reportable operating segments—the “SMB” segment, which serves small- and medium-sized businesses as well as consumers; the “Large Account” segment, acquired in April 2002, which serves medium-to-large corporations; and the “Public Sector” segment, which serves federal, state and local government organizations, and educational institutions.

[Table of Contents](#)

Segment information applicable to our reportable operating segments for the years ended December 31, 2005, 2004, and 2003 is shown below:

	Year Ended December 31, 2005				
	SMB Segment	Large Acct. Segment	Public Sector Segment	Eliminations	Consolidated
Sales to external customers	\$ 834,618	\$ 347,508	\$ 262,171	\$ —	\$ 1,444,297
Transfers between segments	243,716	—	—	(243,716)	—
Net sales	<u>\$ 1,078,334</u>	<u>\$ 347,508</u>	<u>\$ 262,171</u>	<u>\$ (243,716)</u>	<u>\$ 1,444,297</u>
Operating income (loss) before allocations	\$ 53,249	\$ 18,140	\$ 4,974	\$ (66,875)	\$ 9,488
Allocations	50,223	1,390	15,262	(66,875)	—
Operating income (loss)	3,026	16,750	(10,288)	—	9,488
Interest and other — net	(1,135)	49	(272)	—	(1,358)
Income (loss) before taxes	<u>\$ 1,891</u>	<u>\$ 16,799</u>	<u>\$ (10,560)</u>	<u>\$ —</u>	<u>\$ 8,130</u>
<b>Selected Operating Expenses:</b>					
Depreciation and amortization	\$ 6,241	\$ 824	\$ 132	\$ —	\$ 7,197
Special charges	1,876	—	251	—	2,127
<b>Balance Sheet Data:</b>					
Total assets	\$ 225,870	\$ 120,552	\$ 63,324	\$ (72,041)	\$ 337,705
Goodwill, net	1,173	48,013	7,634	—	56,820

	Year Ended December 31, 2004				
	SMB Segment	Large Acct. Segment	Public Sector Segment	Eliminations	Consolidated
Sales to external customers	\$ 802,303	\$ 298,458	\$ 253,073	\$ —	\$ 1,353,834
Transfers between segments	224,114	—	—	(224,114)	—
Net sales	<u>\$ 1,026,417</u>	<u>\$ 298,458</u>	<u>\$ 253,073</u>	<u>\$ (224,114)</u>	<u>\$ 1,353,834</u>
Operating income (loss) before allocations	\$ 58,103	\$ 16,217	\$ 2,746	\$ (62,973)	\$ 14,093
Allocations	46,856	1,615	14,502	(62,973)	—
Operating income (loss)	11,247	14,602	(11,756)	—	14,093
Interest and other — net	(987)	39	(285)	—	(1,233)
Income (loss) before taxes	<u>\$ 10,260</u>	<u>\$ 14,641</u>	<u>\$ (12,041)</u>	<u>\$ —</u>	<u>\$ 12,860</u>
<b>Selected Operating Expenses:</b>					
Depreciation and amortization	\$ 6,306	\$ 706	\$ 115	\$ —	\$ 7,127
Special charges	1,389	225	3,618	—	5,232
<b>Balance Sheet Data:</b>					
Total assets	\$ 197,914	\$ 93,178	\$ 54,116	\$ (58,666)	\$ 286,542
Goodwill, net	1,173	42,880	7,634	—	51,687

[Table of Contents](#)

	Year Ended December 31, 2003				
	<u>SMB Segment</u>	<u>Large Acct. Segment</u>	<u>Public Sector Segment</u>	<u>Eliminations</u>	<u>Consolidated</u>
Sales to external customers	\$ 744,396	\$ 247,873	\$ 320,622	\$ —	\$ 1,312,891
Transfers between segments	245,466	—	—	(245,466)	—
Net sales	<u>\$ 989,862</u>	<u>\$ 247,873</u>	<u>\$ 320,622</u>	<u>\$ (245,466)</u>	<u>\$ 1,312,891</u>
Operating income (loss) before allocations	\$ 49,151	\$ 14,270	\$ 9,840	\$ (62,335)	\$ 10,926
Allocations	48,511	1,397	12,427	(62,335)	—
Operating income (loss)	640	12,873	(2,587)	—	10,926
Interest and other — net	(1,002)	16	(202)	—	(1,188)
Income (loss) before taxes	<u>\$ (362)</u>	<u>\$ 12,889</u>	<u>\$ (2,789)</u>	<u>\$ —</u>	<u>\$ 9,738</u>
<u>Selected Operating Expenses:</u>					
Depreciation and amortization	\$ 7,595	\$ 682	\$ 86	\$ —	\$ 8,363
Special charges	421	1,116	392	—	1,929
<u>Balance Sheet Data:</u>					
Total assets	\$ 202,778	\$ 96,237	\$ 93,241	\$ (81,651)	\$ 310,605
Goodwill, net	1,173	36,457	7,634	—	45,264

General and administrative expenses were charged to the reportable operating segments, based on their estimated usage of the underlying functions. Interest and other expense was charged to the segments, based on the actual costs incurred by each segment, net of interest and other income generated. The amount shown above representing total assets eliminated consists of inter-segment receivables, resulting primarily from inter-segment sales and transfers reported above and from inter-segment service charges.

Senior management also monitors revenue by sales channel (Outbound Telemarketing and Field Sales, Inbound Telesales, and Online Internet) and product mix (Notebooks and PDAs; Desktops and Servers; Storage Devices; Software; Net/Com Products; Printers and Printer Supplies; Video, Imaging, and Sound; Memory and System Enhancements; and Accessories/Other).

[Table of Contents](#)

Net sales by segment, sales channel, and product mix are presented below:

	Years Ended December 31,		
	2005	2004	2003
<b>Segment (excludes transfers between segments)</b>			
SMB	\$ 834,618	\$ 802,303	\$ 744,396
Large Account	347,508	298,458	247,873
Public Sector	262,171	253,073	320,622
Total	<u>\$ 1,444,297</u>	<u>\$ 1,353,834</u>	<u>\$ 1,312,891</u>
<b>Sales Channel</b>			
Outbound Telemarketing and Field Sales	\$ 990,249	\$ 992,955	\$ 1,007,758
Inbound Telesales	71,104	85,481	93,056
Online Internet	382,944	275,398	212,077
Total	<u>\$ 1,444,297</u>	<u>\$ 1,353,834</u>	<u>\$ 1,312,891</u>
<b>Product Mix</b>			
Notebooks and PDAs	\$ 265,562	\$ 276,208	\$ 261,540
Desktop/Servers	208,596	192,563	193,560
Storage Devices	123,360	110,442	116,785
Software	173,952	162,575	144,843
Net/Com Products	114,107	98,522	103,995
Printers and Printer Supplies	150,824	149,211	149,302
Video, Imaging, and Sound	179,035	164,933	154,268
Memory and System Enhancements	75,489	71,480	75,109
Accessories/Other	153,372	127,900	113,489
Total	<u>\$ 1,444,297</u>	<u>\$ 1,353,834</u>	<u>\$ 1,312,891</u>

Substantially, all of our net sales in 2005, 2004, and 2003 were made to customers located in the United States. Shipments to customers located in foreign countries aggregated less than 2% in 2005, 2004, and 2003. All of our assets at December 31, 2005 and 2004 were located in the United States. Our primary target customers are SMBs comprised of 20 to 1,000 employees, federal, state, and local governmental agencies, educational institutions, and medium-to-large corporate accounts. No single customer other than the federal government accounted for more than 2% of total net sales in 2005. Net sales to the federal government in 2005, 2004, and 2003 were \$68,924, \$64,900, and \$156,600, or 4.8%, 4.8%, and 11.9% of total net sales, respectively.



## 17. SELECTED UNAUDITED QUARTERLY FINANCIAL RESULTS

The following table sets forth certain unaudited quarterly data of the Company for each of the quarters since January 2004. This information has been prepared on the same basis as the annual financial statements and all necessary adjustments, consisting only of normal recurring adjustments, have been included in the amounts stated below to present fairly the selected quarterly information when read in conjunction with the annual financial statements and the notes thereto included elsewhere in this document. The quarterly operating results are not necessarily indicative of future results of operations. See “Factors That May Affect Future Results and Financial Condition” in Item 1A of this Annual Report on Form 10-K for the year ended December 31, 2005.

	Quarters Ended			
	March 31, 2005	June 30, 2005	Sept. 30, 2005	Dec. 31, 2005
Net sales	\$323,851	\$350,710	\$371,124	\$398,612
Cost of sales	286,517	310,346	329,044	354,794
Gross profit	37,334	40,364	42,080	43,818
Selling, general, and administrative expenses	35,416	37,379	37,531	41,655
Special charges	—	—	853	1,274
Income from operations	1,918	2,985	3,696	889
Interest expense	(272)	(285)	(289)	(601)
Other, net	(25)	50	25	39
Income before income taxes	1,621	2,750	3,432	327
Income tax provision	(673)	(1,186)	(1,508)	(316)
Net income	\$ 948	\$ 1,564	\$ 1,924	\$ 11
Weighted average common shares outstanding:				
Basic	25,127	25,157	25,224	25,226
Diluted	25,362	25,211	25,271	25,290
Earnings per common share:				
Basic	\$ .04	\$ .06	\$ .08	\$ .00
Diluted	\$ .04	\$ .06	\$ .08	\$ .00

	Quarters Ended			
	March 31, 2004	June 30, 2004	Sept. 30, 2004	Dec. 31, 2004
Net sales	\$327,635	\$335,335	\$351,265	\$339,599
Cost of sales	293,710	299,173	311,859	297,038
Gross profit	33,925	36,162	39,406	42,561
Selling, general, and administrative expenses	30,690	31,483	32,765	37,791
Special charges	1,030	753	1,800	1,649
Income from operations	2,205	3,926	4,841	3,121
Interest expense	(384)	(341)	(334)	(326)
Other, net	47	54	35	16
Income before income taxes	1,868	3,639	4,542	2,811
Income tax provision	(710)	(1,383)	(1,725)	(738)
Net income	\$ 1,158	\$ 2,256	\$ 2,817	\$ 2,073
Weighted average common shares outstanding:				
Basic	24,998	25,008	25,047	25,057
Diluted	25,356	25,225	25,215	25,271
Earnings per common share:				
Basic	\$ .05	\$ .09	\$ .11	\$ .08
Diluted	\$ .05	\$ .09	\$ .11	\$ .08

**18. SUBSEQUENT EVENT**

On March 30, 2006, Robert F. Wilkins, Executive Vice President, resigned from the Company. The Company intends to enter into a separation agreement under which Mr. Wilkins will receive a total of \$430, payable in equal bi-weekly payments over a period of 52 weeks. A copy of Mr. Wilkins's employment agreement was filed previously by the Company with the Securities and Exchange Commission.

Mr. Wilkins will be retained as a consultant by the Company following his separation. Under the terms of the consulting agreement, Mr. Wilkins will earn between \$264 and \$304 over a period of one year.

**PC CONNECTION, INC. AND SUBSIDIARIES**  
**SCHEDULE II—VALUATION AND QUALIFYING ACCOUNTS**  
*(amounts in thousands)*

<u>Description</u>	<u>Balance at Beginning of Period</u>	<u>Charged to Costs and Expenses</u>	<u>Deductions- Write-Offs</u>	<u>Balance at End of Period</u>
<b>Allowance for Sales Returns</b>				
Year Ended December 31, 2003	\$ 1,467	\$ 34,174	\$ (34,121)	\$ 1,520
Year Ended December 31, 2004	1,520	32,892	(32,919)	1,493
Year Ended December 31, 2005	1,493	34,081	(33,286)	2,288
<b>Allowance for Doubtful Accounts</b>				
Year Ended December 31, 2003	5,142	2,953 <sup>(1)</sup>	(3,966)	4,129
Year Ended December 31, 2004	4,129	4,279 <sup>(1)</sup>	(4,275)	4,133
Year Ended December 31, 2005	4,133	3,986 <sup>(1)</sup>	(4,491)	3,628
<b>Inventory Valuation Reserve</b>				
Year Ended December 31, 2003	1,270	5,889	(5,699)	1,460
Year Ended December 31, 2004	1,460	5,636	(5,861)	1,235
Year Ended December 31, 2005	1,235	6,119	(5,805)	1,549

<sup>(1)</sup> Additions to the provision for doubtful accounts include charges to advertising and cost of sales aggregating \$1,321, \$1,878, and \$(104), for the years ended December 31, 2005, 2004, and 2003 respectively. Such allowances relate to receivables under cooperative arrangements with vendors.

## PC CONNECTION, INC.

## 1997 EMPLOYEE STOCK PURCHASE PLAN, AS AMENDED

The purpose of this Plan is to provide eligible employees of PC Connection, Inc., a Delaware corporation (the "Company"), and certain of its U.S. subsidiaries with opportunities to purchase shares of the Company's common stock, \$.01 par value per share (the "Common Stock"), commencing on January 1, 1999. Eight Hundred Thirty-Seven Thousand Five Hundred (837,500) shares of Common Stock in the aggregate have been reserved for this purpose.

1. Administration. The Plan will be administered by the Company's Board of Directors (the "Board") or by the Compensation Committee appointed by the Board (the "Committee"). The Board or the Committee has authority to make rules and regulations for the administration of the Plan, to determine any brokerage and other fees to be paid or subsidized by the Company, and to determine the number of shares in each Offering; its interpretation and decisions with regard thereto shall be final and conclusive.

2. Eligibility. Participation in the Plan will neither be permitted nor denied contrary to the requirements of Section 423 of the Internal Revenue Code of 1986, as amended (the "Code"), and regulations promulgated thereunder. All employees of the Company, including Directors who are employees, and all employees of any subsidiary of the Company (as defined in Section 424(f) of the Code) designated by the Board or the Committee from time to time (a "Designated Subsidiary"), are eligible to participate in any one or more of the offerings of Options (as defined in Section 9) to purchase Common Stock under the Plan provided that:

(a) they are customarily employed by the Company or a Designated Subsidiary for more than 20 hours a week and for more than five months in a calendar year; and

(b) they have been employed by the Company or a Designated Subsidiary for at least six months prior to enrolling in the Plan; and

(c) they are employees of the Company or a Designated Subsidiary on the first day of the applicable Plan Period (as defined below).

No employee may be granted an option hereunder if such employee, immediately after the option is granted, owns 5% or more of the total combined voting power or value of the stock of the Company or any subsidiary. For purposes of the preceding sentence, the attribution rules of Section 424(d) of the Code shall apply in determining the stock ownership of an employee, and all stock which the employee has a contractual right to purchase shall be treated as stock owned by the employee.

3. Offerings. The Company will make one or more offerings (each, an "Offering") to employees to purchase shares of Common Stock under this Plan. Offerings will begin each January 1 and July 1, or the first business day thereafter (the "Offering Commencement Dates"). Each Offering Commencement Date will begin a six-month or one-year period (a "Plan Period")

during which payroll deductions will be made and held for the purchase of Common Stock at the end of the Plan Period.

4. Participation. An employee eligible on the Offering Commencement Date of any Offering may participate in such Offering by completing and forwarding a payroll deduction authorization form to the employee's appropriate payroll office, or in any other manner determined to be appropriate by the Board or the Committee ("Appropriate Authorization"), at least ten (10) days prior to the applicable Offering Commencement Date. The Appropriate Authorization will authorize a regular payroll deduction from the Compensation received by the employee during the Plan Period. Unless an employee notifies the Company of a new Appropriate Authorization or withdraws from the Plan, his deductions and purchases will continue at the same rate for future Offerings under the Plan as long as the Plan remains in effect. The term "Compensation" means the amount of money reportable on the employee's Federal Income Tax Withholding Statement, excluding allowances and reimbursements for expenses such as relocation allowances, travel expenses, income or gains on the exercise of Company stock options or stock appreciation rights, whether or not shown on the employee's Federal Income Tax Withholding Statement, but including, in the case of salespersons, sales commissions.

5. Deductions. The Company will maintain payroll deduction accounts for all participating employees. With respect to any Offering made under this Plan, an employee may authorize a payroll deduction in any dollar amount up to a maximum of 10% of the Compensation he receives during the Plan Period. In no event may an employee's total payroll deductions during a calendar year exceed \$20,000. The minimum payroll deduction is such percentage of Compensation as may be established from time to time by the Board or the Committee.

No employee may be granted an Option (as defined in Section 9) which permits his rights to purchase Common Stock under this Plan and any other employee stock purchase plan (as defined in Section 423(b) of the Code) of the Company and its subsidiaries, to accrue at a rate which exceeds \$25,000 of the fair market value of such Common Stock (determined as of the last business day of the Plan Period) for each calendar year in which the Option is outstanding at any time.

6. Deduction Changes. An employee may increase, decrease or discontinue his or her payroll deduction once during any Plan Period, by effecting a new Appropriate Authorization. If an employee elects to discontinue his or her payroll deductions during a Plan Period, but does not elect to withdraw his or her funds pursuant to Section 8 hereof, funds deducted prior to his or her election to discontinue will be applied to the purchase of Common Stock on the Exercise Date (as defined below).

7. Interest. Interest will not be paid on any employee accounts.

8. Withdrawal of Funds. An employee may at any time prior to the close of business on the last business day in a Plan Period and for any reason permanently draw out the balance accumulated in the employee's account and thereby withdraw from participation in an Offering. Partial withdrawals are not permitted. Any employee who withdraws from participation in an

Offering shall not be permitted to participate in the Plan again until the start of the next Plan Period.

9. Purchase of Shares. On the Offering Commencement Date of each Plan Period, the Company will grant to each eligible employee who is then a participant in the Plan an option ("Option") to purchase on the last business day of such Plan Period (the "Exercise Date"), at the Option Price hereinafter provided for, the largest number of whole shares of Common Stock of the Company as does not exceed the number of shares determined by dividing \$12,500 (in the case of a six-month Plan Period) or \$25,000 (in the case of a one-year Plan Period) by the closing price (as defined below) on the Offering Commencement Date of such Plan Period.

The purchase price for each share purchased will be 95% of the closing price of the Common Stock on the Exercise Date. Such closing price shall be (a) the closing price on any national securities exchange on which the Common Stock is listed, (b) the closing price of the Common Stock on the Nasdaq National Market or (c) the average of the closing bid and asked prices in the over-the-counter-market, whichever is applicable, as published in The Wall Street Journal. If no sales of Common Stock were made on such a day, the price of the Common Stock for purposes of clauses (a) and (b) above shall be the reported price for the next preceding day on which sales were made.

Each employee who continues to be a participant in the Plan on the Exercise Date shall be deemed to have exercised his or her Option at the Option Price on such date and shall be deemed to have purchased from the Company the number of full shares of Common Stock reserved for the purpose of the Plan that his or her accumulated payroll deductions on such date will pay for, but not in excess of the maximum number determined in the manner set forth above.

Any balance remaining in an employee's payroll deduction account at the end of a Plan Period will be automatically refunded to the employee, except that any balance which is less than the purchase price of one share of Common Stock will be carried forward into the employee's payroll deduction account for the following Offering, unless the employee elects not to participate in the following Offering under the Plan, in which case the balance in the employee's account shall be refunded.

10. Issuance of Certificates. Certificates representing shares of Common Stock purchased under the Plan may be issued only in the name of the employee, in the name of the employee and another person of legal age as joint tenants with rights of survivorship, or (in the Company's sole discretion) in the name of a brokerage firm, bank or other nominee holder designated by the employee. The Company may, in its sole discretion and in compliance with applicable laws, authorize the use of book entry registration of shares in lieu of issuing stock certificates.

11. Rights on Retirement, Death or Termination of Employment. In the event of a participating employee's termination of employment prior to the last business day of a Plan Period, no payroll deduction shall be taken from any pay due and owing to an employee and the balance in the employee's account shall be paid to the employee or, in the event of the employee's death, (a) to a beneficiary previously designated in a revocable notice signed by the employee (with any spousal consent required under state law) or (b) in the absence of such a designated beneficiary, to the executor or administrator of the employee's estate or (c) if no such

executor or administrator has been appointed to the knowledge of the Company, to such other person(s) as the Company may, in its discretion, designate.

12. **Optionees Not Stockholders.** Neither the granting of an Option to an employee nor the deductions from his or her pay shall constitute such employee a stockholder of the shares of Common Stock covered by an Option under this Plan until such shares have been purchased by and issued to him or her.

13. **Rights Not Transferable.** Rights under this Plan are not transferable by a participating employee other than by will or the laws of descent and distribution, and are exercisable during the employee's lifetime only by the employee.

14. **Application of Funds.** All funds received or held by the Company under this Plan may be combined with other corporate funds and may be used for any corporate purpose.

15. **Adjustment in Case of Changes Affecting Common Stock.** In the event of a subdivision of outstanding shares of Common Stock, or the payment of a dividend in Common Stock, the number of shares reserved for issuance under this Plan, the number of shares issuable in any Offering, and the share limitation set forth in Section 9, shall be increased proportionately, and such other adjustment shall be made as may be deemed equitable by the Board or the Committee. In the event of any other change affecting the Common Stock, such adjustment shall be made as may be deemed equitable by the Board or the Committee to give proper effect to such event.

16. **Merger.** In the event of a proposed sale of all or substantially all of the assets of the Company or a merger or consolidation of the Company with or into another corporation (other than a merger in which the Company is the surviving corporation and the holders of the capital stock of the Company immediately prior to such merger continue to hold at least 50% by voting power of the capital stock of the Company) or the proposed dissolution or liquidation of the Company during a Plan Period, the Board or the Committee shall set a new Exercise Date (the "New Exercise Date") for such Plan Period, and such Plan Period shall end on the New Exercise Date. The New Exercise Date shall be before the date of such asset sale, merger, consolidation, dissolution or liquidation. The Board or the Committee shall send written notice to each employee participating in the Offering for such Plan Period, at least ten business days prior to the New Exercise Date, that the Exercise Date for such Offering has been changed to the New Exercise Date and that the employee's Option shall be exercised automatically on the New Exercise Date, unless prior to such date the employee has withdrawn from such Offering as provided in Section 8 hereof.

17. **Amendment of the Plan.** The Board may at any time, and from time to time, amend this Plan in any respect, except that (a) if the approval of any such amendment by the shareholders of the Company is required by Section 423 of the Code, such amendment shall not be effected without such approval, and (b) in no event may any amendment be made which would cause the Plan to fail to comply with Section 423 of the Code.

18. **Insufficient Shares.** In the event that the total number of shares of Common Stock specified in elections to be purchased under any Offering plus the number of shares purchased under previous Offerings under this Plan exceeds the maximum number of shares issuable under

this Plan, the Board or the Committee will allot the shares then available on a pro rata basis. Any balance remaining in an employee's payroll deduction account at the end of a Plan Period due to an insufficiency of shares will be refunded to the employee without interest.

19. Termination of the Plan. This Plan may be terminated at any time by the Board. Upon termination of this Plan all amounts in the accounts of participating employees shall be promptly refunded.

20. Governmental Regulations. The Company's obligation to sell and deliver Common Stock under this Plan is subject to listing on a national stock exchange or quotation on the Nasdaq National Market and the approval of all governmental authorities required in connection with the authorization, issuance or sale of such stock.

21. Governing Law. The Plan shall be governed by New Hampshire law except to the extent that such law is preempted by federal law.

22. Issuance of Shares. Shares may be issued upon exercise of an Option from authorized but unissued Common Stock, from shares held in the treasury of the Company, or from any other proper source.

23. Notification upon Sale of Shares. Each employee agrees, by entering the Plan, to promptly give the Company notice of any disposition of shares purchased under the Plan where such disposition occurs within two years after the date of grant of the Option pursuant to which such shares were purchased.

24. Effective Date and Approval of Shareholders. The Plan shall take effect on January 1, 1999, but is subject to approval by the stockholders of the Company as required by Section 423 of the Code, which approval must occur within twelve months of the adoption of the Plan by the Board.

Adopted by the Board of Directors on November 21, 1997

Approved by the stockholders on February 17, 1998

Amended on May 16, 2002, and approved by the stockholders on June 18, 2002

Amended on April 28, 2003, and approved by the stockholders on June 3, 2003

Amended on April 22, 2005, and approved by the stockholders on June 9, 2005

Amended on December 2, 2005, and approved by the Board of Directors on December 2, 2005.



**SEPARATION AGREEMENT**

**THIS SEPARATION AGREEMENT** (the "Agreement"), effective on the last date executed below, is entered into by and between **PC Connection, Inc.**, on behalf of itself and its officers, directors, shareholders, employees, agents, benefit plans and parent, affiliated, predecessor, successor, subsidiary, and other related companies, and each of them, jointly and severally (herein singularly and collectively called the "**COMPANY**") and Kenneth A. Grady, on behalf of himself and his heirs, executors, guardians, administrators, successors and assigns, and each of them, jointly and severally (hereinafter singularly and collectively called the "**EXECUTIVE**"), who agree to be bound by all of the terms and conditions hereof.

**WHEREAS**, the parties desire to fully, equitably, and completely settle and dispose of any and all claims of whatever kind or nature which the EXECUTIVE ever had, may now have, or may hereafter have, whether known or unknown, against the COMPANY, the parties hereto agree as follows:

1. **Separation Date.** The EXECUTIVE's employment with the COMPANY terminated on November 18, 2005 (the "Separation Date").
2. **Executive's Separation Payment.** Subject to the EXECUTIVE's fulfillment of all of the EXECUTIVE's obligations hereunder, the COMPANY and the EXECUTIVE agree as follows:

A. The COMPANY will pay the EXECUTIVE severance compensation, at his current level of base salary, less all applicable deductions for federal, state, and local taxes, social security, medical coverage premiums, wage withholding, and other taxes, for a period of forty-two (42) weeks (the "Separation Payment"). The EXECUTIVE acknowledges and agrees that the Separation Payment exceeds complete satisfaction of any and all compensation due to the EXECUTIVE from the COMPANY, whether for services rendered or otherwise, through the Separation Date and that, except as expressly provided under this Agreement, no further compensation is owed to the EXECUTIVE. The COMPANY agrees to pay the EXECUTIVE for all accrued, unused vacation, less applicable deductions for federal, state, and local taxes, social security, wage withholding, and other taxes.

B. The COMPANY represents that the EXECUTIVE is currently not vested in any stock options under the parties' Option Agreement.

C. The COMPANY agrees to waive and forgive any relocation expenses repayment that might otherwise be due from the EXECUTIVE.

3. **Benefit Plans and Programs: COBRA.**

A. The COMPANY and the EXECUTIVE hereby agree that all COMPANY benefits, including, but not limited to, employee discount, long-term disability, short-term disability and life insurance coverage will cease as of the Separation Date, except to the extent explicitly set forth in the Agreement. The EXECUTIVE will likewise not continue to earn

vacation or other paid time off after the Separation Date. The EXECUTIVE's right to contribute to the COMPANY's 401(k) plan terminated as of the Separation Date, in accordance with the terms of that plan.

B. As of the Separation Date, the EXECUTIVE will be eligible for continued health care coverage, in accordance with the provisions of the federal Consolidated Omnibus Budget and Reconciliation Act, as amended ("COBRA"). Provided the EXECUTIVE timely elects to continue receiving group medical coverage pursuant to COBRA, the COMPANY agrees to pay for the EXECUTIVE's COBRA coverage as of the Separation Date for a period of forty-two(42) weeks. The COMPANY's obligation to pay for the EXECUTIVE's COBRA coverage, however, shall be reduced by the amount that the EXECUTIVE will pay from the EXECUTIVE's Separation Payments toward such coverage, which shall be equal to the amount of the EXECUTIVE's medical coverage premiums as of the Separation Date. At the conclusion of the forty-two (42) week Separation Payment period, all continuing COBRA coverage shall be at the EXECUTIVE's sole election and expense. To the extent that the EXECUTIVE obtains employment during the forty-two (42) week Separation Payment period that the COMPANY is paying for the EXECUTIVE's COBRA coverage, the EXECUTIVE shall immediately notify the COMPANY of such employment. Regardless of such notification, however, upon the EXECUTIVE obtaining employment the COMPANY's obligation to pay for COBRA coverage shall immediately cease.

4. **Eligibility for Reinstatement.** The EXECUTIVE agrees to waive any and all eligibility for and rights to reinstatement or future employment with the COMPANY. The EXECUTIVE further agrees that, as of the Separation Date, the EXECUTIVE relinquished all officer and director positions with PC Connection, Inc., including with its subsidiaries and related entities.

5. **Covenant not to Sue.** The EXECUTIVE covenants not to file any suits, complaints, or other actions against the COMPANY in any court of law with respect to any aspect of the EXECUTIVE's employment by, or termination of employment from, the COMPANY, or with respect to any other matter whatsoever, whether known or unknown to the EXECUTIVE at the time of execution of this Agreement. It is agreed that if the EXECUTIVE should breach this Agreement, the EXECUTIVE will pay the COMPANY'S attorney's fees and litigation costs in their entirety.

6. **Waiver and Release.** The EXECUTIVE waives, releases, and forever discharges the COMPANY of and from all, and in all manner of, actions and causes of action, suits, debts, claims and demands whatsoever, in law or in equity, which the EXECUTIVE ever had, may now have, or may hereafter have with respect to any aspect of the EXECUTIVE's employment by, or termination of employment from, the COMPANY, or with respect to any other matter whatsoever, whether known or unknown to the EXECUTIVE at the time of his execution of this Agreement. In exchange for the severance pay and benefits provided the EXECUTIVE under this Agreement, to which the EXECUTIVE would not otherwise be entitled, on the EXECUTIVE's own behalf and that of the EXECUTIVE's heirs, executors, administrators, beneficiaries, personal representatives and assigns, the EXECUTIVE agrees that this Agreement shall be in complete and final settlement of any and all causes of action, rights or claims that the EXECUTIVE may have had in the past, now has, or might now have, known or unknown, in any way related to, connected with or arising out of the EXECUTIVE's employment with or

separation from the COMPANY. The EXECUTIVE's covenants and releases, as set forth in the Agreement, include a waiver of any and all rights or remedies which the EXECUTIVE ever had, may now have or may hereafter have against the COMPANY under any federal, state, or local discrimination law including, but not limited to, Title VII of the 1964 Civil Rights Act, 42 U.S.C. §2000e, et seq. (as amended by the Civil Rights Act of 1991), the Age Discrimination in Employment Act of 1967, 29 U.S.C. §621, et seq., the Americans With Disabilities Act of 1990, 42 U.S.C. §12101, et seq., the Family and Medical Leave Act, 29 U.S.C. §2601, et seq., the Fair Credit Reporting Act, 15 U.S.C. §1681, et seq., the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. §1001, et seq., and the Older Workers Benefit Protection Act ("OWBPA"), 29 U.S.C. §623, et seq., all as amended. Furthermore, the EXECUTIVE hereby specifically releases and forever discharges the COMPANY and all of its past and present affiliates, directors, shareholders, officers, employees, employee benefit plans, agents, and representatives, its successors and assigns, and all others connected with it, both individually and in their official capacities, from any and all such causes of action, rights, or claims.

**7. Return of Company Property.** The EXECUTIVE represents that the EXECUTIVE has returned, as of the Separation Date, to the COMPANY all COMPANY vehicles, computers, software, printers and facsimile machines, credit cards, keys, key cards, identification badges, cell phones, pagers, business cards, customer, client or vendor lists and records, policy and procedure manuals, price lists, business contracts, and all other documents, information, equipment and property (of any kind) belonging to the COMPANY, and certifies that he has neither retained nor shared with others copies or derivatives of any of the foregoing.

**8. Company's Confidential Information.** The EXECUTIVE recognizes that the COMPANY is the owner of proprietary rights in certain systems, information, records and other tangible and intangible properties which constitute valuable trade secrets of the COMPANY, and that EXECUTIVE has been employed in a position in which the COMPANY has a legitimate interest in protecting such confidential and proprietary information in order to maintain and enhance a competitive position within its industry. Accordingly, the EXECUTIVE covenants and agrees that the EXECUTIVE has not and the EXECUTIVE will not remove, duplicate, or use on behalf of or disclose, directly or indirectly, to any persons or entities outside the COMPANY, any information, property, trade secrets or other things of value which have not been publicly disclosed, including, but not limited to, products, product specifications, procedures, prices, costs, business affairs, plans, ideas, or past, present or prospective customers, clients or vendors. The EXECUTIVE further agrees that he will zealously preserve all matters falling within the scope of the attorney-client privilege, asserting such privilege wherever applicable and to the fullest extent consistent with law.

**9. Disclosures and Subpoena.** The EXECUTIVE agrees that the EXECUTIVE will not, directly or indirectly, and without the COMPANY's prior written consent, voluntarily provide information, documents, or statements to any entity or person, including current or former employees of the COMPANY (except the EXECUTIVE's counsel, tax preparer, and immediate family) regarding: (a) any other person's employment with, or termination of employment from, the COMPANY; or (b) any information or documents concerning the COMPANY. In the event that a subpoena or other lawful process is properly served upon the EXECUTIVE requiring production or disclosure of information or documents concerning the foregoing matters, the EXECUTIVE shall promptly notify the COMPANY, in accordance with the Notices provisions

detailed herein, and shall provide it with copies of any subpoena or other process served upon the EXECUTIVE. The EXECUTIVE shall thereafter make such documents available to the COMPANY for inspection and copying at a reasonable time and place designated by the COMPANY prior to their production. In the event that the subpoena or other process requires testimony or statements from the EXECUTIVE, the EXECUTIVE agrees to meet, telephonically or in person, with attorneys or agents designated by the COMPANY, at a reasonable time and place designated by the COMPANY and prior to giving the testimony or the production of documents, for the purpose of discussing the same. Nothing herein shall give the COMPANY the right to control or dictate the content of any testimony given by the EXECUTIVE, or any documents produced by the EXECUTIVE pursuant to subpoena or other lawful process. It is understood that the EXECUTIVE shall provide all information lawfully required of the EXECUTIVE, but shall not waive any matters of attorney-client privilege without the Company's express consent. In the event that the COMPANY requires any information or testimony from the EXECUTIVE in connection with any claim made against the COMPANY, or any claims made by the COMPANY against persons or entities not party to this Agreement, the EXECUTIVE agrees to cooperate fully with and without cost to the COMPANY, including: (a) appearing at any deposition, trial, hearing or arbitration; (b) meeting telephonically or in person with attorneys or agents designated by the COMPANY, at a reasonable time and place designated by the COMPANY and prior to the giving of testimony, for the purpose of discussing such testimony; and (c) providing the COMPANY with any relevant documentation in the EXECUTIVE's custody, control or possession.

10. **Mutual Consideration.** The EXECUTIVE agrees that the EXECUTIVE's covenants and promises made in this Agreement are in consideration of the payments and other promises made hereunder by the COMPANY. Likewise, the COMPANY agrees that its covenants and promises made in this Agreement are in consideration of the promises made hereunder by the EXECUTIVE. It is agreed and understood that the EXECUTIVE's right to receive and retain the economic consideration provided to him hereunder shall be expressly conditioned on the full and continuing performance of all of his obligations under this Agreement.

11. **Future Cooperation.** The EXECUTIVE agrees that, in the future, the EXECUTIVE will cooperate with the COMPANY and will execute such documents that the COMPANY requests in order to fulfill his obligations hereunder.

12. **Confidentiality of this Agreement.** The EXECUTIVE agrees that the EXECUTIVE will neither reveal the existence of this Agreement, nor any terms hereof, to any person, entity, or organization, except to the EXECUTIVE's immediate family, to the EXECUTIVE's attorney, to the EXECUTIVE's tax preparer, or as may be required by law, and only then subject to their agreement to preserve the confidentiality hereof. Likewise, the COMPANY agrees that it will not reveal the existence of this Agreement, nor any of the terms hereof, to any person, entity, or organization, except as may be reasonably appropriate for the conduct of its business or as may be required by law.

13. **Breach of this Agreement.** In the event that the EXECUTIVE, or any person, entity, or organization, including those to which the EXECUTIVE has made permissible disclosures hereunder, breaches any of the EXECUTIVE's promises made in this Agreement, and the COMPANY defends or pursues any charge, suit, complaint, claim, or grievance as a result

thereof, the EXECUTIVE shall be liable to the COMPANY for all damages, attorney's fees, expenses, and costs (including discovery costs) incurred by it in defending or pursuing the same. Likewise, should the COMPANY breach any of its promises made in this Agreement, and the EXECUTIVE defends or pursues any charge, suit, complaint, claim, or grievance as a result thereof, the COMPANY shall be liable to the EXECUTIVE for all damages, attorney's fees, expenses and costs (including discovery costs) incurred by the EXECUTIVE in defending or pursuing the same.

14. **Review and Execution of this Agreement.** The EXECUTIVE acknowledges that the EXECUTIVE had the right to review and consider this Agreement for twenty-one (21) days prior to execution, and to consult with legal counsel (which the EXECUTIVE has been encouraged to do). The EXECUTIVE further acknowledges that the EXECUTIVE has entered into this Agreement voluntarily and it is of the EXECUTIVE's own free will. The EXECUTIVE acknowledges the EXECUTIVE's right to revoke this Agreement within seven (7) days following the EXECUTIVE's execution hereof, by giving written notice thereof to the COMPANY. In the event of such revocation, this Agreement shall become null and void, and no party hereto shall have any rights or obligations hereunder. If the EXECUTIVE does not revoke this Agreement, then, at the expiration of the seven-day period, this Agreement shall take effect as a legally binding agreement between the EXECUTIVE and the COMPANY on the basis set forth herein.

15. **Governing Law and Venue.** The parties agree that this Agreement shall be construed in accordance with New Hampshire law, and that any action brought by any party hereunder may be instituted and maintained only in a state or federal court in New Hampshire.

16. **Non-Disparagement.** The parties agree that the relationship between them has terminated, and that they shall refrain from disparaging each other in communications with third parties unless required to do so by a duly authorized officer of the Court or under the terms and conditions specifically set forth in the Agreement. The COMPANY agrees that requests for references concerning the EXECUTIVE that are directed to its Chief Executive Officer or Vice President of Human Resources will be responded to with the transmittal of the reference letter appended hereto as Exhibit A.

17. **Notices.** Notifications to the COMPANY made under this Agreement shall be made by certified mail or other means permitted by applicable law as follows:

Attn.: Chief Executive Officer  
730 Milford Road  
Merrimack, NH 03054

Notification to the EXECUTIVE shall be made by certified mail or other means permitted by law as follows:

Kenneth A. Grady, Esq.  
55 The Flume  
Amherst, NH 03031

18. **Nature of Agreement.** The EXECUTIVE understands and agrees that this Agreement is a severance and settlement agreement and does not constitute an admission of liability or wrongdoing on the part of him or the COMPANY.

19. **Waiver or Rights.** No delay or omission by either of the parties in exercising any rights under this Agreement shall operate as a waiver of that or any other right. A waiver or consent given by either of the parties on any one occasion shall be effective only in that instance and shall not be construed as a bar or waiver of any right on any other occasion.

20. **Severability.** If any clause or provision of this Agreement is illegal, invalid or unenforceable under applicable present or future laws effective during the term of this Agreement, the remainder of this Agreement shall not be affected. In lieu of each clause or provision of this Agreement that is illegal, invalid or unenforceable, there shall be added as a part of this Agreement a clause or provision as nearly identical as may be possible and as may be legal, valid and enforceable.

21. **Entire Agreement.** The parties agree that, with the exception of the Covenant Not to Compete And Disclose Confidential Information And Assignment of Rights dated July 11, 2005, the foregoing constitutes the entire Agreement among them, and that there exist no other Agreements, oral or written, express or implied, relating to any matters covered by this Agreement, or relating to any other matter whatsoever, whether or not within the knowledge or contemplation of either of the parties at the time of execution of this Agreement, except to the extent specifically identified herein. This Agreement may only be modified in a writing signed by both parties hereto.

22. **Headings.** The use of headings, captions and numbers in this Agreement is solely for the convenience of identifying and indexing the various paragraphs and shall in no event be considered when construing or interpreting any provision in this Agreement.

23. **Counterparts.** This Agreement may be executed in two (2) signature counterparts, each of which shall constitute an original, but all of which taken together shall constitute one and the same instrument.

24. **Executive's Understanding of Executive's Rights.** THE EXECUTIVE HEREBY ACKNOWLEDGES THAT THE EXECUTIVE HAS READ THIS AGREEMENT IN ITS ENTIRETY, HAS HAD THE OPPORTUNITY TO CONSULT WITH AN ATTORNEY, UNDERSTANDS THE AGREEMENT AND VOLUNTARILY SIGNS IT WITH FULL KNOWLEDGE THAT THE EXECUTIVE IS WAIVING IMPORTANT RIGHTS.

WHEREFORE, the parties have read all of the foregoing, understand the same, and agree to all of the provisions contained herein.

PC CONNECTION, INC.

KENNETH GRADY

By: /s/ Brad Mousseau

/s/ Kenneth A. Grady

Its: \_\_\_\_\_

\_\_\_\_\_

Date: 11/28/05

November 28, 2005

**AMENDMENT No. 2  
TO  
AGREEMENT FOR INVENTORY FINANCING**

This Amendment No. 2 ("Amendment") to the Agreement for Inventory Financing is made as of May 9, 2004 by and by and among **PC Connection, Inc.**, duly organized under the laws of the State of Delaware ("PC Connection"), **Merrimack Services Corporation**, a corporation, duly organized under the laws of the State of Delaware ("Merrimack"), **GovConnection, Inc.**, a corporation, duly organized under the laws of the State of Delaware ("GovConnection"), **MoreDirect, Inc.**, a corporation, duly organized under the laws of the State of Delaware ("MoreDirect"), (Merrimack, GovConnection and MoreDirect are referred to herein as a "Customer" or, collectively, the "Customers") and **IBM Credit LLC**, a Delaware limited liability company ("IBM Credit").

**RECITALS:**

**A.** PC Connection, the Customers and IBM Credit have entered into that certain Agreement for Inventory Financing dated as of October 31, 2002 (as amended, modified or supplemented from time to time, the "Agreement").

**B.** The parties have agreed to modify the Agreement as more specifically set forth below, upon and subject to the terms and conditions set forth herein.

**AGREEMENT**

**NOW THEREFORE**, in consideration of the premises and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, Customers and IBM Credit hereby agree as follows:

**Section 1. Definitions.** All capitalized terms not otherwise defined herein shall have the respective meanings set forth in the Agreement.

**Section 2. Amendment.** The Agreement is hereby amended as follows:

Attachment E to the Agreement for Inventory Financing is hereby amended by deleting such Attachment E in its entirety and substituting, in lieu thereof, the Attachment E attached hereto. Such new Attachment E shall be effective immediately. The change contained in the new Attachment E includes, without limitation, the following:

(a) Subsection (d) In Transit, of Section 1. of Loan Status has been reduced from up to 4 days to up to 2 days.

**Section 3. Representations and Warranties.** Each Customer makes to IBM Credit the following representations and warranties all of which are material and are made to induce IBM Credit to enter into this Amendment.

**Section 3.1 Accuracy and Completeness of Warranties and Representations.** All representations made by each Customer in the Agreement were true and accurate and complete in every respect as of the date made, and, as amended by this Amendment, all representations made by each Customer in the Agreement are true, accurate and complete in every material respect as of the date hereof, and do not fail to disclose any material fact necessary to make representations not misleading.

**Section 3.2 Violation of Other Agreements.** The execution and delivery of this Amendment and the performance and observance of the covenants to be performed and observed hereunder do not







**AMENDMENT No. 3  
TO  
AGREEMENT FOR INVENTORY FINANCING**

This AMENDMENT (“Amendment”) to AGREEMENT FOR INVENTORY FINANCING is made as of May 27, 2005 by and between **PC CONNECTION, INC.**, a corporation, duly organized under the laws of the State of Delaware (“PC Connection”), **MERRIMACK SERVICES CORPORATION** a corporation, duly organized under the laws of the State of Delaware (“Merrimack”), **GOVCONNECTION, INC.**, a corporation, duly organized under the laws of the State of Maryland (“GovConnection”), and **MOREDIRECT, INC.**, a corporation, duly organized under the laws of the State of Florida (“MoreDirect”) (PC Connection, Merrimack, GovConnection and MoreDirect are referred to herein as a “Customer” or, collectively, the “Customers”) and **IBM CREDIT LLC**, a Delaware limited liability company, formerly IBM Credit Corporation (“IBM Credit”).

**RECITALS:**

**WHEREAS**, Customers and IBM Credit have entered into that certain Agreement for Inventory Financing dated as of October 31, 2002 (as amended, supplemented or otherwise modified from time to time, the “Agreement”); and

**WHEREAS**, Customers AND IBM Credit desire to amend the Agreement as more fully set forth herein.

**AGREEMENT**

**NOW THEREFORE**, in consideration of the premises set forth herein, and for other good and valuable consideration, the value and sufficiency of which is hereby acknowledged, the parties hereto agree that the Agreement is amended as follows:

**Section 1.** Definitions. All capitalized terms not otherwise defined herein shall have the respective meanings set forth in the Agreement.

**Section 2.** Amendment. The Agreement is hereby amended by deleting subsection (A) of Section 4.1 in its entirety and substituting, in lieu thereof, the following:

“(A) all goods manufactured or sold by International Business Machines Corporation (“IBM”), Lenovo (United States) Inc. (“Lenovo”) or Lexmark International, Inc. (“Lexmark”) or bearing the trademarks or trade names of IBM, Lenovo or Lexmark, including, inventory and equipment and all parts thereof, attachments, accessories and accessions thereto, products thereof and documents therefor, but excluding, however, each Customer’s capital equipment;”

**Section 3.** Representations and Warranties. Customer makes to IBM Credit the following representations and warranties all of which are material and are made to induce IBM Credit to enter into this Amendment.

**Section 3.1** Accuracy and Completeness of Warranties and Representations. All representations made by Customer in the Agreement were true and accurate and complete in every respect as of the date made, and, as amended by this Amendment, all representations made by Customer in the Agreement are true, accurate and complete in every material respect as of the date hereof, and do not fail to disclose any material fact necessary to make representations not misleading.

**Section 3.2** Violation of Other Agreements. The execution and delivery of this Amendment and the performance and observance of the covenants to be performed and observed hereunder do not violate or cause Customer not to be in compliance with the terms of any agreement to which Customer is a party.

**Section 3.3** Litigation. Except as has been disclosed by Customer to IBM Credit in writing, there is no litigation, proceeding, investigation or labor dispute pending or threatened against Customer, which if adversely determined, would materially adversely affect Customer's ability to perform Customer's obligations under the Agreement and the other documents, instruments and agreements executed in connection therewith or pursuant hereto.

**Section 3.4** Enforceability of Amendment. This Amendment has been duly authorized, executed and delivered by Customer and is enforceable against Customer in accordance with its terms.

**Section 4.** Ratification of Agreement. Except as specifically amended hereby, all of the provisions of the Agreement shall remain unamended and in full force and effect. Customer hereby, ratifies, confirms and agrees that the Agreement, as amended hereby, represents a valid and enforceable obligation of Customer, and is not subject to any claims, offsets or defenses.

**Section 5.** Governing Law. This Amendment shall be governed by and interpreted in accordance with the laws which govern the Agreement.

**Section 6.** Counterparts. This Amendment may be executed in any number of counterparts, each of which shall be an original and all of which shall constitute one agreement.

**IN WITNESS WHEREOF**, the duly authorized representatives of the parties hereto have executed this Amendment as of the date first above written.

**IBM CREDIT LLC,**

/s/ Thomas Harahan

Thomas Harahan, Manager

[PLEASE PRINT NAME & TITLE]

**PC CONNECTION, INC.**

/s/ Jack L. Ferguson

Jack L. Ferguson, Treasurer and Interim CFO

[PLEASE PRINT NAME & TITLE]

**MERRIMACK SERVICES CORPORATION**

/s/ Jack L. Ferguson

Jack L. Ferguson Treasurer and Interim CFO

[PLEASE PRINT NAME & TITLE]

**GOVCONNECTION, INC.**

/s/ Gary Anderson

Gary Anderson, Treasurer

[PLEASE PRINT NAME & TITLE]

[Signatures continue on following page.]

**MOREDIRECT, INC.**

/s/ Scott J. Modist

---

Scott J. Modist C.F.O.

[PLEASE PRINT NAME & TITLE]

**AMENDMENT NO. 3 TO LEASE**

THIS AGREEMENT made this 11 day of November, 2005, by and between EWE WAREHOUSE INVESTMENTS V., LTD., as Lessor and MERRIMACK SERVICES CORPORATION dba PC CONNECTION SERVICES, as Lessee located at 2841-2931 Old State Route 73, Wilmington, Ohio 45177.

WITNESSETH:

WHEREAS, Lessor and Lessee entered into a Lease dated May 13, 1993, as amended June 19, 2001, April 24, 2003, and

WHEREAS, the Lessor and Lessee desire to amend the Lease of approximately 102,400 square feet to extend the term, revise rent, add a Right to Terminate and add an Option to Renew.

NOW THEREFORE, the Lease is amended as follows.

1. Article 1. TERM. shall be revised as follows.

Effective December 1, 2005, the term of this Lease shall be extended for an additional four (4) years, for a total term of sixteen (16) years, two (2) months, commencing October 1, 1993 and ending November 30, 2009, both dates inclusive.

2. Lessee warrants that Lessee has accepted and is now in possession of the Leased Premises and that the Lease is valid and presently in full force and effect. Lessee accepts the Premises in its present "as is" condition.

3. Article 3. RENT. shall be revised as follows.

For the one (1) year period commencing December 1, 2005 and ending November 30, 2006, the Lessee shall pay to the Lessor as Basic Annual Rent for the Leased Premises the sum of FOUR HUNDRED EIGHTY-SIX THOUSAND THREE HUNDRED NINETY-NINE AND 96/100 DOLLARS (\$486,399.96) which shall be paid in equal monthly installments of FORTY THOUSAND FIVE HUNDRED THIRTY-THREE AND 33/100 DOLLARS (\$40,533.33), due and payable on the first day of each month, in advance, without demand. Checks should be made payable to EWE Warehouse Investments V, Ltd. and sent c/o Easton & Associates, 10165 N.W. 19<sup>th</sup> Street, Miami, Florida 33172. Said rent shall be paid to the Lessor, or to the duly authorized agent

of the Lessor, at its office during business hours. If the commencement date of this Lease is other than the first day of the month, any rental adjustment or additional rents hereinafter provided for shall be prorated accordingly. The Lessee will pay the rent as herein provided, without deduction whatsoever, and without any obligation of the Lessor to make demand for it. Any installment of rent accruing hereunder and any other sum payable hereunder, if not paid when due, shall bear interest at the rate of eighteen percent (18%) per annum until paid. The Basic Annual Rent of \$486,399.96 shall be adjusted annually based on any increases in the Consumer Price Index beginning one year after the commencement date of this Lease and at the end of each year thereafter, whether during the term of this Lease or any renewal or extension thereof. Increases in the Annual Rent shall be made in accordance with the following procedure:

a. The index to be used for this adjustment shall be the Consumer Price Index (NORTH CENTRAL REGION, All Urban Consumers, All Items, 1982-1984 equaling a base of 100, from the U.S. Department of Labor, Bureau of Labor Statistics, Washington, D.C.).

b. The Consumer Price Index of 2005 for the month of August shall be the "Base Period Consumer Price Index". The Consumer Price Index for the month of August in each adjustment year shall be the "Adjustment Period Consumer Price Index".

c. The Base Period Consumer Price Index shall be subtracted from the Adjustment Period Consumer Price Index; the difference shall be divided by the Base Period Consumer Price Index. This quotient shall then be multiplied by the \$486,399.96, and the result shall then be added to the \$486,399.96. The resulting sum shall be the adjusted Annual Rent for such immediately succeeding leasehold period which shall be paid in equal monthly installments. **Notwithstanding the Index, the annual percentage increase shall be capped at four percent (4%).**

d. If the said Consumer Price Index is, at any time during the term of this Lease, discontinued by the Government, then the most nearly comparable index shall be substituted for the purpose of the aforesaid calculations.

4. The following RIGHT TO TERMINATE, shall be added.

Lessor shall grant Lessee a Right to Terminate this Lease anytime after the twenty-four months of the extended Lease Term (November 30, 2007) with prior written notice to Lessor no less than one hundred eighty (180) days in advance of intended termination provided Lessee is not in default of the Lease. Lessee shall pay to Lessor as a penalty for early termination the sum equivalent to \$0.50 per square foot per year and prorated based on the number of days remaining on the Lease until the end of the four (4) year extension. The penalty amount shall be paid by Lessee to Lessor upon receipt of Lessee's written notice to Lessor at which time Lessor shall invoice Lessee. Such invoice shall be paid immediately upon receipt by Lessee to Lessor.

5. OPTION TO RENEW shall be amended as follows.

Lessee is hereby granted an option to renew this Lease for an additional term of four (4) years on the same terms and conditions contained herein except for the rental and the length of the term, upon the conditions that:

a. written notice of the exercise of such option shall be given by Lessee to Lessor not less than one hundred eighty (180) days prior to the end of the term of this Lease (by May 31, 2009); and

b. at the time of the giving of such notice and at the expiration of the term of this Lease, there are no defaults in the covenants, agreements, terms and conditions on the part of Lessee to be kept and performed, and all rents are and have been fully paid. Provided also, that the rent to be paid during each year of the said renewal period shall be as determined in accordance with the following:

a. The index to be used for this adjustment shall be the Consumer Price Index (NORTH CENTRAL REGION, All Urban Consumers, All Items, 1982-1984 equaling a base of 100, from the U.S. Department of Labor, Bureau of Labor Statistics, Washington, D.C.).

b. The Consumer Price Index of 2005 for the month of August shall be the "Base Period Consumer Price Index". The Consumer Price Index for the month of August in each adjustment year shall be the "Adjustment Period Consumer Price Index".

c. The Base Period Consumer Price Index shall be subtracted from the Adjustment Period Consumer Price Index; the difference shall be divided by the Base Period Consumer Price Index. This quotient shall then be multiplied by the \$486,399.96, and the result shall then be added to the \$486,399.96. The resulting sum shall be the adjusted Annual Rent for such immediately succeeding leasehold period which shall be paid in equal monthly installments.

d. If the said Consumer Price Index is, at any time during the term of this Lease, discontinued by the Government, then the most nearly comparable index shall be substituted for the purpose of the aforesaid calculations.

6. Except as expressly amended herein, all other terms and conditions of the Lease remain in full force and effect.

IN WITNESS WHEREOF, the Lessor and Lessee have affixed their signatures to duplicates of this Amendment, this 3rd day of November, 2005, as to Lessee and this 11 day of November, 2005, as to Lessor.

Signed and acknowledged  
in the presence of:

LESSOR: EWE WAREHOUSE INVESTMENTS V, LTD.  
By: Miller-Valentine Realty, Inc.  
Its: Managing Agent



/s/ Barbara J. Gilmore

Barbara J. Gilmore  
Print Name

By: /s/ Chuck McCosh

Chuck McCosh  
Its: President

/s/ Michelle Atkinson

Michelle Atkinson  
Print Name

LESSEE: MERRIMACK SERVICES CORPORATION  
DBA PC CONNECTION SERVICES

/s/ Maureen R. Cram

Maureen R. Cram  
Print Name

By: /s/ Robert A. Pratt

Title: Robert Pratt  
Director of Facilities

/s/ Eric Burbank

Eric Burbank  
Print Name

[NOTARY ON NEXT PAGE...]

STATE OF OHIO, COUNTY OF MONTGOMERY, SS:

The foregoing instrument was acknowledged before me this 11 day of November, 2005, by Chuck McCosh, President of Miller-Valentine Realty, Inc., managing agent for EWE INVESTMENTS V, LTD.

/s/ Rita A. Hughes

Notary Public

STATE OF NH, COUNTY OF Hillsborough, SS:

The foregoing instrument was acknowledged before me this 3rd day of November, 2005, by Robert A. Pratt, the Director of Facilities of MERRIMACK SERVICES CORPORATION DBA PC CONNECTION SERVICES, a corporation on behalf of said corporation.

/s/ Jennifer A. Losik

NOTARY PUBLIC

**FIFTH AMENDMENT TO AGREEMENT OF LEASE**

**THIS FIFTH AMENDMENT TO AGREEMENT OF LEASE** ("Fifth Amendment") is made this 12th day of December 2005, by and between **METRO PARK I, LLC**, a Delaware limited liability company ("Lessor") and **GOVCONNECTION, INC.**, a Maryland corporation, formerly known as Comteq Federal, Inc. ("Lessee").

**WITNESSETH:**

**WHEREAS**, Rockville Office/Industrial Associates, Lessor's predecessor in interest and Comteq Federal, Inc., Lessee's predecessor in interest, entered into that certain Lease dated December 14, 1993 (the "Original Lease"), as amended by that certain First Amendment to Lease dated November 1, 1996 (the "First Amendment"), as further amended by that certain Second Amendment to Agreement of Lease and Extension of Term dated as of March 31, 1998 (the "Second Amendment"), as further amended by that certain Third Amendment to Agreement of Lease dated as of August 31, 2000 (the "Third Amendment"), and as further amended by that certain Fourth Amendment to Agreement of Lease dated November 20, 2002 (the "Fourth Amendment") (the Original Lease, First Amendment, Second Amendment, Third Amendment and Fourth Amendment shall be referred to collectively as the "Lease"), pursuant to which Lessee leased that certain space in the building located at 7501 and 7503 Standish Place, Rockville, Maryland (the "Building"), said leased premises containing approximately Ten Thousand One Hundred Ninety-Six (10,196) rentable square feet of space (the "Premises");

**WHEREAS**, the Term of the Lease is scheduled to expire March 31, 2006; and

**WHEREAS**, Lessor and Lessee desire to amend the Lease to extend the Term of the Lease and modify and amend certain other terms and conditions of the Lease as herein provided.

**NOW, THEREFORE**, in consideration of the premises and mutual covenants and agreements herein contained and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Lessor and Lessee hereby agree to the following:

1. **Recitals.** The recitals set forth above are incorporated herein by this reference with the same force and effect as if fully set forth hereinafter.

2. **Capitalized Terms.** Capitalized terms not otherwise defined herein shall have the meaning ascribed to them in the Lease. The Lease and this Fifth Amendment shall be known collectively as the "Lease".

3. **Term.** The Term of the Lease is hereby extended for a period of three (3) years commencing on April 1, 2006 (the "Renewal Date") and expiring on March 31, 2009 (inclusively, the "Renewal Term"), unless terminated sooner pursuant to the provisions of the Lease or hereof.

4. **Base Rent.** Notwithstanding anything to the contrary contained in the Lease, as of the Renewal Date, Lessee shall pay Base Rent with respect to the Premises at the times and in the manner set forth in Section 2.1 of the Original Lease, as restated in Paragraph 5 of the Fourth Amendment, according to the following schedule:

<u>Lease Period</u>	<u>Monthly Base Rent</u>
04/01/06 – 03/31/07	\$ 16,780.92
04/01/07 – 03/31/08	\$ 17,284.35
04/01/08 – 03/31/09	\$ 17,802.88

5. **Base Year.** As of the Renewal Date, Section 2.2.4 of the Lease as set forth in Paragraph 5 of the Fourth Amendment, shall be modified by deleting the penultimate sentence therefrom and substituting the following in lieu thereof: "Lessee's Expense Base Year shall be the calendar year 2006."

6. **Security Deposit.** Lessor currently holds a Security Deposit under the Lease in the amount of Four Thousand Eight Hundred Ninety-Nine and No/100 Dollars (\$4,899.00). Lessee shall have no obligation to supplement such security deposit in connection with this Fifth Amendment.

7. **Lessee Improvements.** Lessee hereby accepts the Premises in its "as-is" condition existing on the Renewal Date. Lessor shall have no obligation to make any Lessee improvements to the Premises during the Renewal Term hereof.

8. **Option to Renew.** Lessee has exercised the option to renew the Lease pursuant to Paragraph 10 of the Fourth Amendment. Accordingly, Paragraph 10 of the Fourth Amendment is hereby deleted in its entirety and shall be of no further force and effect.

9. **Brokers.** Lessee represents and warrants to Lessor that Lessee has not had any dealings or entered into any agreements with any person, entity, realtor, broker, agent or finder in connection with the negotiation of this Fifth Amendment. Lessee shall indemnify and hold harmless Lessor from and against any loss, claim, damage, expense (including costs of suit and reasonable attorneys' fees) or liability for any compensation, commission or charges claimed by any realtor, broker, agent or finder claiming to have dealt with Lessee in connection with this Fifth Amendment.

10. **Reaffirmation of Terms.** Except as expressly modified hereby, all of the terms, covenants and provisions of the Lease are hereby confirmed and ratified and shall remain unchanged and in full force and effect.

11. **Representations.** Lessee hereby represents and warrants to Lessor that Lessee (i) is not in default of any of its obligations under the Lease and that such Lease is valid, binding and enforceable in accordance with its terms, (ii) has full power and authority to execute and perform this Fifth Amendment, and (iii) has taken all action necessary to authorize the execution and performance of this Fifth Amendment.

12. **Counterpart Copies.** This Fifth Amendment may be executed in two or more counterpart copies, each of which shall be deemed to be an original and all of which counterparts shall have the same force and effect as if the parties hereto had executed a single copy of this Fifth Amendment.

[SIGNATURES APPEAR ON NEXT PAGE]

IN WITNESS WHEREOF, Lessor and Lessee have executed this Fifth Amendment as of the day and year first above written.

**LESSOR:**

**METRO PARK I, LLC,**  
a Delaware limited liability company

By: PS Business Parks, L.P.,  
a California limited partnership,

By: PS Business Parks, Inc., a  
California corporation, its  
General Partner

By: /s/ William McFaul  
William A. McFaul  
Vice President

Date: 12/14/05  
Lessor's Execution Date

Lessor Fed. ID #: 91-1804826

**LESSEE:**

**GOVCONNECTION, INC.,**  
a Maryland corporation

By: /s/ Robert Howard  
Name: Robert Howard  
Title: Vice President of Sales

Date: 12-12-05  
Lessee's Execution Date

**OFFICE LEASE**

This lease ("Lease") is made as of January 6, 2006 by and between the Landlord and the Tenant named below.

**ARTICLE 1. BASIC LEASE TERMS**

For the purposes of this Lease the following underlined terms shall have the meanings set forth below:

**1.1 LANDLORD. RMC MIDWAY WALNUT, LP**

**1.2 TENANT. MOREDIRECT, INC.**

**1.3 BUILDING.** That certain office building commonly known as the Midway Atrium III located at 14295 Midway Road, in the City of Addison, Dallas County, Texas 75001. The Building and the land on which the Building is situated together with all other buildings, structures, fixtures and other improvements located thereon from time to time are collectively referred to herein as the "Property".

**1.4 LEASED PREMISES.** That portion of the Building highlighted on the Site Plan attached to this Lease as Exhibit "A", on the floor(s) indicated thereon, resulting in an aggregate area hereby deemed to consist of 3,267 rentable square feet in the Building, commonly referred to as Suite 110.

**1.5 LEASE TERM.** Forty-eight (48) months, beginning on the Commencement Date; provided that if the Commencement Date is a date other than the first (1<sup>st</sup>) day of a calendar month, the Lease Term shall be said number of months in addition to the remainder of the calendar month following the Commencement Date.

**1.6 COMMENCEMENT DATE.** The Commencement Date shall be the earliest to occur of (i) the date Tenant takes possession of the Leased Premises for the purpose of conducting its business therefrom, (ii) the Date of Substantial Completion (as defined in the Work Letter attached to this Lease as Exhibit "E" [if any]) or (iii) March 1, 2006. Notwithstanding the foregoing, the Commencement Date shall constitute the commencement of the Lease Term for all purposes, whether or not Tenant has actually taken possession of the Leased Premises.

**1.7 BASE RENT.** Tenant shall pay, in accordance with the terms and provisions of Section 2.2 of this Lease, Base Rent for the lease and use of the Leased Premises at the annual rental rate per rentable square foot of space in the Leased Premises for the specific time periods set forth below:

<u>Time Period</u>	<u>Annual Rental Rate Per Rentable Square Foot</u>	<u>Applicable Monthly Rent</u>
Months 1 – 48	\$ 13.50	\$3,675.38

**1.8 SECURITY DEPOSIT.** Three Thousand Six Hundred Seventy-Five and 38/100 Dollars (\$3,675.38), due and payable concurrently with the execution of this Lease.

**1.9 ADDRESSES.**

<u>Landlord's Address</u>	<u>Tenant's Address</u>	<u>Manager's Address</u>
RMC Midway Walnut, LP 5944 Luther Lane Suite 501 Dallas, Texas 75225	MoreDirect, Inc. 14295 Midway Road Suite 110 Addison, Texas 75001	R.M. Crowe Property Management, LP 14275 Midway Road Suite 120 Addison, Texas 75001

Landlord, Tenant and Manager, by written notice to the others may change from time to time their respective addresses, and Landlord, by written notice to Tenant, may notify Tenant from time to time of the appointment of a new Manager and such new Manager's address.

**1.10 PERMITTED USE.** To provide general office services and other lawful incidental office uses directly related thereto, but for no other purpose.

**1.11 COMMON AREAS.** Such parking areas, streets, driveways, aisles, sidewalks, curbs, delivery passages, loading areas, lighting facilities, and all other areas situated on or in the Property which are designated by Landlord, from time to time, for use by all tenants of the Property in common.

**1.12 GUARANTOR.** Intentionally deleted.

**1.13 BUILDING STANDARD HOURS.** Under all applicable terms and conditions of this Lease, Building Standard Hours shall be Monday through Friday, 7:00 a.m. through 6:00 p.m. and Saturday 8:00 a.m. through 1:00 p.m.

**ARTICLE 2. GRANTING CLAUSE AND RENT PROVISIONS**

**2.1 GRANT OF PREMISES.** In consideration of the obligation of Tenant to pay the rent and other charges as provided in this Lease and in consideration of the other terms and provisions of this Lease, Landlord hereby leases the Leased Premises to Tenant during the Lease Term, subject to the terms and provisions of this Lease. Tenant's parking rights are set forth in Exhibit "B" attached to this Lease.



**2.2 BASE RENT.** Tenant agrees to pay monthly the Base Rent set forth in Section 1.7 of this Lease, which Base Rent shall be payable by Tenant to Landlord at the address shown in Section 1.9 of the Lease or at such other address as Landlord in writing shall notify Tenant. One (1) monthly installment of Base Rent shall be due and payable on the date of execution of this Lease by Tenant for the first (1<sup>st</sup>) month's Base Rent and a like monthly installment shall be due and payable on or before the first (1<sup>st</sup>) day of each calendar month succeeding the Commencement Date during the Lease Term, without abatement, notice, demand, offset, reduction or counterclaim; provided, however, that if the Commencement Date should be a date other than the first (1<sup>st</sup>) day of a calendar month, the monthly rental set forth above shall be prorated to the end of that calendar month, and all succeeding installments of Base Rent shall be payable on or before the first (1<sup>st</sup>) day of each succeeding calendar month during the Lease Term.

**2.3 OPERATING EXPENSES; UTILITIES; AND TAXES.**

(a) The "Base Year" shall mean the calendar year 2006; provided, however, that in the event that the Property is less than ninety-five percent (95%) occupied during the Base Year, the Operating Expenses (defined below) for the Base Year shall be grossed up as if the Property were ninety-five percent (95%) occupied for the Base Year.

(b) If the Operating Expenses, in any calendar year during the Lease Term exceed the Operating Expenses for the Base Year, Tenant shall pay as additional rent Tenant's Proportionate Share (defined below) of Excess Operating Expenses (defined below). "Tenant's Proportionate Share" shall be the percentage obtained by dividing the number of rentable square feet in the Leased Premises by the total number of rentable square feet in the Property. "Excess Operating Expenses" shall mean the amount by which Operating Expenses in a particular calendar year exceed the Operating Expenses for the Base Year. Landlord may invoice Tenant monthly for Tenant's estimated share of Excess Operating Expenses for each calendar year, subsequent to the Base Year, beginning on the first day of the month of the first subsequent calendar year. Landlord may adjust its estimate by notice to Tenant at any time during the applicable calendar year if actual Operating Expenses are substantially different from the estimate, and thereafter payments by Tenant under this Section shall adjust accordingly. Within approximately one hundred twenty (120) days following the end of each calendar year, Landlord shall provide Tenant an accounting (the "Accounting") showing in reasonable detail all computations of additional rent under this Section. If the Accounting shows that the total of the monthly payments made by Tenant exceeds the amount of additional rent due by Tenant under this Section, the Accounting shall be accompanied by a refund. If the Accounting shows that the total of the monthly payments by Tenant is less than the amount of additional rent due by Tenant under this Section, the Accounting shall be accompanied by an invoice for the additional rent. Notwithstanding any other provisions in this Lease, Landlord, within one (1) year following the expiration of the Lease Term or earlier termination of this Lease, shall have the option to invoice Tenant for Tenant's

Proportionate Share of Excess Operating Expenses for the year in which this Lease terminates based upon that year's actual Operating Expenses. If this Lease shall terminate on a day other than the last day of a calendar year, the amount of any additional rent payable by Tenant applicable to the year in which such termination shall occur shall be prorated on the ratio that the number of days from the commencement of the calendar year to and including the termination date bears to 365. Notwithstanding anything to the contrary contained in this Lease, if the Property is not ninety-five percent (95%) occupied during any calendar year, Tenant's additional rent under this Section and the Operating Expenses shall be determined as if the Property had been ninety-five percent (95%) occupied during such year. Tenant agrees to pay any additional rent due under this Section within thirty (30) days following receipt of the invoice and/or Accounting showing additional rent due.

(c) The term "Operating Expenses" includes all expenses paid by Landlord with respect to the maintenance, servicing, repairing and operation of the Property, including, but not limited to the following: maintenance, repair and replacement costs; fuel, landscaping and pest control; management fees, including those payable to any affiliate of Landlord; wages and benefits payable to employees of Landlord whose duties are directly connected to the operation and maintenance of the Property; all service, supplies, repairs, replacement or other expenses for maintaining and operating the Property including parking and common area; the cost, including interest, amortized over its useful life, of any capital improvement made to the Property by Landlord which is required under any applicable Legal Requirements (defined below); the cost, including interest, amortized over its useful life, of installation of any device or other equipment designed or intended to improve the operating efficiency of any system within the Leased Premises; all other expenses which generally would be regarded as operating and maintenance expenses which would reasonably be amortized over a period not to exceed five (5) years; and all insurance premiums Landlord is required to pay or deems necessary to pay, including public liability insurance and casualty insurance, with respect to the Property. The term "Operating Expenses" does not include the following: Taxes (as hereinafter defined) and Utilities (as hereinafter defined); expenses for repairs, restoration or other work occasioned by fire, wind, the elements or other casualty that are covered by Landlord's insurance; income and franchise taxes of Landlord (except to the extent a tax on the rental income produced from the Property); expenses incurred in leasing to or procuring of tenants, leasing commissions, advertising expenses and expenses for the renovating of space for new tenants; interest or principal payments on any mortgage or other indebtedness of Landlord; any depreciation allowance or expense; or expenses which are the responsibility of Tenant.

(d) The "Tax Base Year" shall mean the calendar year 2006; provided, however, that in the event that the Property is less than ninety-five percent (95%) occupied during the Base Year, the Taxes for the Tax Base Year shall be grossed up as if the Property were ninety-five percent (95%) occupied for the Tax Base Year.

(e) If the Taxes, in any calendar year during the Lease Term exceed the Taxes for the Tax Base Year, Tenant shall pay as additional rent Tenant's Proportionate Share of Excess Taxes (defined below). "Excess Taxes" shall mean the amount by which Taxes in a particular calendar year exceed the Taxes for the Tax Base Year. Landlord may invoice Tenant monthly for Tenant's estimated share of Excess Taxes for each calendar year, subsequent to the Tax Base Year, beginning on the first day of the month of the first subsequent calendar year. Landlord may adjust its estimate by notice to Tenant at any time during the applicable calendar year if actual Taxes are substantially different from the estimate, and thereafter payments by Tenant under this Section shall adjust accordingly. Landlord and Tenant will follow the procedures for annual Accounting as stated in Section 2.3(b) above. Notwithstanding any other provisions in this Lease, Landlord, within one (1) year following the expiration of the Lease Term or earlier termination of this Lease, shall have the option to invoice Tenant for Tenant's Proportionate Share of Excess Taxes for the year in which this Lease terminates based upon that year's actual Taxes. Notwithstanding anything to the contrary contained in this Lease, if the Property is not ninety-five percent (95%) occupied during any calendar year, Tenant's additional rent under this Section and the Taxes shall be determined as if the Property had been ninety-five percent (95%) occupied during such year. Tenant agrees to pay any additional rent due under this Section within thirty (30) days following receipt of the invoice and/or Accounting showing additional rent due.

The term "Taxes" includes all ad valorem taxes paid by Landlord with respect to the Property, including, but not limited to all real property taxes and installments of special assessments, including dues and assessments by means of deed restrictions and/or owner's associations which accrue against the Property during the Lease Term (including costs of contesting assessed values and/or taxes); governmental levies or charges of any kind or nature assessed or imposed on the Property, whether by state, county, city or any political subdivision thereof.

(f) The "Utilities Base Year" shall mean the calendar year 2006; provided, however, that in the event that the Property is less than ninety-five percent (95%) occupied during the Base Year, the Utilities for the Utilities Base Year shall be grossed up as if the Property were ninety-five percent (95%) occupied for the Utilities Base Year.

(g) If the Utilities, in any calendar year during the Lease Term exceed the Utilities for the Utilities Base Year, Tenant shall pay as additional rent Tenant's Proportionate Share of Excess Utilities (defined below). "Excess Utilities" shall mean the amount by which Utilities in a particular calendar year exceed the Utilities for the Utilities Base Year. Landlord may invoice Tenant monthly for Tenant's estimated share of Excess Utilities for each calendar year, subsequent to the Utilities Base Year, beginning on the first day of the month of the first subsequent calendar year. Landlord may adjust its estimate by notice to Tenant at any time during the applicable calendar year if actual Utilities are substantially different from the estimate, and thereafter payments by Tenant under this Section shall adjust accordingly. Landlord and Tenant will follow the reconciliation and Accounting procedures established in Section 2.3(b) above.

Notwithstanding any other provisions in this Lease, Landlord, within one (1) year following the expiration of the Lease Term or earlier termination of this Lease, shall have the option to invoice Tenant for Tenant's Proportionate Share of Excess Utilities for the year in which this Lease terminates based upon that year's actual Utilities. Notwithstanding anything to the contrary contained in this Lease, if the Property is not ninety-five percent (95%) occupied during any calendar year, Tenant's additional rent under this Section and the Utilities shall be determined as if the Property had been ninety-five percent (95%) occupied during such year. Tenant agrees to pay any additional rent due under this Section within thirty (30) days following receipt of the invoice and/or Accounting showing additional rent due.

(h) The term "Utilities" includes all utility expenses paid by Landlord with respect to the maintenance, servicing, repairing and operation of the Property, including, but not limited to the following: cable, telephone, electricity, water, sewer, gas.

**2.4 ADDITIONAL RENT.** Tenant agrees to pay all rent and other sums of money (whether specified in this Article 2, pursuant to indemnity or reimbursement obligations or otherwise) as shall become due from and payable by Tenant to Landlord under this Lease (collectively, the "Rent") at the times and in the manner provided in this Lease, without abatement, notice, demand, offset, reduction or counterclaim (except as otherwise provided in this Lease). All Rent in addition to Base Rent shall constitute additional rental under this Lease and Landlord shall be entitled to exercise the same rights and remedies provided for in this Lease for the nonpayment of any Rent.

**2.5 LATE PAYMENT CHARGE.** Other remedies for nonpayment of Rent notwithstanding, if any regular monthly installment of Rent is not received by Landlord on or before the fifth (5<sup>th</sup>) day of the month for which such Rent is due, a late payment charge of ten percent (10%) of such past due amount shall become due and payable in addition to any other amounts due and payable. In addition, all Rent owed by Tenant to Landlord under this Lease shall bear interest from the date due until the date received at a rate (the "Interest Rate") equal to the lesser of the highest rate allowable under applicable law or eighteen percent (18%) per annum.

**2.6 INCREASE IN INSURANCE PREMIUMS.** If an increase in any insurance premiums paid by Landlord for the Property is caused by Tenant's use of the Leased Premises in a manner other than as set forth in Section 1.10 of this Lease, or if Tenant vacated the Leased Premises and caused an increase in such premiums, then Tenant shall pay as additional rent the amount of such increase to Landlord. Tenant agrees to pay any amount due under this Section within ten (10) days following receipt of the invoice showing the additional rent due.

**2.7 SECURITY DEPOSIT.** The Security Deposit (if any), as set forth in Section 1.8 of this Lease, shall be paid by Tenant to Landlord, in cash or by certified check, on the date of execution of this Lease by Tenant and shall be held by Landlord as security for the performance of Tenant's covenants and obligations under this Lease, it being expressly understood that the Security Deposit shall not be considered an advance payment of Rent or a measure of Landlord's

damages in case of default hereunder by Tenant, and shall be held by Landlord without payment of any interest thereon. Upon the occurrence of any event of default or breach of a covenant by Tenant under this Lease, Landlord may, from time to time, without prejudice to any other remedy, use the Security Deposit to the extent necessary to make good any arrearage of Rent, or to repair any damage or injury, or pay any expense or liability incurred by Landlord as a result of such event of default or breach of covenant, and any remaining balance of the Security Deposit shall be returned by Landlord to Tenant upon the termination of this Lease. If any portion of the Security Deposit is so used or applied, Tenant shall upon ten (10) days written notice from Landlord, deposit with Landlord, by cash or certified check, an amount sufficient to restore the Security Deposit to its original amount. The Security Deposit may be assigned and transferred by Landlord to the successor in interest of Landlord and, upon acknowledgment by such successor of receipt of such Security Deposit and its assumption of the obligation to account to Tenant for the Security Deposit in accordance with the terms and provisions of this Lease, Landlord shall thereby be discharged of any further obligation relating thereto.

**2.8 HOLDING OVER.** If Tenant does not vacate the Leased Premises upon the expiration or earlier termination of this Lease, as may be extended by Tenant pursuant to Tenant's exercise of the option to extend set forth in Rider "1" attached to this Lease, Tenant shall be deemed to be holding over, and all of the terms and provisions of this Lease shall be applicable during the holdover period, except that (i) the term of Tenant's tenancy shall be terminable at any time by either party and (ii) Tenant shall pay Landlord (in addition to additional rent and any other sums payable under this Lease) as base rental for the period of such holdover an amount equal to two (2) times the greater of (a) the Base Rent which was payable by Tenant during the last month of the initial Lease Term or (b) the then current market rent for the Leased Premises (without waiver of Landlord's right to recover damages as permitted by law). Upon the expiration of this Lease, Tenant agrees to vacate and deliver the Leased Premises (and all keys thereto) in good condition, to Landlord upon delivery to Tenant of notice from Landlord to vacate. The Rent payable during the holdover period shall be payable to Landlord on demand. No holding over by Tenant, whether with or without the consent of Landlord, shall operate to extend the Lease Term. Tenant shall indemnify Landlord against all claims made by any tenant or prospective tenant against Landlord resulting from delay by Landlord in delivering possession of the Leased Premises to such other tenant or prospective tenant.

**2.9 SURRENDER OF LEASED PREMISES.**

(a) Upon the expiration or earlier termination of this Lease, Tenant shall peaceably surrender to Landlord the Leased Premises broom-clean and in the condition the same were in on the Commencement Date, subject only to (i) ordinary and customary wear and tear, and (ii) damage resulting from condemnation, a fire or other casualty.

(b) Notwithstanding anything in this Lease to the contrary, all permanent or built-in fixtures or improvements and all mechanical, electrical and plumbing ("MEP") equipment in the Leased Premises shall be the property of Landlord upon the expiration or earlier termination of this Lease. Except as otherwise provided, all furnishings, equipment, furniture, trade fixtures and other removable equipment installed in the

Leased Premises by Tenant and paid for by Tenant shall remain the property of Tenant and shall be removed by Tenant upon the expiration or termination of this Lease. Tenant shall repair any damage caused by such removal. If any of Tenant's furnishings, equipment, furniture, trade fixtures or other removable equipment are not removed on or prior to the expiration or earlier termination of this Lease, then Tenant hereby grants to Landlord the option, exercisable at any time thereafter without the requirement of any notice to Tenant: (i) to treat such property or any portion thereof as being abandoned by Tenant to Landlord, whereupon Landlord shall be deemed to have full rights of ownership thereof; (ii) to elect to remove and store such property, or any portion thereof, on Tenant's behalf (but without assuming any liability to any person) and at Tenant's sole cost and expense, with reimbursement therefor to be made to Landlord upon demand; and/or (iii) to sell, give away, donate or dispose of as trash or refuse any or all of such property without any responsibility to deliver to Tenant any proceeds therefrom. Landlord shall have no liability of any kind whatsoever to Tenant with respect to the exercise or failure to exercise the options set forth in this Section 2.9(b). Specifically, Tenant shall not have the right to assert against Landlord a claim either for the value, or the use, of any such property, either as an offset against any amount of money owing to Landlord or otherwise.

### ARTICLE 3. OCCUPANCY, USE AND OPERATIONS

**3.1 USE.** Tenant warrants and represents to Landlord that the Leased Premises shall be used and occupied only for the purpose as set forth in Section 1.10 of this Lease. Tenant shall occupy the Leased Premises, conduct its business and control its agents, employees, invitees and visitors in such a manner as is lawful, reputable and will not create a nuisance to other tenants in the Property. Tenant shall not solicit business, distribute handbills or display merchandise within the Common Areas. Tenant shall not permit any operation which emits any odor or matter which intrudes into other portions of the Property, use any apparatus or machine which makes undue noise or causes vibration in any portion of the Property or otherwise interfere with, annoy or disturb any other tenant in its normal business operations or Landlord in its management of the Property. Tenant shall neither permit any waste on the Leased Premises nor allow the Leased Premises to be used in any way which would, in the opinion of Landlord, be extra hazardous on account of fire or which would in any way increase the cost of or render void the fire insurance on the Property. Tenant may not use or allow or permit the Leased Premises to be used in any way or for any purpose that is visible from the exterior of the Leased Premises, adversely affects ventilation in other areas of the Building, creates unreasonable elevator loads, causes structural loads to be exceeded, creates unreasonable noise levels, or is in violation of any applicable Legal Requirements (defined below).

**3.2 SIGNS.** No signs of any type or description shall be erected, placed or painted by Tenant on or about the exterior of the Leased Premises without the prior written consent of Landlord. Landlord reserves the right to remove, at Tenant's expense, all exterior signs other than signs approved in writing by Landlord under this Section 3.2, without notice to Tenant, and Landlord shall not be liable to Tenant for damages sustained by Tenant as a result thereof. Tenant shall be permitted to erect signage within the interior of the Leased Premises, provided that all such signage be removed by Tenant upon the expiration or earlier termination of this Lease. Tenant shall repair any damage caused by such removal.

**3.3 COMPLIANCE WITH LAWS, RULES AND REGULATIONS.** Tenant, at Tenant's sole cost and expense, shall comply with all laws, ordinances, orders, rules and regulations of any and all state, federal, municipal and/or other agencies and/or bodies having jurisdiction over the use, condition or occupancy of the Leased Premises, or which are applicable in the jurisdiction(s) in which the Property is located (all of the foregoing, the "Legal Requirements"). Tenant shall procure at its own expense all permits and licenses required for the transaction of its business in the Leased Premises. Tenant will comply with the Rules and Regulations of the Property adopted by Landlord which are set forth in Exhibit "D" attached to this Lease. If Tenant is not complying with the Rules and Regulations, or if Tenant is in any way not complying with any term or provision of this Article 3, then, notwithstanding anything to the contrary contained herein, Landlord may, at its election, enter the Leased Premises without liability therefor and fulfill Tenant's obligations, provided, however, Tenant may contest same in good faith, provided that such contest is made in a lawful manner. Tenant shall reimburse Landlord on demand for any expenses which Landlord may incur in effecting compliance with Tenant's obligations and agrees that Landlord shall not be liable for any damages resulting to Tenant from such action. Landlord shall have the right at all times to change and amend the Rules and Regulations in any reasonable manner as it may deem advisable for the safety, care, cleanliness, preservation of good order and operation or use of the Property or the Leased Premises. All changes and amendments to the Rules and Regulations of the Property will be forwarded by Landlord to Tenant in writing and shall thereafter be carried out and observed by Tenant.

**3.4 WARRANTY OF POSSESSION.** Landlord and Tenant each hereby warrants to the other that it has the right and authority to execute this Lease, and Landlord warrants to Tenant, that upon payment of the required Rent by Tenant and compliance by Tenant with all the terms, provisions, conditions, covenants and agreements contained in this Lease, Tenant shall have possession of the Leased Premises during the Lease Term, as well as any extension or renewal thereof, without hindrance from Landlord or any person or persons lawfully claiming the Leased Premises by, through or under Landlord (but not otherwise); subject, however, to all mortgages, deeds of trust, leases and agreements to which this Lease is subordinate and to all Legal Requirements.

**3.5 LANDLORD'S RIGHT OF ENTRY.** Without limitation of Landlord's other rights of entry set forth in this Lease, Landlord or its authorized agents, with prior notice to Tenant, shall at any and all reasonable times have the right to enter the Leased Premises during Building Standard Hours to inspect the same, and to supply janitorial service or any other service to be provided by Landlord. Upon prior written notice to Tenant, Landlord may enter the Leased Premises to show the Leased Premises to prospective mortgagees or prospective purchasers. Upon prior written notice to Tenant, and for a period of time beginning ninety (90) calendar days prior to the expiration of the Lease Term, Landlord may enter the Leased Premises to show the Leased Premises to prospective tenants; provided, however, Landlord's right to show the Leased Premises to prospective tenants shall terminate upon Tenant's submission of its notice to extend

the Lease Term pursuant to Tenant's exercise of the option to extend set forth in Rider "1". Landlord shall at all times have and retain a key with which to unlock all of the doors in, upon and about the Leased Premises. Notwithstanding anything to the contrary contained herein, Landlord shall have the right at all times to enter the Leased Premises by any means in the event of an emergency without liability therefor.

**3.6 PERSONAL PROPERTY TAXES.** Tenant shall be liable for all taxes levied against leasehold improvements, merchandise, personal property, trade fixtures and all other taxable property located in the Leased Premises. If any such taxes for which Tenant is liable are levied against Landlord or Landlord's property and if Landlord elects to pay the same or if the assessed value of Landlord's property is increased by inclusion of personal property and trade fixtures placed by Tenant in the Leased Premises and Landlord elects to pay the taxes based on such increase, Tenant shall pay to Landlord, upon demand, that part of such taxes for which the Tenant is primarily liable pursuant to the terms of this Section. Tenant shall pay when due all taxes related to Tenant's use and operation of its business in the Leased Premises.

**3.7 EARLY OCCUPANCY.** If for any reason, Tenant or any of its employees, agents, contractors, guests or invitees enter the Leased Premises prior to the Commencement Date, Tenant acknowledges and agrees that such entrance into the Leased Premises shall be subject to each and every term and provision of this Lease, other than those requiring Tenant to pay Base Rent or additional rent as a result of such occupancy prior to the Commencement Date.

#### ARTICLE 4. UTILITIES AND SERVICE

**4.1 BUILDING SERVICES.** Landlord shall furnish Tenant water at those points of supply provided for general use of other tenants in the Building (subject to the terms and provisions of Sections 7.1, 7.2, 8.1 and 8.2 of this Lease), electrical power not to exceed at any given time four (4) watts per rentable square foot of space in the Leased Premises, pest control, and central heating and air conditioning in season, on business days during Building Standard Hours, and at temperatures and in amounts as are considered by Landlord to be standard or in compliance with any applicable Legal Requirements; provided that heating and air conditioning service at times other than Building Standard Hours shall be furnished by way of overtime heating and air conditioning. In accordance with, and subject to, the terms and provisions set forth below in this Section 4.1, Tenant must notify Landlord at least twenty-four (24) hours in advance of Tenant's need for overtime heating and air conditioning and Tenant shall bear the entire cost thereof at the rate established by Landlord from time to time (currently, Fifty and No/100 Dollars (\$50.00) per hour per half-floor) and will be billed monthly by Landlord. Landlord shall provide routine maintenance, painting and electric lighting service for all Common Areas and for any special service areas of the Property (as designated by Landlord) in the manner and to the extent deemed by Landlord to be standard. Landlord may, in its sole discretion, provide additional services not enumerated herein. Failure by Landlord to any extent to provide these defined services or any other services not enumerated, or any cessation thereof, shall not render Landlord liable in any respect for damages to either person or property, be construed as an eviction of Tenant, work as an abatement of Rent or relieve Tenant from fulfillment of any covenant or obligation under this Lease. If any of the equipment or machinery



which is useful or necessary for provision of utility services, and for which Landlord is responsible, breaks down or for any cause ceases to function properly, Landlord shall use reasonable diligence to repair the same promptly, but Tenant shall have no claim for abatement of Rent or offset or damages on account of any interruption in service occasioned from such repairs. Landlord reserves the right from time to time to make changes in the utilities and services provided by Landlord to the Property (including the Leased Premises).

**4.2 THEFT OR BURGLARY.** Landlord shall not be liable to Tenant for losses to Tenant's property or personal injury caused by criminal acts or entry by unauthorized persons in the Leased Premises or on the Property.

**4.3 JANITORIAL SERVICE.** Landlord shall furnish janitorial service to the Leased Premises and the Common Areas of the Building five (5) times per week during the Lease Term, excluding holidays. Landlord shall not provide janitorial service to kitchen or storage areas located in the Leased Premises. Should (i) Landlord fail to provide or (ii) Tenant elect not to receive, janitorial or any other building service, Landlord shall not be liable to Tenant in any respect for damages, nor shall such failure or election work as an abatement of Rent or relieve Tenant from fulfillment of any covenant or obligation under this Lease.

**4.4 EXCESSIVE UTILITY CONSUMPTION.** Without limitation of the terms and provisions set forth in Section 2.3 of this Lease, Tenant shall pay all utility costs occasioned by electrodata processing machines, telephone equipment, computers and other equipment of high electrical consumption as determined by Landlord, including (without limitation) the cost of installing, servicing and maintaining any special or additional inside or outside wiring or lines, meters or submeters, transformers, poles, air conditioning costs, or the cost of any other equipment necessary to increase the amount or type of electricity or power available to the Leased Premises. If Tenant's electricity use exceeds the limits specified in Section 4.1 of this Lease or any of Tenant's equipment generates excessive heat, Landlord may also, at its sole option and without any obligation to do so, install supplemental air conditioning units in and/or meters for the Leased Premises to monitor Tenant's excess electricity usage and/or to offset the heat-generating effect of Tenant's excess electricity usage and Tenant's equipment and Tenant shall pay Landlord the installation cost and the cost of operation, use, repair, and replacement of such supplemental air conditioning units and/or meters on demand as additional rent.

**4.5 WINDOW COVERINGS.** Landlord may (but shall not be obligated to) furnish and install window coverings on all exterior windows to maintain a uniform exterior appearance. Tenant shall not remove or replace these window coverings or install any other window covering which would affect the exterior appearance of the Building. Tenant may install lined or unlined over draperies on the interior sides of the Landlord furnished window coverings for interior appearance or in order to reduce light transmission, provided such over draperies do not (in Landlord's determination) affect the exterior appearance of the Building or affect the operation of the Building's heating, ventilating and air conditioning systems.

**4.6 CHARGE FOR SERVICE.** All costs of Landlord for providing the services set forth in this Article 4 shall be subject to the additional rent provisions in Article 2 of this Lease and shall be payable as therein provided.

## **ARTICLE 5. REPAIRS AND MAINTENANCE**

**5.1 LANDLORD REPAIRS.** Landlord shall not be required to make any improvements, replacements or repairs of any kind or character in or to the Leased Premises during the Lease Term except as set forth in this Section. Landlord shall maintain only the roof, foundation, parking and Common Areas, elevators, the structural soundness of the exterior walls, doors, corridors, windows, and other structures or equipment servicing the Leased Premises. Landlord's cost of maintaining and repairing the items set forth in this Section are subject to the provisions set forth in Section 2.3 of this Lease. Landlord shall not be liable to Tenant, except as expressly provided in this Lease, for any damage or inconvenience, and Tenant shall not be entitled to any damages nor to any abatement, offset or reduction of Rent by reason of any repairs, alterations or additions made by Landlord under this Lease.

**5.2 TENANT REPAIRS.** Tenant, at its own costs and expense, shall maintain the Leased Premises in a first-class condition (except for those items that are the responsibility of Landlord under Section 5.1 of this Lease) and shall repair, maintain and/or replace any damage or injury to all or any part of the Leased Premises and/or the Property caused by any act or omission of Tenant or Tenant's agents, employees, invitees, licensees or visitors. All repairs and replacements must be equal in quality and class to the original work. If Tenant fails to commence any such repairs and/or replacements within five (5) days after written notice from Landlord, and thereafter diligently proceed with such repair until completion, then Landlord may at its option make the repairs and replacements and Tenant shall pay Landlord on demand as additional rent the costs incurred by Landlord plus any administrative fee equal to fifteen percent (15%) of the costs. If Tenant requests Landlord to perform any maintenance or repairs to the Leased Premises, over and above the services required to be performed by Landlord pursuant to Article 4 of this Lease, Tenant shall pay the actual cost thereof, plus an administrative fee equal to fifteen percent (15%) of the actual cost thereof, to Landlord as additional rent within five (5) business days after demand.

**5.3 REQUEST FOR REPAIRS.** All requests for repairs or maintenance that are the responsibility of Landlord pursuant to any provision of this Lease must be made in writing to Landlord at the address in Section 1.9 of this Lease.

**5.4 TENANT DAMAGES.** Tenant shall not allow any damage to be committed on any portion of the Leased Premises or the Property, and at the termination of this Lease, by lapse of time or otherwise, Tenant shall deliver the Leased Premises to Landlord in accordance with all terms and provisions of Section 2.9 of this Lease in as good condition as existed at the Commencement Date of this Lease, reasonable wear and tear and casualty excepted. The cost and expense of any repairs necessary to restore the condition of the Leased Premises shall be borne by Tenant.

## ARTICLE 6. ALTERATIONS AND IMPROVEMENTS

### 6.1 CONSTRUCTION.

(a) If any construction or tenant improvements are to be performed in or to the Leased Premises in connection with Tenant's initial occupancy of the Leased Premises under this Lease, then such construction shall be accomplished, and the cost of such construction shall be borne by Landlord and/or Tenant in accordance with the terms and provisions of the Work Letter attached hereto as Exhibit "E" (if any), and Landlord and Tenant hereby agree to comply with all terms and provisions of the same.

(b) Tenant has made a complete examination and inspection of the Leased Premises and, except as may be expressly provided to the contrary in Exhibit "E" (if any), Tenant accepts the Leased Premises in its current condition, as-is, where-is and with all faults, without recourse to Landlord, and Landlord shall have no obligation to complete any improvements in or to the Leased Premises. ADDITIONALLY, LANDLORD SHALL MAKE NO WARRANTIES, EXPRESS OR IMPLIED, WITH RESPECT TO THE LEASEHOLD IMPROVEMENTS IN THE LEASED PREMISES. ALL IMPLIED WARRANTIES WITH RESPECT THERETO, INCLUDING BUT NOT LIMITED TO THOSE OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE, ARE EXPRESSLY NEGATED AND WAIVED. Furthermore, subject to the terms of Exhibit "E" (if any), Tenant hereby waives any defects in the Leased Premises and acknowledges and accepts (1) the Leased Premises as suitable for the purpose for which they are leased and (2) the Property and every part and appurtenance thereof as being in good and satisfactory condition. Upon the request of Landlord, Tenant shall deliver to Landlord a completed acceptance of premises memorandum in Landlord's standard form.

**6.2 TENANT IMPROVEMENTS.** Tenant shall not make or allow to be made any alterations, physical additions or improvements to the Leased Premises without first obtaining the written consent of Landlord, which consent may in the sole and absolute discretion of Landlord be denied. If Landlord is requested to make any such alterations, physical additions or improvements for Tenant, Tenant shall pay to Landlord, in addition to the cost of such work, a fee equal to fifteen percent (15%) of the cost of such work. Any alterations, physical additions or improvements to the Leased Premises made by or installed by either party hereto shall remain upon and be surrendered with the Leased Premises and become the property of Landlord upon the expiration or earlier termination of this Lease without credit to Tenant; provided, however, Landlord at its option may require Tenant to remove any physical improvement or additions and/or repair any alterations in order to restore the Leased Premises to the condition existing at the time Tenant took possession (all cost of such removal and/or repairs to be borne by Tenant). The foregoing sentence shall not apply to moveable equipment, furniture, or movable trade fixtures owned by Tenant, which items may be removed by Tenant at the end of the Lease Term if Tenant is not then in default and if such equipment and furniture are not then subject to any other rights, liens and interests of Landlord. Tenant shall have no authority or power, express or implied, to create or cause any mechanic's or materialmen's lien, charge or encumbrance of any kind against the Leased Premises, the Property or any portion thereof. Tenant shall promptly

cause any such liens that have arisen by reason of any work claimed to have been undertaken by or through Tenant to be released by payment, bonding or otherwise within thirty (30) days after request by Landlord, and shall indemnify Landlord against losses arising out of any such claim or claims (including, without limitation, legal fees and costs of court). Alterations, improvements, and additions in and to the Leased Premises requested by Tenant must be made in accordance with complete and accurate plans and specifications and construction documents (including, without limitation, complete MEP requirements) prepared by Tenant and approved in advance by Landlord. All work must be performed at Tenant's expense either by Landlord or by contractors and/or subcontractors approved in advance by Landlord. Tenant shall ensure that all workers are cooperative with Property personnel and comply with all Property rules and regulations. Tenant must deliver to Landlord evidence that Tenant has obtained all necessary governmental permits and approvals for the improvements or alterations prior to starting any work. All construction must be done in a good and workmanlike manner and is subject to approval by Landlord during and after construction to determine compliance with the approved plans and specifications and construction documents, in Landlord's sole discretion. Tenant must use Landlord's fire protection contractor and must either (1) use Landlord's MEP engineer to prepare the MEP portions of the plans and specifications and construction documents, or (2) reimburse the cost of one review by Landlord's MEP engineer of the plans and specifications and construction documents. All alterations and improvements by Tenant must comply with all Legal Requirements. If Tenant's use of or alterations or additions to the Leased Premises cause Landlord to make any alterations or improvements to the Property to comply with the provisions of the Americans With Disabilities Act of 1990 (as amended), the Texas Architectural Barriers Act (as amended) [Tex. Rev. Civ. Stat. Ann. Art. 9102], and/or any other similar law, rule or regulation relating to access by disabled persons to the Leased Premises or the Property, Tenant shall reimburse Landlord for the cost of the alterations or improvements (plus a fee equal to fifteen percent (15%) of such costs) upon demand as additional rent.

**6.3 COMMON AND SERVICE AREA ALTERATIONS.** Landlord shall have the right (i) to decorate and to make repairs, alterations, additions, changes or improvements, whether structural or otherwise, in, about or on the Property or any part thereof, (ii) to change, alter, relocate, remove or replace Common Areas and any special service areas of the Property (as designated by Landlord), (iii) to place, inspect, repair and replace in the Leased Premises (below floors, above ceilings or next to columns) utility lines, pipes and the like in order to serve other areas of the Property outside the Leased Premises and (iv) to otherwise alter or modify the Property, and for such purposes (set forth in subclauses (i) through (iv) above) Landlord shall have the right to enter upon the Leased Premises and, during the continuance of any such work, to take such measures for safety or for the expediting of such work as may be required, in Landlord's judgment, all without affecting any of Tenant's obligations hereunder, and without entitling Tenant to any damages or to any abatement, offset or reduction of Rent.

**ARTICLE 7. CASUALTY AND INSURANCE**

**7.1 SUBSTANTIAL DESTRUCTION.** If in the determination of Landlord (i) the Leased Premises should be totally destroyed by fire or other casualty, (ii) the Leased Premises should be damaged so that rebuilding cannot be substantially completed within one hundred

eighty (180) working days after Landlord's receipt of written notification by Tenant of such damage, or (iii) the Leased Premises are damaged or destroyed by casualty not covered by Landlord's fire and extended coverage insurance, then, at Landlord's sole option, this Lease may be terminated. If the Property or the Building is so damaged by fire or other casualty that substantial alteration or reconstruction of the Property or the Building is, in Landlord's sole opinion, required (whether or not the Leased Premises are damaged) or if any mortgagee under a mortgage or deed of trust covering the Property requires that the insurance proceeds payable as a result of the fire or other casualty be used to pay down or retire the mortgage debt, Landlord may, at its sole option, terminate this Lease. If Landlord terminates this Lease under this Section, Rent shall be abated for the unexpired portion of the Lease, effective as of the date of Tenant's written notification to Landlord of the applicable destruction and/or damage.

**7.2 PARTIAL DESTRUCTION.** In the event that the Leased Premises, or any portion thereof, shall be damaged by fire or other casualty, Tenant shall provide Landlord written notice of the same as soon as practicable thereafter. If following damage or destruction to the Leased Premises by fire or other casualty, this Lease is not terminated pursuant to Section 7.1 of this Lease, Landlord shall proceed, to the extent of insurance proceeds actually received by Landlord after the exercise by a mortgagee of the Property of an option to apply proceeds against Landlord's debt to such mortgagee, with reasonable diligence to rebuild or repair the Building or other improvements to substantially the same conditions in which they existed prior to such damage or destruction. If the Leased Premises are to be rebuilt or repaired and are untenable in whole or in part following the damage, and the damage or destruction was not caused or contributed to by act or negligence of Tenant, its agents, employees, invitees or others for whom Tenant is responsible, the Rent payable under this Lease during the period for which the Leased Premises are untenable shall be reduced to an amount determined by multiplying the Base Rent that would otherwise be payable but for this provision by the ratio that the portion of Leased Premises not rendered untenable bears to the total net rentable area of the Leased Premises prior to the casualty. Landlord's obligation to rebuild or restore under this Section shall be limited to restoring the Leased Premises to substantially the condition in which the same existed prior to the casualty, exclusive of improvements for which Tenant is responsible under the terms of Exhibit "E" (if any) described in Section 6.1 of this Lease, and Tenant shall, promptly after the completion of such work by Landlord, proceed with reasonable diligence (and at Tenant's sole cost and expense) to restore those improvements for which Tenant is responsible under the terms of Exhibit "E" (if any) to substantially the condition in which the same existed prior to the casualty and to otherwise make the Leased Premises suitable for Tenant's use. Landlord shall in no event be obligated to expend for such repair or replacements any amount in excess of the insurance proceeds actually received by Landlord (i.e. after the exercise by a mortgagee of the Property of an option to apply proceeds against Landlord's debt to such mortgagee). If the cost of repair and replacements for the leasehold improvements (based on Landlord's or its contractor's estimate of the cost) exceeds the insurance proceeds received by Landlord from Tenant's insurance carrier (which Tenant shall cause its insurance carrier to pay to Landlord), the shortfall shall be paid by Tenant to Landlord prior to Landlord's repair of the damage (to the extent to which Landlord is required to perform such repairs and replacements under the terms and provisions of this Section 7.2 and/or Exhibit "E" [if any]). Landlord is not liable for any inconvenience or annoyance to Tenant or injury to the business of Tenant resulting in any way

from casualty damage or any repairs related to the same. If Landlord has failed to substantially complete the repairs and/or replacements required by this Section 7.2 and/or Exhibit "E" (if any) within two hundred seventy (270) working days from the date of Landlord's receipt of written notification by Tenant of the applicable damage or destruction at issue, Tenant may at its option terminate this Lease by delivering written notice of such termination to Landlord prior to the date on which Landlord has substantially completed Landlord's work under this Section 7.2 and/or Exhibit "E" (if any).

**7.3 PROPERTY INSURANCE.** Landlord shall at all times during the Lease Term insure the Property against all risk of direct physical loss in such amounts and with such deductibles as Landlord considers appropriate; provided, Landlord shall not be obligated in any way or manner to insure any personal property (including, but not limited to, any furniture, machinery, goods or supplies) of Tenant upon or within the Leased Premises, any fixtures installed or paid for by Tenant upon or within the Leased Premises, or any improvements which Tenant may construct on the Leased Premises. Tenant shall have no right in or claim to the proceeds of any policy of insurance maintained by Landlord even if the cost of such insurance is borne by Tenant as set forth in Article 2 of this Lease. Landlord shall have the right to self-insure. At all times during the Lease Term, Tenant shall, at its own expense, keep in full force and effect insurance against fire and such other risks as are from time to time included in standard all-risk insurance (including coverage against vandalism and malicious mischief) for the full insurable value of Tenant's trade fixtures, furniture, supplies and all items of personal property of Tenant located upon or within the Leased Premises. Landlord shall be named as an additional insured on said policy.

**7.4 WAIVER OF SUBROGATION.** ANYTHING IN THIS LEASE TO THE CONTRARY NOTWITHSTANDING, LANDLORD AND TENANT HEREBY WAIVE AND RELEASE EACH OTHER OF AND FROM ANY AND ALL RIGHTS OF RECOVERY, CLAIM, ACTION OR CAUSE OF ACTION, AGAINST EACH OTHER, THEIR AGENTS, OFFICERS AND EMPLOYEES, FOR ANY LOSS OR DAMAGE THAT MAY OCCUR TO THE LEASED PREMISES, IMPROVEMENTS TO THE PROPERTY, OR PERSONAL PROPERTY WITHIN THE PROPERTY **REGARDLESS OF CAUSE OR ORIGIN, INCLUDING THE NEGLIGENCE OF LANDLORD OR TENANT AND/OR THE AGENTS, OFFICERS AND/OR EMPLOYEES OF EITHER, IF SUCH LOSS OR DAMAGE IS COVERED BY INSURANCE.** LANDLORD AND TENANT AGREE IMMEDIATELY TO GIVE THEIR RESPECTIVE INSURANCE COMPANIES WHICH HAVE ISSUED POLICIES OF INSURANCE COVERING ALL RISK OF DIRECT PHYSICAL LOSS, WRITTEN NOTICE OF THE TERMS OF THE MUTUAL WAIVERS CONTAINED IN THIS SECTION, AND TO HAVE THE INSURANCE POLICIES PROPERLY ENDORSED, IF NECESSARY TO PREVENT THE INVALIDATION OF THE INSURANCE COVERAGE BY REASON OF THE MUTUAL WAIVERS.

**7.5 HOLD HARMLESS.** Landlord shall not be liable to Tenant or to Tenant's customers, employees, agents, guests or invitees, or to any other person whomever, for any injury to persons or damage to property on or about the Leased Premises or the Common Areas, including but not limited to, consequential damage, (1) caused by any act or omission of Tenant,

its employees, subtenants, licensees and concessionaires or of any other person entering the Property or the Leased Premises by express or implied invitation of Tenant, or (2) arising out of the use of the Leased Premises or the Property by Tenant, its employees, subtenants, licensees, concessionaires or invitees, or (3) arising out of any breach or default by Tenant in the performance of its obligations hereunder, or (4) caused by the improvements located in the Leased Premises becoming out of repair or by any defect in or failure of equipment, pipes, or wiring, or by broken glass, or by the backing of drains, or by gas, water, steam, electricity or oil leaking, escaping or flowing into the Leased Premises or the Property, or (5) arising out of the failure or cessation of any service provided by Landlord (including, without limitation, security services and devices), and Tenant hereby agrees to indemnify Landlord and hold Landlord harmless from any liability, loss, expense or claim (including, without limitation, reasonable attorney's fees and costs of court) arising out of any such damage or injury. Landlord shall not be liable to Tenant for any loss or damage that may be occasioned by or through the acts or omissions of Tenant or of any other persons whomsoever. Further, Tenant specifically agrees to be responsible for and to indemnify and hold Landlord harmless from any and all damages or expenses of whatever kind arising out of or caused by burglary, theft, vandalism, malicious mischief or any other illegal act performed in, at or from the Leased Premises.

**7.6 LIABILITY INSURANCE.** Tenant at all times during the Lease Term shall, at its own expense, keep in full force and effect comprehensive general liability insurance with "personal injury" coverage and contractual liability coverage, within minimum limits of Two Million and No/100 Dollars (\$2,000,000.00) on account of bodily injuries to, or death of, one or more than one person as the result of any one accident or occurrence and Five Hundred Thousand and No/100 Dollars (\$500,000.00) on account of damage to property as the result of any one accident or occurrence. Landlord and Landlord's lenders shall be named as additional insureds on such policy, and such policy shall provide that (i) such insurance shall be primary and shall not contribute with any insurance carried by Landlord and (ii) the insurance company issuing the same shall notify Landlord thirty (30) days prior to the expiration date of the policy if the policy is not renewed prior to such date. All insurance policies or duly executed certificates for the same required to be carried by Tenant under this Lease, together with satisfactory evidence of the payment of the premiums thereof, shall be deposited with Landlord on the date Tenant first occupies the Leased Premises and upon renewals of such policies not less than fifteen (15) days prior to the expiration of the term of the same. All insurance required to be carried by Tenant under this Lease shall be in form and content, and written by insurers, reasonably acceptable to Landlord. If Tenant shall fail to comply with any of the requirements contained herein relating to insurance, Landlord may obtain such insurance and Tenant shall pay to Landlord, on demand, as additional rent hereunder, one hundred fifteen percent (115%) of the premium cost thereof.

**7.7 BOILER INSURANCE.** At all times when a "boiler," as that term is defined for the purposes of boiler insurance, is located within the Leased Premises, Tenant shall carry, at its expense, boiler insurance with policy limits of not less than One Hundred Thousand and No/100 Dollars (\$100,000.00) insuring both Landlord and Tenant against loss or liability caused by the operation or malfunction of such boiler. If no so-called boiler is located within the Leased Premises, then this Section 7.7 shall not apply to Tenant.

**7.8 ENVIRONMENTAL MATTERS.** Throughout the Lease Term, Tenant shall comply with all applicable Legal Requirements regarding health, safety and/or the environment and shall prevent the presence, use, generation, release, discharge, storage, disposal, or transportation of any Hazardous Materials (defined below) on, under, in, above, to, or from the Property and/or the Leased Premises other than in strict compliance with all applicable Legal Requirements. For purposes of this provision, the term "Hazardous Materials" shall mean and refer to any wastes, materials, or substances of any kind or character that are or become regulated as hazardous or toxic waste or substances, or which require special handling or treatment, under any applicable Legal Requirements (including, without limitation, under the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as now or later amended, the Resource Conservation and Recovery Act, as now or later amended, and/or the Toxic Substance Control Act of 1976, as now or later amended). To the extent to which the same may result from Tenant's failure to comply with the terms and provisions of this Section 7.8, Tenant shall indemnify, defend, and hold Landlord harmless from and against (i) any loss, cost, expense, claim, or liability arising out of any investigation, monitoring, enforcement action, clean-up, containment, removal, storage, or remediation work (herein called "Remediation") required by any applicable Legal Requirements, or by any government agency, authority, or political subdivision having jurisdiction over the Leased Premises, or which may be incurred by Landlord or any other person or party in a reasonable belief that such Remediation is or will be required by any applicable Legal Requirements, or by any government agency, authority, or political subdivision having jurisdiction over the Leased Premises, and (ii) any claims of third parties for loss, injury, expense, or damage arising out of the presence, release, or discharge of any Hazardous Materials on, under, in, above, to, or from the Leased Premises. In the event any Remediation is so required under any applicable Legal Requirements, Tenant shall promptly perform or cause to be performed such Remediation in compliance with such Legal Requirements. In the event Tenant shall fail to commence the Remediation in a timely fashion, or shall fail to prosecute diligently the Remediation to completion, such failure shall constitute an event of default on the part of Tenant under this Lease, and Landlord, in addition to any other rights or remedies afforded it under this Lease, may, but shall not be obligated to, cause the Remediation to be performed, and Tenant shall promptly reimburse Landlord for the cost and expense thereof upon demand.

#### **ARTICLE 8. CONDEMNATION**

**8.1 CONDEMNATION.** If the Leased Premises shall be taken or condemned (or sold in lieu thereof) for any public purpose to such an extent as to render the Leased Premises untenable, either party shall have the right to terminate this Lease by giving notice of such election to terminate to the other party within ten (10) days from the date of such condemnation or taking (or sale in lieu thereof), which termination shall be effective on the date of the transfer of possession of the Leased Premises to the condemning authority. If only a portion thereof shall be so taken so as not to render the remainder untenable, this Lease shall not terminate, and Base Rent shall be diminished by an equitable amount (based upon the number of rentable square feet of the Leased Premises so taken) and Landlord shall, to the extent practicable, restore the Leased Premises so that the remaining portion of the Leased Premises shall be partitioned off from the portion so taken or condemned; however, Landlord shall be obligated to restore or



rebuild the damaged property only to the extent the holder of any mortgage or deed of trust or the landlord under any ground lease makes the proceeds of such taking available to Landlord for the purposes of rebuilding and restoration, or if no mortgage or ground lease then affects the Building or the Property, then only to the extent of the net proceeds of such taking. If all or substantially all of the Building or the Property (whether or not the Leased Premises are affected), or a portion of the Building or the Property (whether or not the Leased Premises are affected) as to cause the remainder of the Building or the Property not to be economically feasible to operate, as reasonably determined by Landlord, should be taken or condemned (or sold in lieu thereof) for any public purpose, then this Lease, at the option of Landlord upon the giving of notice to Tenant within ten (10) days from the date of such condemnation or taking (or sale in lieu thereof), shall cease and terminate effective on the date of the transfer of possession of the Leased Premises to the condemning authority. If this Lease is terminated in accordance with this Section 8.1, Base Rent shall be apportioned on a per diem basis and shall be payable through the effective date of the termination.

**8.2 TEMPORARY TAKING.** In the event of any taking or condemnation for any public purpose of the Leased Premises or any portion thereof occurs for one hundred eighty (180) days or less, then it shall be deemed a temporary taking, this Lease shall continue in full force and effect, Landlord shall be under no obligation to make any repairs or alterations, and at Landlord's option either (i) there shall be no abatement of Base Rent and all proceeds of such taking relating to the Lease Term occurring during such taking shall belong to Tenant, or (ii) Base Rent shall be diminished by an equitable amount (based upon the number of rentable square feet so taken) for the period of time the Leased Premises are so taken and Landlord shall be entitled to the proceeds of such taking.

**8.3 CONDEMNATION PROCEEDS.** All proceeds from any taking or condemnation (or sale in lieu thereof) of the Leased Premises or any portion of the Property shall belong to and be paid to Landlord, and Tenant shall not be entitled to any portion of such award (except that Tenant shall have all rights permitted under the laws of the state in which the Property is located to appear, claim and prove in proceedings relative to such taking (i) the value of any fixtures, furnishings, and other personal property which are taken but which under the terms and provisions of this Lease Tenant is permitted to remove at the end of the Lease Term, (ii) the unamortized cost [such costs having been amortized on a straight line basis over the Lease Term excluding any renewal terms] of Tenant's leasehold improvements which are taken that Tenant is not permitted to remove at the end of the Lease Term and which were installed solely at Tenant's expense [i.e. not paid for by Landlord or purchased with allowances provided by Landlord], and (iii) relocation and moving expenses, but not the value of Tenant's leasehold estate created by this Lease and only so long as such claims in no way diminish the award Landlord receives from the condemning authority).

## ARTICLE 9. ASSIGNMENT OR SUBLEASE

### 9.1 TENANT ASSIGNMENT.

(a) Tenant shall not assign, in whole or in part, this Lease, or allow it to be assigned, in whole or in part, by operation of law or otherwise (including without limitation by merger, dissolution or transfer of a controlling interest in any partnership or corporate Tenant, which merger, dissolution or transfer shall be deemed an assignment) or mortgage or pledge the same, or sublet the Leased Premises, in whole or in part, without the prior written consent of Landlord, and in no event shall any such assignment or sublease ever release Tenant from any obligation or liability hereunder. No assignee or sublessee of the Leased Premises or any portion thereof may assign or sublet the Leased Premises or any portion thereof. Notwithstanding anything in this Section 9.1 to the contrary, Tenant may assign its interest in this Lease to any entity controlled by and majority owned by PC Connection, Inc., a Delaware corporation, with a principal address of 730 Milford Road, Merrimack, New Hampshire 03054.

(b) For the purposes hereof, (A) the transfer of the ownership or voting rights in a controlling interest of the voting stock of Tenant (if Tenant is a corporation), (B) the transfer of any general partnership interest or the transfer of twenty-five percent (25%) of the limited partnership interest in Tenant (if Tenant is a partnership), (C) the transfer of any ownership or membership interest in Tenant (if Tenant is a limited liability company), (D) the merger or consolidation of Tenant with or into any other corporation or entity, or (E) a sale or transfer of fifty percent (50%) or more of Tenant's assets, at any time during the Lease Term shall be deemed to be an assignment of this Lease.

**9.2 CONDITIONS OF TENANT ASSIGNMENT.** Except as otherwise permitted within Section 9.1 of this Lease, if Tenant desires to assign or sublet all or any part of the Leased Premises, it shall so notify Landlord in writing at least thirty (30) days in advance of the date on which Tenant desires to make such assignment or sublease. Tenant shall provide Landlord with a copy of the proposed assignment or sublease and such information as Landlord might request concerning the proposed sublessee or assignee to allow Landlord to make informed judgments as to the financial condition, reputation, operations and general desirability of the proposed sublessee or assignee. Within fifteen (15) days after Landlord's receipt of Tenant's proposed assignment or sublease and all required information concerning the proposed sublessee or assignee, Landlord shall have the following options: (1) cancel this Lease as to the Leased Premises or portion thereof proposed to be assigned or sublet; (2) consent to the proposed assignment or sublease, and if the rent due and payable by an assignee or sublessee under any such permitted assignment or sublease (or a combination of the rent payable under such assignment or sublease plus any bonus or any other consideration or any payment incident thereto) exceeds the Rent payable under this Lease for such space, Tenant shall pay to Landlord all such excess rent and other excess consideration within ten (10) days following receipt thereof by Tenant; or (3) refuse, in its sole and absolute discretion and judgment, to consent to the proposed assignment or sublease, which refusal shall be deemed to have been exercised unless Landlord gives Tenant written notice stating otherwise. Landlord's consent to any assignment,

subletting, or reorganization is not a waiver of Landlord's right to approve or disapprove any subsequent assignment, subletting, or reorganization. Tenant shall remain liable for the payment of Rent and performance of all other obligations under this Lease after any assignment or subletting. Receipt by Landlord of rent from any assignee, sublessee, or occupant of the Leased Premises is not a waiver of the covenant against assignment and subletting or a release of Tenant. In no event shall the following be considered as suitable assignees or sublessees under this Lease: any governmental body, agency or bureau (of the United States, any state, county, municipality or any subdivision thereof); any foreign government or subdivision thereof; any health care professional or health care service organization; schools or similar organizations; employment agencies; radio, television or other communication stations; restaurants; and retailers offering retail services from the Leased Premises. Notwithstanding the giving by Landlord of its consent to any sublease or assignment with respect to the Leased Premises, no sublessee or assignee may exercise any renewal options, expansion options, preferential rights to lease (i.e. rights of first offer or rights of first refusal) or similar rights under this Lease. Tenant may not exercise any renewal options, expansion options, preferential rights to lease (i.e. rights of first offer or rights of first refusal) or similar rights under this Lease if Tenant has assigned any portion of its interest in this Lease or subleased any portion of the Leased Premises. Upon the occurrence of an event of default of Tenant under this Lease, if all or any part of the Leased Premises are then assigned or sublet, Landlord, in addition to any other remedies provided by this Lease or provided by law, may at its option, collect directly from the assignee or sublessee all rents becoming due to Tenant by reason of the assignment or sublease, and Landlord, in addition to any other remedies provided by this Lease or provided by law, may, at its option, collect directly from the assignee or sublessee all rents becoming due to Tenant by reason of the assignment or sublease, and Landlord shall have a security interest in all properties belonging to Tenant on the Leased Premises to secure payment of such sums. No collection directly by Landlord from the assignee or sublessee shall be construed to constitute a novation or a release of Tenant from the further performance of its obligations under this Lease. If Landlord agrees to an assignment of the Lease or sublease of the Leased Premises, Tenant shall pay Landlord (i) One Thousand Five Hundred and No/100 Dollars (\$1,500.00) to reimburse Landlord for the administrative costs associated with such assignment or sublease and (ii) an amount equal to all legal fees and expenses incurred by Landlord in connection with the review by Landlord of Tenant's requested assignment or sublease pursuant to this Section, together with any legal fees and disbursements incurred by Landlord in the preparation and/or review of any documentation. Tenant shall be required to pay such amounts within five (5) days of demand for payment thereof, as additional rent under this Lease.

**9.3 LANDLORD ASSIGNMENT.** Landlord shall have the right to sell, transfer or assign, in whole or in part, its rights and obligations under this Lease and in the Property. Any such sale, transfer or assignment shall operate to release Landlord from any and all liabilities under this Lease arising after the date of such sale, assignment or transfer.

**9.4 RIGHTS OF MORTGAGEE.** Tenant accepts this Lease subject and subordinate to any recorded Lease, mortgage or deed of trust lien presently existing, if any, or hereafter encumbering the Property and to all existing ordinances and recorded restrictions, covenants, easements, and agreements with respect to the Property. Landlord hereby is

irrevocably vested with full power and authority to subordinate Tenant's interest under this Lease to any mortgage or deed of trust lien hereafter placed on the Property. Upon any foreclosure, judicially or non-judicially, of any such mortgage or lien, or the sale of the Property in lieu of foreclosure, or any other transfer of Landlord's interest in the Property, whether or not in connection with a mortgage or lien (any of foregoing forms of transfer, a "Transfer"), Tenant hereby does, and hereafter agrees to attorn to the purchaser at such foreclosure or to any other transferee of Landlord's interest, and shall recognize such purchaser, grantee, or other transferee as Landlord under this Lease, and no further attornment or other agreement shall be required to effect or evidence Tenant's attornment to and recognition of such purchaser or grantee as Landlord hereunder. Such agreement of Tenant to attorn shall survive any such foreclosure sale, trustee's sale, conveyance in lieu thereof, or any other transfer of Landlord's interest in the Property. Tenant, upon demand, at any time before or after any such foreclosure sale, trustee's sale, conveyance in lieu thereof, or other transfer shall execute, acknowledge and deliver to the prospective transferee and/or mortgagee a subordination and attornment agreement in a form acceptable to such mortgagee, and any additional written instruments and certificates evidencing such attornment as the mortgagee or other prospective transferee may reasonably require, and Tenant hereby irrevocably appoints Landlord as Tenant's agent and attorney-in-fact for the purpose of executing, acknowledging, and delivering any such instruments and certificates. Notwithstanding anything to the contrary set forth or implied in this Section: (a) any mortgagee under any mortgage shall have the right at any time to subordinate any such mortgage to this Lease on such terms and subject to such conditions as the mortgagee in its discretion may consider appropriate (specifically, without limitation, any such mortgagee may require that the casualty and condemnation provisions of this Lease remain subordinate to any applicable mortgage even in the event that such mortgagee chooses to subordinate the remainder of such mortgage to this Lease); and (b) no transferee of Landlord's interest in this Lease by way of any Transfer shall be responsible for or liable with respect to any representation, warranty, act, omission or default by Landlord under this Lease, or for the return of any Security Deposit (except to the extent to which such Security Deposit has been actually received by such transferee).

**9.5 ESTOPPEL CERTIFICATE.** Tenant agrees to furnish, from time to time, within ten (10) business days after receipt of a request from Landlord or Landlord's mortgagee, a statement certifying, if applicable, the following: Tenant is in possession of the Leased Premises; the Lease is in full force and effect; the Lease is unmodified (except as disclosed in such statement); Tenant claims no present charge, lien, or claim of offset against Rent; all Rent is paid for the current month, but is not prepaid for more than one (1) month and will not be prepaid for more than one (1) month in advance; there is no existing default by reason of any act or omission by Landlord; that Landlord has performed all inducements required of Landlord in connection with this Lease, including construction obligations, and Tenant accepts the Leased Premises as constructed; an acknowledgment of the assignment of rentals and other sums due hereunder to the mortgagee and agreement to be bound thereby; an agreement requiring Tenant to advise the mortgagee of damage to or destruction of the Leased Premises by fire or other casualty requiring reconstruction; an agreement by Tenant to give the mortgagee written notice of Landlord's default hereunder and to permit the mortgagee to cure such default within a reasonable time after such notice before exercising any remedy Tenant might possess as a result of such default; and

such other matters as may be reasonably required by Landlord or Landlord's mortgagee. Tenant's failure to deliver such statement, in addition to being a default under this Lease, shall be deemed to establish conclusively that this Lease is in full force and effect except as declared by Landlord, that Landlord is not in default of any of its obligations under this Lease, and that Landlord has not received more than one (1) month's Rent in advance.

## ARTICLE 10. LIENS

### 10.1 RESERVED.

## ARTICLE 11. DEFAULT AND REMEDIES

**11.1 DEFAULT BY TENANT.** The following shall be deemed to be events of default by Tenant under this Lease: (1) Tenant shall fail to pay when due any installment of Rent or any other payment required pursuant to this Lease; (2) Tenant shall abandon any substantial portion of the Leased Premises; (3) Tenant shall file a petition or be adjudged bankrupt or insolvent under any applicable federal or state bankruptcy or insolvency law or admit that it cannot meet its financial obligations as they become due, or a receiver or trustee shall be appointed for all or substantially all of the assets of Tenant; (4) Tenant shall make a transfer in fraud of creditors or shall make an assignment for the benefit of creditors; (5) Tenant shall do or permit to be done any act which results in a lien being filed against the Leased Premises or the Property; (6) the liquidation, termination, dissolution or (if the Tenant is a natural person) the death of Tenant; or (7) Tenant shall be in default of any other term, provision or covenant of this Lease, other than those specified in subparts (1) through (6) above, and such default is not cured within ten (10) days after written notice thereof to Tenant.

**11.2 REMEDIES FOR TENANT'S DEFAULT.** Upon the occurrence of any event of default set forth in this Lease, which default is not cured within thirty (30) calendar days of Tenant's receipt of Landlord's written notice of default, provided, however, that if such default is, by nature, not susceptible to cure during said thirty (30) calendar day period, then the cure period shall be extended as needed (but not for a period in excess of sixty (60) calendar days from the date of the above-referenced notice of default) to accommodate the efforts of Tenant to effectuate a cure. Thereafter, Landlord shall have the option to pursue any one or more of the remedies set forth in this Section 11.2 (immediately or at any time after such event of default) without additional notice or demand:

(a) Without declaring the Lease terminated, Landlord may enter upon and take possession of the Leased Premises, by picking or changing locks if necessary, and lock out, expel or remove Tenant and any other person who may be occupying all or any part of the Leased Premises without being liable for any claim or damages arising therefrom, and correct or repair any condition which shall constitute a failure on Tenant's part to keep, observe, perform, satisfy or abide by any term, condition, covenant, agreement or obligation of this Lease and Tenant shall fully reimburse and compensate Landlord on demand for the costs incurred by Landlord in doing so.

(b) Without declaring the Lease terminated, Landlord may terminate Tenant's right of possession (but not this Lease) and may repossess the Leased Premises by forcible entry or detainer suit or otherwise, or by picking or changing locks if necessary, without demand or notice of any kind and without being liable for any claim or damages arising therefrom, and remove all persons or property therefrom, using such force as may be necessary (Tenant hereby waiving any claim by reason of such reentry, repossession or removal or by issuance of any distress warrant or writ of sequestration), in which event Landlord may (but shall be under no obligation to do so unless required by law), relet the Leased Premises or any part thereof for the account of Tenant for such rent and upon such terms as shall be satisfactory to Landlord (however, to the extent Landlord is so required by law to relet the Leased Premises, Landlord shall be under no obligation to relet the Leased Premises or any portion thereof in preference to any other space in the Property or on terms unsatisfactory to Landlord). For the purpose of such reletting Landlord is authorized to decorate or to make any repairs, changes, alterations or additions in or to the Leased Premises, or provide leasing inducements or brokerage commissions that may be necessary or convenient, and (i) if Landlord shall fail or refuse to relet the Leased Premises, or (ii) if relet and a sufficient sum shall not be realized from such reletting (after paying the unpaid amounts due hereunder earned but unpaid at the time of reletting plus interest thereon at the Interest Rate, the cost of recovering possession [including, without limitation, attorney's fees and cost of court], all of the costs and expenses of such decorations, repairs, changes, alterations and additions and all other expenses of such reletting [including, without limitation, leasing inducements and brokerage commission] and of the collection of the rent accruing therefrom) to satisfy the Rent provided for in this Lease to be paid, then Tenant shall pay to Landlord as damages a sum equal to the amount of the Rent reserved in this Lease for such period or periods or, if the Leased Premises have been relet, Tenant shall satisfy and pay any such deficiency upon demand therefor from time to time as the same accrues or becomes due. Tenant agrees that Landlord may file suit to recover any sums falling due under the terms of this Section from time to time on one or more occasions without Landlord being obligated to wait until expiration of the Lease Term, and no delivery or recovery of any portion due Landlord hereunder shall be any defense in any action to recover any amount not theretofore reduced to judgment in favor of Landlord, nor shall such reletting be construed as an election on the part of Landlord to terminate this Lease unless a written notice of such intention be given to Tenant by Landlord. Notwithstanding any such reletting without termination, Landlord may at any time thereafter elect to terminate this Lease for such previous breach. If Landlord re-enters the Leased Premises or terminates this Lease pursuant to any of the provisions of this Lease, Tenant hereby waives all claims for damages which may be caused by such re-entry or termination by Landlord. No such re-entry or termination shall be considered or construed to be a forcible entry.

(c) Landlord may terminate this Lease, in which event Tenant shall immediately surrender the Leased Premises to Landlord, and if Tenant fails to surrender the Leased Premises, Landlord may, without prejudice to any other remedy which it may have for possession or arrearage in Rent, enter upon and take possession of the Leased Premises, by picking or changing locks if necessary, and lock out, expel or remove

Tenant and any other person who may be occupying all or any part of the Leased Premises without being liable for any claim for damages. Tenant agrees to pay on demand the amount of all loss and damage which Landlord may suffer for any reason due to the termination of this Lease under this Section, including (without limitation) (i) loss and damage due to the failure of Tenant to maintain and/or repair the Leased Premises as required hereunder, (ii) the cost of recovering the Leased Premises (including, without limitation, attorney's fees and costs of court), (iii) the cost as reasonably estimated by Landlord of any alterations of, or repairs to, the Leased Premises which are necessary or proper to prepare the same for reletting, (iv) the unpaid Rent owed at the time of termination, plus interest thereon from due date at the Interest Rate, (v) the present value of the balance of the Rent for the remainder of the Lease Term less the present value of the fair market rental value (and in computing the fair market value the factors taken into account shall include without limitation the market rental concessions and the time necessary to relet the Leased Premises) of the Leased Premises for said period (in each case using a discount rate of eight percent (8%) per annum), and (vi) any other sum of money and damages owed by Tenant to Landlord.

(d) Interrupt or cause the interruption of any utility service serving the Leased Premises, deactivate Tenant's parking access cards, suspend elevator service to the Leased Premises, remove, alter, or change any door, window, attic hatchway cover to the Leased Premises, or any lock, latch, hinge, hinge pin, doorknob, or other mechanism connected to any door, window, or attic hatchway cover to the Leased Premises, and intentionally prevent Tenant from entering the Leased Premises without resort to judicial process. Landlord is under no obligation to restore any door, window, or attic hatchway cover of any lock, latch, hinge, hinge pin, doorknob, or other mechanism attached thereto.

No repossession of or reentering all or any part of the Leased Premises, and no reletting of the Leased Premises or any part thereof, shall relieve Tenant, all of which shall survive any such repossession, re-entering or reletting by Landlord (except as otherwise expressly set forth in this Lease). If Landlord repossesses or re-enters all or any part of the Leased Premises after an event of default, Tenant shall pay to Landlord all Rent then required to be paid by Tenant. In addition to other remedies provided under this Lease, Landlord is entitled, to the extent permitted by applicable law, to injunctive relief in case of the violation, or attempted or threatened violation, of any of the terms of this Lease, or to a decree compelling specific performance of the terms of this Lease.

Notwithstanding anything in this Lease to the contrary, if Landlord is deemed to have a duty to mitigate its damages arising from a default by Tenant under this Lease, then Landlord's duty to mitigate shall be limited to using reasonable and good faith efforts to relet the Leased Premises, which duty to relet the Leased Premises shall not (i) require Landlord to give priority to the Leased Premises over other premises owned or managed by Landlord or its affiliates, (ii) require Landlord to relet for less than market rent, or (iii) require Landlord to relet to a tenant (or for a use) which is not in keeping with the first-class character of the Property.

Landlord's exercise, following an event of default on behalf of Tenant under this Lease, of any right granted hereunder or under any applicable law to lock or change the locks securing the Leased Premises shall not impose upon Landlord any duty to notify Tenant of the name and address or telephone number of the individual or company from whom a new key may be obtained, nor shall Landlord have any duty to provide Tenant with a new key or any other means of access to the Leased Premises. Landlord and Tenant agree that the parties hereto intend that all rights and remedies of Landlord under this Lease or otherwise available to Landlord under applicable law shall supersede any conflicting provisions of Chapters 91, 92 and 93 of the Texas Property Code, and any amendments, modifications, recodification or other changes thereto.

Notwithstanding any other remedy set forth in this Lease, if Landlord has made Rent concessions of any type or character, or waived any Base Rent, and Tenant fails to take possession of the Leased Premises on the Commencement Date or otherwise defaults at any time during the Lease Term, the rent concessions, including any waived Base Rent, shall be canceled and the amount of the Base Rent or other rent concessions shall be due and payable immediately as if no rent concessions or waiver of any Base Rent had ever been granted. A rent concession or waiver of the Base Rent shall not relieve Tenant of any obligation to pay any other charge due and payable under this Lease, including, without limitation, any sum due under Section 2.3 of this Lease. Notwithstanding anything contained in this Lease to the contrary, this Lease may be terminated by Landlord only by written notice of such termination to Tenant given in accordance with Section 13.7 below, and no other act or omission of Landlord shall be construed as a termination of this Lease.

**11.3 REMEDIES CUMULATIVE.** All rights and remedies of Landlord herein or existing at law or in equity are cumulative, and the exercise of one or more rights or remedies shall not be taken to exclude or waive the right to the exercise of any other.

**11.4 DEFAULT BY LANDLORD.** If Landlord defaults in the performance of any term, covenant or condition required to be performed by Landlord under this Lease, Landlord shall have thirty (30) days following the receipt of written notice from Tenant specifying such default to cure such default, provided that if Landlord has commenced actions to cure such default within said thirty (30) day period, then the cure period shall be extended as needed (but not for a period in excess of sixty (60) days from the date of the above-referenced notice of default) to accommodate the efforts of Landlord to effectuate a cure.

**11.5 REMEDIES FOR LANDLORD'S DEFAULT.** Upon the occurrence of any default on behalf of Landlord under this Lease and subsequent failure by Landlord to cure or commence actions to cure as provided in Section 11.4, Tenant shall, as Tenant's sole remedy, have the right to maintain an action against Landlord, for actual damages suffered as a result of Landlord's default.

**11.6 NOTICE TO MORTGAGEES.** Provided that Tenant has received prior written notice of the name and address of such lender, Tenant shall serve written notice of any claimed default or breach by Landlord under this Lease upon any lender which is a beneficiary under any deed of trust or mortgage against the Leased Premises, and no notice to Landlord shall be



effective against Landlord unless such notice is served upon said lender. Notwithstanding anything to the contrary contained herein, Tenant shall allow such lender the same period following lender's receipt of such notice to cure such default or breach as is afforded Landlord, plus such longer period of time as may be reasonably necessary under the circumstances (but in no event less than thirty (30) days) for such lender to cure such default or breach.

**11.7 WAIVER BY TENANT.** Tenant waives and surrenders for itself and all persons or entities claiming by, through, and under it, including creditors of all kinds: (i) any right and privilege which it or any of them has under any present or future constitution, statute, or rule of law to redeem the Leased Premises or to have a continuance of this Lease for the Lease Term after termination of Tenant's right of occupancy by order or judgment of any court, or by any legal process or writ, or under the terms of this Lease; (ii) the benefits of any present or future constitution, statute, or rule of law that exempts property from liability for debt or for distress for rent; (iii) any provision of law relating to notice or delay in levy of execution in case of eviction of a tenant for nonpayment of rent; (iv) any rights, privileges, and liens set out under Sections 91.004 and 93.003 of the Texas Property Code (as amended), and Tenant exempts Landlord from any liability or duty thereunder; and (v) any rights of Tenant to contest reappraisals of the Property (but not ad valorem taxes on Tenant's personal property in the Leased Premises) under Sections 41.143 and 42.015 of the Texas Tax Code (as amended).

## ARTICLE 12. RELOCATION

### 12.1 RESERVED.

## ARTICLE 13. MISCELLANEOUS

**13.1 WAIVER.** Failure of Landlord to declare an event of default immediately upon its occurrence, or delay in taking any action in connection with an event of default, shall not constitute a waiver of the default, but Landlord shall have the right to declare the default at any time and take such action as is lawful or authorized under this Lease. Pursuit of any one or more of the remedies set forth in Article 11 above shall not preclude pursuit of any one or more of the other remedies provided elsewhere in this Lease or provided by law, nor shall pursuit of any remedy hereunder or at law constitute forfeiture or waiver of any Rent or damages accruing to Landlord by reason of the violation of any of the terms, provisions or covenants of this Lease. Failure by Landlord to enforce one or more of the remedies provided hereunder or at law upon any event of default shall not be deemed or construed to constitute a waiver of the default or of any other violation or breach of any of the terms, provisions and covenants contained in this Lease. Landlord may collect and receive Rent due from Tenant without waiving or affecting any rights or remedies that Landlord may have at law or in equity or by virtue of this Lease at the time of such payment. Institution of a forcible detainer action to re-enter the Leased Premises shall not be construed to be an election by Landlord to terminate this Lease.

**13.2 ACT OF GOD.** Landlord shall not be required to perform any covenant or obligation in this Lease, or be liable in damages to Tenant, so long as the performance or non-performance of the covenant or obligation is delayed, caused or prevented by an Act of God, Force Majeure or by Tenant. For the purposes of this Lease, an "Act of God" or "Force Majeure"

shall mean strikes, lockouts, sitdowns, material or labor restrictions by any governmental authority, unusual transportation delays, riots, floods, washouts, explosions, earthquakes, fire, storms, weather (including wet grounds or inclement weather which prevents construction), acts of the public enemy, wars, insurrections, and/or any other cause not reasonably within the control of Landlord or which by the exercise of due diligence Landlord is unable wholly or in part to prevent or overcome.

**13.3 ATTORNEY'S FEES.** If any party defaults in the performance of any terms, covenants, agreements or conditions contained in this Lease and the other party places in the hands of any attorney the enforcement of all or any part of this Lease, then the party which does not prevail agrees to pay the reasonable fees and costs of the prevailing party's attorneys, whether suit is actually filed or not.

**13.4 SUCCESSORS.** This Lease shall be binding upon and inure to the benefit of Landlord and Tenant and their respective heirs, successors and assigns.

**13.5 RENT TAX.** If applicable in the jurisdiction where the Leased Premises are situated, Tenant shall pay and be liable for all rental, sales and use taxes or other similar taxes, if any, levied or imposed by any city, state, county or other governmental body having authority, such payments to be in addition to all other payments required to be paid to Landlord by Tenant under the terms of this Lease; provided, however, nothing in this Section 13.5 shall require Tenant to pay any of Landlord's income taxes. Any such payment shall be paid concurrently with the payment of the Rent, operating expenses or other charge(s) upon which the tax is based as set forth above.

**13.6 INTERPRETATION.** The captions appearing in this Lease are for convenience only and in no way define, limit, construe or describe the scope or intent of any Section. Grammatical changes required to make the provisions of this Lease apply (i) in the plural sense where there is more than one tenant and (ii) to either corporations, associations, partnerships or individuals, males or females, shall in all instances be assumed as though in each case fully expressed. The laws of the State of Texas shall govern the validity, performance and enforcement of this Lease. This Lease shall not be construed more or less favorably with respect to either party as a consequence of the Lease or various provisions hereof having been drafted by one of the parties hereto.

**13.7 NOTICES.** All payments required to be made by Landlord to Tenant shall be payable to Tenant at Tenant's address set forth in Section 1.9 of this Lease. Any notice or document (other than Rent) required or permitted to be delivered by the terms of this Lease shall be deemed to be delivered upon the earlier to occur of (i) actual receipt or (ii) whether or not actually received, three (3) days after deposit in the United States Mail, postage prepaid, certified mail, return receipt requested or (iii) one (1) day after deposit with a nationally recognized overnight delivery service (e.g. FedEx), addressed to the applicable party at the applicable address set forth in Section 1.9 of this Lease (or, in the case of Tenant, at the Leased Premises), or to such other addresses as the parties may have designated by written notice to each other, with copies of notices to Landlord being sent to Landlord's address as shown in Section 1.9 of

this Lease. Manager shall be a co-addressee with Landlord on all notices sent to Landlord by Tenant hereunder, and any notice sent to Landlord and not to Manager also, in accordance with this Section, shall be deemed ineffective at the option of Landlord.

**13.8 SUBMISSION OF LEASE.** Submission of this Lease to Tenant for signature does not constitute a reservation of space or an option to lease. This Lease is not effective until execution by and delivery to both Landlord and Tenant.

**13.9 CORPORATE AUTHORITY.** If Tenant executes this Lease as a corporation or a partnership (general or limited), each person executing this Lease on behalf of Tenant hereby personally represents and warrants that: Tenant is a duly authorized and existing corporation or partnership (general or limited); Tenant is qualified to do business in the state in which the Leased Premises are located; the corporation or partnership (general or limited) has full right and authority to enter into this Lease; each person signing on behalf of the corporation or partnership (general or limited) is authorized to do so; and the execution and delivery of the Lease by Tenant will not result in any breach of, or constitute a default under, any mortgage, deed of trust, lease, loan, credit agreement, partnership agreement, or other contract or instrument to which Tenant is a party or by which Tenant may be bound. If any representation or warranty contained in this Section is false, each person who executes this Lease shall be liable individually as Tenant hereunder.

**13.10 MULTIPLE TENANTS.** If this Lease is executed by more than one person or entity as "Tenant," each such person or entity shall be jointly and severally liable hereunder. It is expressly understood that any one of the named Tenants shall be empowered to execute any modification, amendment, exhibit, floor plan, or other document herein referred to and bind all of the named Tenants thereto; and Landlord shall be entitled to rely on same to the same extent as if all of the named Tenants had executed same.

**13.11 TENANT'S FINANCIAL STATEMENTS.**

(a) Tenant represents and warrants to Landlord that, as of the date of execution of this Lease by Tenant, the financial statements of Tenant provided to Landlord prior to or simultaneously with the execution of this Lease accurately represent the financial condition of Tenant as of the dates and for the periods indicated therein, such financial statements are true and do not contain any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements included therein not misleading, and there has been no material adverse change in the financial condition or business prospects of Tenant since the respective dates of such financial statements. If there is a material adverse change in Tenant's financial condition, Tenant will give immediate notice of such material adverse change to Landlord. If Tenant fails to give such immediate notice to Landlord, such failure shall be deemed an event of default under this Lease.

(b) If Landlord intends to sell all or any portion of the Building or the Property (or any interest therein), or obtain a loan secured by the Building or the Property (or any interest therein), then Tenant shall, within fifteen (15) days of Landlord's written request

(but not more frequently than three (3) times in any calendar year), furnish Landlord with financial statements, dated no earlier than one (1) year before such request, certified as accurate by Tenant, or, if available, audited financial statements prepared by an independent certified public accountant with copies of the auditor's statement, reflecting Tenant's then current financial condition, or the financial condition of the individuals compromising Tenant, in such form and detail as Landlord may reasonably request.

**13.12 SEVERABILITY.** If any provision of this Lease or the application thereof to any person or circumstances shall be invalid or unenforceable to any extent, the remainder of this Lease and the application of such provisions to other persons or circumstances shall not be affected thereby and shall be enforced to the greatest extent permitted by law. Each covenant and agreement contained in this Lease shall be construed to be a separate and independent covenant and agreement, and any default or breach of the terms of this Lease by Landlord shall not discharge or relieve Tenant from Tenant's obligation to perform each and every covenant and agreement of this Lease to be performed by Tenant.

**13.13 LANDLORD'S LIABILITY.** If Landlord shall be in default under this Lease and, if as a consequence of such default, Tenant shall recover a money judgment against Landlord, such judgment shall be satisfied only out of the right, title and interest of Landlord in the Property as the same may then be encumbered and neither Landlord nor any person or entity comprising Landlord shall be liable for any deficiency. In no event shall Tenant have the right to levy execution against any property of Landlord nor any person or entity comprising Landlord other than its interest in the Property as herein expressly provided.

**13.14 SALE OF PROPERTY.** Upon any conveyance, sale or exchange of the Leased Premises or assignment of this Lease, Landlord shall be and is hereby entirely free and relieved of all liability under any and all of its covenants and obligations contained in or derived from this Lease arising out of any act, occurrence, or omission relating to the Leased Premises or this Lease occurring after the consummation of such sale or exchange and assignment.

**13.15 TIME IS OF THE ESSENCE.** The time of the performance of all of the covenants, conditions and agreements of this Lease is of the essence.

**13.16 SUBTENANCIES.** At Landlord's option the voluntary or other surrender of this Lease by Tenant, or a mutual cancellation thereof, shall not work a merger of estates and shall operate as an assignment of any or all permitted subleases or subtenancies.

**13.17 BROKERAGE; MUTUAL INDEMNITIES.**

(a) Tenant warrants that it has had no dealings with any broker or agent in connection with the negotiation or execution of this Lease other than R.M. Crowe Leasing, LLC ("Broker"). Tenant shall indemnify, defend, and hold Landlord harmless against all costs, expenses, attorneys' fees, or other liability for commission or other compensation or charges claimed by any broker or agent other than Broker claiming by, through, or under Tenant with respect to this Lease or any renewal or extension of the same or with respect to any expansion of the Leased Premises.

(b) Landlord warrants that it has had no dealings with any broker or agent in connection with the negotiations or execution of this Lease other than Broker. Landlord shall indemnify, defend, and hold Tenant harmless against all costs, expenses, attorneys' fees, or other liability for commissions or other compensation or charges claimed by any broker or agent, including Broker, claiming by, through or under Landlord with respect to this Lease or any renewal or extension of the same or with respect to any expansion of the Leased Premises.

(c) Any brokerage commission payable to Broker is payable by Landlord pursuant to the terms of separate agreements between Landlord and Broker.

**13.18 WAIVER OF TRIAL RIGHTS.** Landlord and Tenant hereby waive trial by jury (i) in any action, proceeding or counterclaim brought by Landlord or Tenant against the other, (ii) in any matter whatsoever arising out of or in any way connected with this Lease, the relationship of Landlord to Tenant, the use or occupancy of the Leased Premises by Tenant or any person claiming through or under Tenant, and (iii) with respect to any claim of injury or damage and/or any emergency or other statutory remedy; provided, however, the foregoing waiver shall not apply to any action for personal injury or property damage. If Landlord commences any summary or other proceeding for nonpayment of Rent or the recovery of possession of the Leased Premises, Tenant shall not interpose any counterclaim of whatever nature or description in any such proceeding, unless the failure to raise the same would constitute a waiver thereof.

#### **ARTICLE 14. AMENDMENT AND LIMITATION OF WARRANTIES**

**14.1 ENTIRE AGREEMENT.** IT IS EXPRESSLY AGREED BY TENANT, AS A MATERIAL CONSIDERATION FOR THE EXECUTION OF THIS LEASE, THAT THIS LEASE, WITH THE SPECIFIC REFERENCES TO EXTRINSIC DOCUMENTS, IS THE ENTIRE AGREEMENT OF LANDLORD AND TENANT; THAT THERE ARE, AND WERE, NO VERBAL REPRESENTATIONS, WARRANTIES, UNDERSTANDINGS, STIPULATIONS, AGREEMENTS OR PROMISES PERTAINING TO THE SUBJECT MATTER OF THIS LEASE OR OF ANY EXPRESSLY MENTIONED EXTRINSIC DOCUMENTS THAT ARE NOT INCORPORATED IN WRITING IN THIS LEASE.

**14.2 AMENDMENT.** THIS LEASE MAY NOT BE ALTERED, WAIVED, AMENDED, OR EXTENDED EXCEPT BY AN INSTRUMENT OF A DATE SUBSEQUENT HERETO IN WRITING SIGNED BY LANDLORD AND TENANT.

**14.3 LIMITATION OF WARRANTIES.** LANDLORD AND TENANT EXPRESSLY AGREE THAT THERE ARE AND SHALL BE NO IMPLIED WARRANTIES OF MERCHANTABILITY, HABITABILITY, SUITABILITY, FITNESS FOR A PARTICULAR PURPOSE OR OF ANY OTHER KIND ARISING OUT OF THIS LEASE, AND THERE ARE NO WARRANTIES WHICH EXTEND BEYOND THOSE EXPRESSLY SET FORTH IN THIS LEASE. WITHOUT LIMITING THE GENERALITY OF THE FOREGOING, TENANT EXPRESSLY ACKNOWLEDGES THAT LANDLORD HAS MADE NO WARRANTIES OR REPRESENTATIONS CONCERNING ANY HAZARDOUS

MATERIALS OR OTHER ENVIRONMENTAL MATTERS AFFECTING ANY PART OF THE PROPERTY, AND LANDLORD HEREBY EXPRESSLY DISCLAIMS AND TENANT WAIVES ANY EXPRESS OR IMPLIED WARRANTIES WITH RESPECT TO ANY SUCH MATTERS.

**14.4 WAIVER AND RELEASES.** TENANT SHALL NOT HAVE THE RIGHT TO WITHHOLD OR TO OFFSET RENT OR TERMINATE THIS LEASE EXCEPT AS EXPRESSLY PROVIDED HEREIN. TENANT WAIVES AND RELEASES ANY AND ALL STATUTORY LIENS AND OFFSET RIGHTS.

**14.5 NON-DISCLOSURE OF LEASE TERMS.** EXCEPT IF OTHERWISE REQUIRED BY LAW, TENANT SHALL NOT DISCLOSE ANY MATERIAL TERMS OR PROVISIONS OF THIS LEASE. IF TENANT DISCLOSES ANY OF THE MATERIAL TERMS AND/OR PROVISIONS OF THIS LEASE, EXCEPT AS MAY BE REQUIRED BY LAW, INCLUDING BUT NOT LIMITED TO THE BASE RENT, THE PERCENTAGE RENT, TENANT'S COMMON AREA COSTS AND/OR OPERATING EXPENSES OR ANY CAPS ON SUCH COSTS OR EXPENSES, MERCHANT ASSOCIATION FEES, TENANT FINISH ALLOWANCE, TENANT'S PROPORTIONATE SHARE OF GENERAL TAXES OR ANY CAP ON SUCH EXPENSE, TENANT'S PROPORTIONATE SHARE OF INSURANCE PREMIUMS OR ANY CAP ON SUCH EXPENSE, OR THE LEASE TERM TO ANY PERSON OR ENTITY NOT A PARTY TO THIS LEASE EXCEPT TENANT'S ATTORNEY, THEN TENANT SHALL BE LIABLE FOR ALL DAMAGES OR INJURY TO LANDLORD RESULTING FROM TENANT'S FAILURE TO KEEP SUCH INFORMATION CONFIDENTIAL AND TENANT SHALL INDEMNIFY AND HOLD LANDLORD HARMLESS FROM ANY DAMAGE, LOSS OR INJURY OCCASIONED THEREBY. IN THE ALTERNATIVE, AND AT LANDLORD'S SOLE OPTION, IF DAMAGES ARE DIFFICULT TO CALCULATE, TENANT SHALL PAY LIQUIDATED DAMAGES EQUAL TO ONE (1) MONTH'S BASE RENT AS DEFINED IN ARTICLE 1 HEREOF.

**14.6 SECURITY DISCLAIMER.** ANY SECURITY MEASURES PROVIDED BY LANDLORD MAY NOT BE TREATED BY TENANT AS A GUARANTEE AGAINST CRIME. LANDLORD DOES NOT MAKE, AND TENANT WAIVES, ANY GUARANTY OR WARRANTY, EXPRESSED OR IMPLIED, WITH RESPECT TO SECURITY AT THE PROPERTY OR IN THE BUILDING, OR THAT ANY SECURITY MEASURES WILL PREVENT OCCURRENCES OR CONSEQUENCES FOR CRIMINAL ACTIVITY. ANY MECHANICAL SECURITY DEVICES CAN BE RENDERED INOPERATIVE ANY TIME. LANDLORD IS NOT RESPONSIBLE FOR A TEMPORARY FAILURE OF SUCH DEVICES. IF SUCH DEVICES ARE IN NEED OF REPAIR, TENANT WAIVES ALL WARRANTIES, EXPRESS OR IMPLIED, WITH RESPECT TO LANDLORD'S REPAIR OF SUCH DEVICES. LANDLORD'S INSTALLATION OR USE OF ANY SECURITY MEASURE DOES NOT CONSTITUTE A VOLUNTARY UNDERTAKING OR AGREEMENT BY LANDLORD TO PROVIDE SECURITY TO TENANT OR ANY TENANT-RELATED PARTY OR ANY PROPERTY OF THE SAME. LANDLORD MAY MODIFY, REDUCE OR ELIMINATE THE USE OF ANY SECURITY MEASURE AT ANY TIME WITHOUT NOTICE TO TENANT. NEITHER LANDLORD NOR ITS AGENTS, EMPLOYEES OR REPRESENTATIVES ARE

LIABLE IN ANY WAY FOR ANY DISRUPTION IN THE OPERATION OR PERFORMANCE OF ANY SECURITY MEASURE. LANDLORD DOES NOT MAKE, AND TENANT WAIVES, ANY GUARANTY OR WARRANTY THAT THE PRESENCE OF ANY SECURITY MEASURE AT THE PROPERTY OR IN THE BUILDING IN ANY WAY INCREASES THE PERSONAL SECURITY OF TENANT OR ANY TENANT-RELATED PARTY OR ANY PROPERTY OF THE SAME. LANDLORD IS NOT LIABLE TO TENANT OR ANY TENANT-RELATED PARTY FOR ANY INJURY, DAMAGE OR LOSS WHATSOEVER WHICH IS CAUSED (I) AS A RESULT OF ANY PROBLEM, DEFECT, MALFUNCTION OR FAILURE OF THE PERFORMANCE OF ANY SECURITY MEASURE OR (II) BY ANY PERSON ENGAGED IN ANY CRIMINAL ACTIVITY.

*[The signature page follows immediately hereafter.]*

**LANDLORD:**

**RMC MIDWAY WALNUT, LP**

a Texas limited partnership

By: RMC Midway Walnut GP, LLC  
its general partner

By: /s/ Maurice Crowe Jr.  
R. Maurice Crowe, Jr.  
Manager

**TENANT:**

**MOREDIRECT, INC.**

a Florida corporation

By: /s/ Jack L. Ferguson  
Name: Jack L. Ferguson  
Title: CFO of PC Connection, Inc. (parent company of MoreDirect, Inc.)

**List of Exhibits:**

- Exhibit "A" – Site Plan
- Exhibit "A-1" – Additional Space
- Exhibit "B" – Parking
- Exhibit "C" – Intentionally Rules and Regulations Deleted
- Exhibit "D" – Rules and Regulations
- Exhibit "E" – Landlord Work Letter
- Rider "1" – Option to Extend (Two-Time)
- Rider "2" – Tenant's Preferential Right to Lease
- Rider "3" – Termination Option



---

**EXHIBIT "A"**

**TO OFFICE LEASE**

**SITE PLAN**

[See Attached]

---

**EXHIBIT "A-1"**  
**TO OFFICE LEASE**  
**ADDITIONAL SPACE**

[See Attached]

**EXHIBIT "B"**  
**TO OFFICE LEASE**  
**PARKING**

**TENANT:**

1. Throughout the Lease Term, subject to availability, Tenant shall be able to lease from Landlord parking spaces in the parking facilities related to the Property. All such parking spaces shall be leased by Tenant on an unassigned basis except as provided below, and shall be used in common with the other tenants. Landlord shall have the right to reserve parking spaces in the parking facilities as it elects, and to condition the use thereof on such terms as it elects.
2. Throughout the Lease Term, to the extent that the same may be required pursuant to the terms and provisions of paragraph 3 below, Tenant shall pay to Landlord as monthly rent (the "Parking Rent") for parking spaces an amount equal to the product of (i) the then current monthly rate for parking in the parking facilities (as established by Landlord from time to time) times (ii) the number of parking spaces used by Tenant. All Parking Rent shall be paid by Tenant to Landlord in advance without demand on the first day of each month, with partial months prorated as applicable, commencing with the Commencement Date.
3. Tenant shall have the right to use (i) thirteen (13) unreserved surface parking spaces at the rate of Zero and No/100 Dollars (\$0.00) per space per month (plus applicable sales tax) and (ii) zero (0) designated reserved parking spaces at the rate of Zero and No/100 Dollars (\$0.00) per space per month (plus applicable sales tax). Such amounts shall be deemed Parking Rent as set forth in paragraph 2 above, payable as provided therein.
4. Lost parking access cards or parking permits will be replaced on request with a charge of Fifteen and No/100 Dollars (\$15.00) per card/permit.
5. Tenant shall cooperate fully in Landlord's efforts to maintain the designated use of the various parking facilities and parking areas, and shall follow all traffic, security, safety, and other rules and regulations issued by the Landlord with respect thereto.
6. Landlord shall have the right to: make a reasonable charge for public parking, control access to the parking facilities, add below grade parking, parking decks, change curb cuts, change traffic patterns, re-stripe the parking facilities and parking surfaces as to size and location of spaces, temporarily displace vehicles (for the purpose of improving and expanding parking facilities and with appropriate rebate of Parking Rent), abandon any parking areas and add or delete acceleration/deceleration lanes on adjacent roads and alleys.

7. Prior to issuance of the parking access cards or parking permits, Tenant must deliver to Landlord a list of the automobile license numbers of Tenant's employees who will be using the cards or parking permits, together with Landlord's then current per card/permit deposit. This deposit is forfeited to Landlord if any card or parking permit, is lost or damaged or not returned to Landlord on request and a new deposit must be delivered to Landlord before a replacement card or parking permit is issued to Tenant.
8. Tenant is not assigned designated unreserved parking spaces, but is permitted to use whatever unreserved stalls are available, on a first-come, first-served basis in areas designated for tenant parking from time to time by Landlord. If for any reason Landlord fails or is unable to provide parking spaces to Tenant, this failure or inability is not a default by Landlord under this Lease.
9. During any renewal or extension of the Lease Term or during any holdover after the termination of this Lease, Landlord reserves the right to charge Tenant the Parking Rent (plus any applicable sales tax) then imposed by Landlord for parking in the parking facilities related to the Property.

---

**EXHIBIT "C"**  
**TO OFFICE LEASE**  
Intentionally Deleted

**EXHIBIT "D"**  
**TO OFFICE LEASE**  
**RULES AND REGULATIONS**

1. Landlord agrees to furnish Tenant with two (2) keys (of every sort that Tenant may require to access the Leased Premises and the Common Areas) without charge. Additional keys will be furnished at a nominal charge. Tenant shall not change locks or install additional locks on doors without prior written consent of Landlord. Tenant shall not make or cause to be made duplicates of keys procured from Landlord without prior written approval of Landlord. All keys to the Leased Premises shall be surrendered to Landlord upon termination of the Lease.
2. Tenant will refer all contractors, contractor's representatives and installation technicians rendering any service on or to the Leased Premises for Tenant to Landlord for Landlord's approval before performance of any such contractual service. Tenant's contractors, contractor's representatives and installation technicians shall comply with Landlord's rules and regulations pertaining to construction and installation, including without limitation, providing Landlord with a certificates of insurance that meet Landlord's requirements. This provision shall apply to all work performed on or about the Property and/or the Leased Premises, including installation of telephones, telegraph equipment, electrical devices and attachments and installations of any nature affecting floors, walls, woodwork, trim, windows, ceilings and equipment or any other physical portion of the Leased Premises or the Property.
3. Tenant shall not at any time occupy any part of the Leased Premises as sleeping or lodging quarters.
4. Tenant shall not place, install or operate on the Leased Premises or in any part of the Property any electrical floor heater, engine, stove or machinery, or conduct mechanical operations or cook thereon or therein, or place or use in or about the Leased Premises or the Property any explosives, gasoline, kerosene, oil, acids, caustics, or any flammable, explosive or hazardous material without written consent of Landlord.
5. Landlord will not be responsible for lost or stolen merchandise, trade fixtures, furniture, furnishings, personal property, equipment, money or jewelry from the Leased Premises or the Property regardless of whether such loss occurs when the area is locked against entry.
6. No dogs, cats, fowl or other animals shall be brought into or kept in or about the Leased Premises or the Property.
7. Employees of Landlord shall not receive or carry messages for or to any Tenant or other person, nor shall they contract with or render free or paid services to Tenant or to any of Tenant's agents, employees or invitees.

8. None of the parking, plaza or recreational lawn areas, entries, passages, doors, elevators, hallways or stairways shall be blocked or obstructed or any rubbish, litter, trash or material of any nature placed, emptied or thrown into these areas or such area used by Tenant's agents, employees or invitees at any time for purposes inconsistent with their designation by Landlord.
9. The water closets and other water fixtures shall not be used for any purpose other than those for which they were constructed, and any damage resulting to them from misuse and any damage, defacing or injury to any other part of the Property shall be the responsibility of (with related costs to be borne by) the person who shall occasion it. No person shall waste water by interfering with the faucets or otherwise.
10. No person shall disturb occupants of the Property by the use of any radios, record players, tape recorders, musical instruments, the making of unseemly noises or any unreasonable use.
11. Nothing shall be thrown out of the windows of the Property or down the stairways or other passages.
12. Tenant and its employees, agents and invitees shall park their vehicles only in those parking areas designated by Landlord. Tenant shall furnish Landlord with state automobile license numbers of Tenant's vehicles and its employees' vehicles within five (5) days after taking possession of the Leased Premises and shall notify Landlord of any changes within five (5) days after such change occurs. Tenant shall not leave any vehicle in a state of disrepair (including without limitation, flat tires, out of date inspection stickers or licenses plates) on the Leased Premises or on the Property. If Tenant or its employees, agents or invitees park their vehicles in areas other than the designated parking areas or leave any vehicle in a state of disrepair, Landlord, after giving written notice to Tenant of such violation, shall have the right (but not the obligation) to remove such vehicles at Tenant's expense.
13. Parking in the parking facilities related to the Property shall be in compliance with all parking rules and regulations including any sticker or other identification system established by Landlord. Failure to observe the rules and regulations shall terminate Tenant's right to use such parking facilities and subject the vehicle in violation of the parking rules and regulations to removal and impoundment. No termination of parking privileges or removal or impoundment of a vehicle shall create any liability on Landlord or be deemed to interfere with Tenant's right to possession of the Leased Premises. Vehicles must be parked entirely within the stall lines and all direction signs, arrows and posted speed limits must be observed. Parking is prohibited in areas not striped for parking, in areas marked as "Customer" or "Visitor" Parking, in aisles, where "No Parking" signs are posted, on ramps, in cross hatched areas, and in other areas as may be designated by Landlord. Parking stickers or other forms of identification supplied by Landlord shall remain the property of Landlord and shall not become the property of Tenant and are not transferable. Every person is required to park and lock his or her own vehicle. All responsibility for damage to vehicles or persons is assumed by the owner of the vehicle and its driver.

14. Movement in or out of the Property of furniture, office supplies and equipment, or dispatch or receipt by Tenant of any merchandise or materials which requires use of elevators or stairways, or movement through the Property entrances or lobby shall be restricted to hours designated by Landlord. All such movement shall be under supervision of Landlord and carried out in the manner agreed between Tenant and Landlord by prearrangement before performance. Such prearrangement will include determination by Landlord of time, method, and routing of movement and limitations imposed by safety or other concerns which may prohibit any article, equipment or any other item from being brought in to the Property. Tenant assumes, and shall indemnify Landlord against, all risks and claims of damage to persons and properties arising in connection with any said movement.
15. Landlord shall not be liable for any damages from the stoppage of elevators for necessary or desirable repairs or improvements or delays of any sort or duration in connection with elevator service.
16. Tenant shall not lay floor covering within the Leased Premises without written approval of Landlord. The use of cement or other similar adhesive materials not easily removed with water is expressly prohibited.
17. Tenant agrees to cooperate and assist Landlord in the prevention of canvassing, soliciting and peddling at the Property. Tenant shall not, without the prior written consent of Landlord, place any signs or other advertising materials (i) in any of the Common Areas or (ii) in any portion of the Leased Premises visible from any of the Common Areas.
18. During all hours other than Building Standard Hours, Landlord reserves the right to exclude from the Property, all persons who are not known to the Property security personnel and who do not present a pass to the Property signed by Tenant. Each Tenant shall be responsible for all persons to whom Tenant supplies a pass.
19. If any governmental license or permit shall be required for the proper and lawful conduct of Tenant's business, Tenant, before occupying the Leased Premises shall procure and maintain such license or permit and submit it to Landlord for inspection. Tenant shall at all times comply with all terms of any such license or permit.
20. Except with the prior written consent of Landlord, Tenant (i) shall not sell or permit the sale from the Leased Premises of, or (ii) use or permit the use of any sidewalk or mail area adjacent to the Leased Premises for, the sale of newspapers, magazines, periodicals, theater tickets or any other goods or merchandise. Furthermore, Tenant shall not carry on, or permit or allow any employee or other person to carry on, business in or from the Leased Premises for the service or accommodation of occupants of any other portion of the Building, nor shall the Leased Premises be used for manufacturing of any kind, or for any business or activity other than that specifically provided for in the Lease.



21. Tenant shall not install any radio or television antenna, loudspeaker or other device on the exterior walls of the Building.
22. Tenant shall not use in any space, or in the Common Areas, any hand trucks except those equipped with rubber tires and side guards or such other material handling equipment as Landlord may approve. No other vehicles of any kind shall be brought by Tenant into the Building or kept in or about the Leased Premises without prior written approval of Landlord.
23. Tenant shall store all its trash and garbage within the Leased Premises until removal of same by janitorial service to such location on the Property as may be designated from time to time by Landlord. No material shall be placed in the Building trash boxes or receptacles if such material is of such nature that it may not be disposed of in the ordinary and customary manner of removing and disposing of trash and garbage in the city in which the Leased Premises is located without being in violation of any applicable Legal Requirements.
24. Tenant shall not permit the use or the operation of any coin operated machines on the Leased Premises, including without limitation, vending machines, video games, pinball machines, or pay telephones without the prior written consent of Landlord.
25. As used in the Lease, "business days" means Monday through Saturday (except holidays); "Building Standard Hours" means 7:00 a.m. to 6:00 p.m. on weekdays and 8:00 a.m. to 1:00 p.m. on Saturdays; and "holidays" means New Years Day, Memorial Day, Fourth of July, Labor Day, Thanksgiving Day and Christmas Day, together with such other holidays as are designated by Landlord consistent with those holidays designated by landlords of comparable office buildings located in the county in which the Building is located.
26. Landlord desires to maintain the Property in the highest standard of dignity and good taste consistent with comfort and convenience for Tenants. Any action or condition not meeting this high standard should be reported directly to Landlord. Your cooperation will be mutually beneficial and sincerely appreciated. Landlord reserves the right to make such other and further reasonable rules and regulations as in its judgment may from time to time be necessary, for the safety, care and cleanliness of the Leased Premises and the Property and for the preservation of good order therein.
27. Tenant acknowledges and agrees that the Property is a non-smoking facility and that smoking is prohibited in the Property including the Leased Premises, restrooms, stairwells, hallways and other portions of the Common Areas. Tenant shall cause its employees, agents, contractors, visitors and invitees to comply with this and all other Rules and Regulations.

In the event of any conflict between the terms and provisions of these Rules and Regulations and any terms and provisions of the Lease, the terms and provisions of the Lease shall control.

**EXHIBIT "E"**  
**TO OFFICE LEASE**  
**LANDLORD WORK LETTER**

1. Construction.

(a) Landlord agrees to construct certain leasehold improvements (the "Finish Work") in a good and workmanlike manner in and upon the Leased Premises in accordance with construction drawings approved by both Landlord and Tenant ("Final Working Drawings"). Subject to the other applicable terms and conditions of this Exhibit and of the Lease, Landlord shall be responsible for all Costs of Construction (defined below) up to an aggregate amount (the "Finish Allowance") equal to Fourteen and No/100 Dollars (\$14.00) per rentable square foot in the Leased Premises. The Finish Allowance shall be used solely for the purpose of completing the Finish Work in the Leased Premises. Notwithstanding the foregoing, to the extent that there is any unused portion of the Finish Allowance remaining (the "Remaining Allowance") after completion of all Finish Work agreed to by and between Landlord and Tenant as set forth above, then up to an aggregate amount equal to Two and No/100 Dollars (\$2.00) per rentable square foot in the Leased Premises of the Remaining Allowance shall be credited to Tenant evenly over the first (1<sup>st</sup>) twelve (12) calendar months of the Lease Term against Base Rent owing monthly under the Lease. Notwithstanding anything to the contrary contained herein, in no event shall Landlord be obligated under this subparagraph (a) for any amount in excess of the Finish Allowance. Additionally, Landlord shall be permitted to offset against the Finish Allowance any amounts past due to Landlord by Tenant under the Lease.

(b) Landlord will employ a qualified, licensed contractor to construct the Finish Work and will require in any construction contract that such contractor construct the Finish Work in a good and workmanlike manner and in compliance with all Legal Requirements; provided, however, Tenant will be solely responsible for determining whether or not Tenant is a public accommodation under The Americans with Disabilities Act and whether or not the Final Working Drawings comply with such law and the regulations thereunder. The parties acknowledge that (i) Landlord is not an architect or engineer, and that the Finish Work will be designed and performed by independent architects, engineers and contractors ("Third Parties"), and (ii) Landlord does not guarantee or warrant that the plans or Final Working Drawings will be free from errors or omission, or that the Finish Work will be free from defects (provided, however, that Landlord agrees to use reasonable efforts to cooperate in any action Tenant desires to bring against applicable Third Parties).

2. Costs.
- (a) Tenant shall be obligated to pay to Landlord the amount by which the Costs of Construction exceed the Finish Allowance (the “Tenant Amounts”) as follows: (i) fifty percent (50%) of the Tenant Amounts shall be payable at such time, and from time to time, as the Costs of Construction are determined by Landlord to be in excess of the Finish Allowance, and (ii) the remaining actual Tenant Amounts shall be payable to Landlord at such time as the applicable Tenant Amounts are payable by Landlord (and Tenant shall make such payments in clauses (i) and (ii) immediately above to Landlord within ten (10) days after Landlord provides Tenant with an invoice therefor). Notwithstanding the foregoing, costs arising out of change orders requested by Tenant and approved by Landlord after construction has commenced and which increase the Costs of Construction shall be paid by Tenant to Landlord within five (5) days of receipt of an invoice therefor from Landlord.
- (b) All installations and improvements now or hereafter placed in the Leased Premises other than building standard improvements shall be for Tenant’s account and at Tenant’s cost (and Tenant shall pay ad valorem taxes and increased insurance thereon or attributable thereto), which cost shall be payable by Tenant to Landlord upon demand as additional rent.
- (c) Tenant further agrees to pay Landlord’s construction management company a fee (the “Construction Management Fee”) of five percent (5%) of the Costs of Construction as compensation for its supervision of the construction and installation of the Finish Work no later than the commencement of construction thereof. Landlord and Tenant agree that the Construction Management Fee may be paid out of the Finish Allowance to the extent funds are available for such purpose. Tenant agrees that in the event of default of payment thereof, Landlord (in addition to all other remedies) shall have the same rights as in the event of default of payment of Rent under the Lease.
3. Substantial Completion. When Landlord considers the Finish Work to be Substantially Complete (defined below), it shall deliver to Tenant notice thereof (the “Notice of Substantial Completion”) which will (i) stipulate any so called “punch list” items which in Landlord’s determination remain incomplete, and (ii) set forth the Date of Substantial Completion (defined below).
4. Warranties. LANDLORD SHALL MAKE NO WARRANTIES, EXPRESS OR IMPLIED, WITH RESPECT TO THE FINISH WORK. ALL IMPLIED WARRANTIES WITH RESPECT THERETO, INCLUDING BUT NOT LIMITED TO THOSE OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE, ARE EXPRESSLY NEGATED AND WAIVED. WITHOUT LIMITING THE FOREGOING, LANDLORD SHALL NOT BE RESPONSIBLE FOR FAILURE OF THE FINISH WORK. Landlord will assign to Tenant, without recourse, any warranties obtained from contractors, subcontractors, suppliers and other Third Parties to the extent such warranties are assignable (provided that in no event shall Landlord be obligated under any such warranties).

5. Landlord Liability. Notwithstanding anything to the contrary set forth in the Lease or in this Exhibit, if the Commencement Date is delayed for any reason (including without limitation, the failure by any current tenant or occupant of any portion of the Leased Premises to vacate any portion of the Leased Premises), Landlord shall not be liable or responsible for any claims, damages or liabilities in connection therewith or by reason thereof, nor shall such delay constitute a default by Landlord hereunder.
6. Time is of the Essence. It is stipulated that time is of the essence in connection with Landlord's and Tenant's compliance with the terms of this Exhibit. Without limitation of the foregoing, it is also stipulated and agreed that Landlord's obligation to undertake any Finish Work or other leasehold improvements (other than "punch list" items) under this Exhibit and Landlord's obligations with respect to the Finish Allowance shall terminate automatically (and without further act or instrument) upon Substantial Completion.
7. Definitions.
- (a) "Costs of Construction" shall mean all costs and expenses of any kind whatsoever related to or arising out of the Finish Work, including, without limitation, (i) all amounts payable to contractors, subcontractors, artisans, laborers, architects, construction managers (including Landlord's construction management company), suppliers of materials and/or manufacturers of materials and engineers with respect to the Finish Work, (ii) all costs and expenses of space planning and design (including, without limitation, costs and expenses directly attributable to space plans and construction drawings, including the Final Working Drawings), and (iii) the cost of an asbestos survey.
- (b) "Date of Substantial Completion" shall mean the date which is the earlier of: (i) the date on which the Finish Work is Substantially Complete, or (ii) the date on which the Finish Work would have been Substantially Complete but for a Tenant Delay, both as reasonably determined by Landlord.
- (c) "Substantially Complete" and "Substantial Completion" shall mean (i) that the Finish Work has been performed in the Leased Premises in substantial accordance with the Final Working Drawings (exclusive of any "punch list" items), (ii) all construction debris has been removed from the Leased Premises and the Leased Premises are clean, and (iii) the Leased Premises may reasonably be used and occupied by Tenant for general office purposes and/or for the Permitted Use.
- (d) "Tenant Delay" shall mean the number of days Substantial Completion is delayed as a result of (i) Tenant's failure to meet any dates established in the Lease or this Exhibit, (ii) any changes to the Finish Work requested to be made by Tenant (and approved by Landlord), (iii) Tenant's failure to sufficiently respond to any of Landlord's inquiries or demands, (iv) any breach by Tenant of its obligations under the Lease, including without limitation, the failure to comply with this Exhibit, and (v) any other delay or delays caused by Tenant or Tenant's engineers, architects, consultants, employees, agents, contractors and subcontractors.

**RIDER "1"**  
**OPTION TO EXTEND**  
**(Two-Time)**

Tenant, at its option, may extend the Lease Term for two (2) successive additional periods of forty-eight (48) months each (the first such period, the "First Extension Period," the second such period, the "Second Extension Period," and each, an "Extension Period"). In order to exercise its option to extend as provided for in this Rider, (i) Tenant must provide Landlord with written notice of its intent to extend the Lease Term at least six (6) months prior to the expiration of the Lease Term (which, in the case of Tenant's exercise of its option with respect to the Second Extension Period, shall be six (6) months prior to the expiration of the First Extension Period), and (ii) Tenant must not be in default (taking into account any applicable notice and cure periods) of its obligations under the Lease either at the time it sends such notice to Landlord or at the time that the applicable Extension Period commences. Upon the service of such notice and subject to the conditions set forth in the preceding sentence, Landlord shall, within ten (10) business days after receipt of Tenant's written notice, notify Tenant in writing of Landlord's determination of the Prevailing Market Rate (defined below) for the Leased Premises during the applicable Extension Period. The "Prevailing Market Rate" for the applicable Extension Period shall be the prevailing rental rate for properties of equivalent quality, size, and utility, in the office submarket in which the Building is located, with the length of the lease term, Landlord concessions, and the credit standing of Tenant to be taken into account. Tenant shall, within thirty (30) business days of receipt of Landlord's written notice of Landlord's determination of the Prevailing Market Rate, notify Landlord in writing of its acceptance, dispute, or rejection of Landlord's determination of the Prevailing Market Rate. If Tenant rejects Landlord's determination or does not timely respond, then the Lease will terminate at the end of the Lease Term (without renewal, or further renewal [as the case may be]). If Tenant disputes Landlord's determination of the Prevailing Market Rate, and Landlord and Tenant are not able to reach a mutual agreement as to the Prevailing Market Rate during the following thirty (30) business day period, then the Lease will terminate at the end of the Lease Term. If Tenant accepts Landlord's determination, or Tenant and Landlord otherwise agree upon the Prevailing Market Rate, this Lease shall be extended without the necessity of the execution of any further instrument or document. Such Extension Period shall (A) commence upon the expiration date of the Lease Term (which, in the case of the Second Extension Period, shall be the date upon which the First Extension Period expires), (B) expire upon the same day of the forty-eighth (48) calendar month thereafter, and (C) be upon the same terms, covenants, and conditions as provided in the Lease for the initial Lease Term, except that the Base Rent payable during an Extension Period shall be at the Prevailing Market Rate as determined above beginning at the commencement of the applicable Extension Period. Payment of all additional rent and other charges required to be made by Tenant under the Lease for the initial Lease Term shall continue to be made during the applicable Extension Period in accordance with the terms and provisions of the Lease. Any assignment of the Lease or subletting of the Leased Premises by Tenant shall terminate the option(s) to extend the Lease Term contained herein. Notwithstanding the foregoing, in no event shall Base Rent for an Extension Period be less than the Base Rent during

the last year of the initial Lease Term (which, in the case of the Second Extension Period, shall be the last year of the First Extension Period). Notwithstanding any provision to the contrary contained in this Rider, Tenant shall not have the option to extend the Lease Term for the Second Extension Period unless it has properly exercised its option to extend the Lease Term for the First Extension Period.

**RIDER "2"**

**TENANT'S PREFERENTIAL RIGHT TO LEASE**

1. Prior to Landlord's leasing that certain contiguous space on the first (1<sup>st</sup>) floor of the Building, designated on Exhibit "A-1" as the additional space (the "Additional Space"), to third parties (other than (i) the tenant then in possession of the Additional Space or (ii) any tenant currently holding a right to expand into, or right of first refusal on, the Additional Space), Landlord shall first offer to lease to Tenant the Additional Space before leasing such space to any third party. Such offer shall be in writing and specify the lease terms for the Additional Space, including the rent to be paid for the Additional Space, the term therefor, and the date on which the Additional Space shall be included in the Leased Premises (the "Offer Notice"). Tenant shall notify Landlord in writing whether Tenant elects to lease the entire Additional Space on the terms set forth in the Offer Notice, within five (5) days after the day on which Landlord delivers to Tenant the Offer Notice. If Tenant timely elects to lease the Additional Space, then Landlord and Tenant shall execute an amendment to the Lease, effective as of the date the Additional Space is to be included in the Leased Premises. Such amendment shall specify the terms set forth in the Offer Notice to the extent not inconsistent with the terms of this Lease; however, Tenant shall accept the Additional Space in its "AS-IS, WHERE-IS, WITH ALL FAULTS" condition, and Landlord shall not provide to Tenant any allowance (e.g. moving allowance, construction allowance, and the like) or other tenant inducements except as specifically provided in the Offer Notice. If Tenant fails to timely notify Landlord of its acceptance of the Offer Notice, Tenant shall be deemed to have rejected the same.

Notwithstanding the foregoing, if prior to Landlord's delivery to Tenant of the Offer Notice, Landlord has received an offer to lease all or part of the Additional Space from a third party (a "Third Party Offer") and such Third Party Offer includes space in excess of the Additional Space, Tenant must exercise its right hereunder, if at all, as to all of the space contained in the Third Party Offer. If Tenant fails or is unable to timely exercise its right hereunder, then such right shall lapse, time being of the essence with respect to the exercise thereof, and Landlord may lease all or any portion of the Additional Space to third parties on such terms as Landlord may elect. Tenant may not exercise its rights under this Rider if an event of default under the Lease exists or, if after the Commencement Date, Tenant is not then occupying the entire Leased Premises. For purposes hereof, if an Offer Notice is delivered for less than all of the Additional Space but such notice provides for an expansion, right of first refusal, or other preferential right to lease some of the remaining portion of the Additional Space, then such remaining portion of the Additional Space shall thereafter be excluded from the provisions of this Rider.

2. Furthermore, Tenant's rights under this Rider shall terminate if (a) the Lease or Tenant's right to possession of the Leased Premises is terminated; (b) Tenant assigns any of its interest in the Lease or sublets any portion of the Leased Premises, other than in conjunction with a Permitted Affiliate; or (c) Tenant rejects (or is deemed to have rejected) any Offer Notice or Third Party Offer.

**RIDER "3"**  
**TERMINATION OPTION**

Subject to the terms of this Rider, Tenant shall have the option ("Termination Option") to terminate this Lease effective upon the date (the "Termination Date") which is the last day of the twenty-fourth (24<sup>th</sup>) full calendar month during the Lease Term by: (i) notifying Landlord (the "Notification") in writing of Tenant's exercise of the Termination Option at least four (4) months prior to the Termination Date; and (ii) paying to Landlord, in cash or its equivalent, concurrently with delivery of the Notification, a termination fee equal to the sum of all unamortized leasing costs (bearing interest at ten percent (10%) per annum compounded monthly) incurred by Landlord with respect to the Lease and/or Tenant's occupancy of the Leased Premises. Should Tenant exercise the Termination Option in accordance with the foregoing terms and provisions, the Lease shall terminate on the Termination Date, and neither Landlord nor Tenant shall have any further liability or obligation under the Lease after the Termination Date; provided, however, that neither Landlord nor Tenant shall be relieved of or from any of its obligations, covenants and/or liabilities arising under the Lease, or in any way relating to the Leased Premises, which accrue on or prior to the Termination Date, including without limitation any obligation of indemnity or reimbursement arising under the Lease.

If Tenant fails to exercise the Termination Option in accordance with all terms and provisions of the foregoing paragraph, then the Termination Option shall be deemed void and Tenant shall have automatically and forever waived Tenant's right to exercise the Termination Option. Notwithstanding any provision of the Lease or of this Rider to the contrary, Tenant shall not be entitled to exercise the Termination Option if: (i) any event of default exists either at the time of the Notification or on the Termination Date; (ii) Tenant is not then occupying the entire Leased Premises; and/or (iii) Tenant has assigned any of its interest in this Lease or sublet any portion of the Leased Premises.



**OFFICE LEASE**

This lease ("Lease") is made as of January 6, 2006 by and between the Landlord and the Tenant named below.

**ARTICLE 1. BASIC LEASE TERMS**

For the purposes of this Lease the following underlined terms shall have the meanings set forth below:

**1.1 LANDLORD.** RMC MIDWAY WALNUT, LP

**1.2 TENANT.** PC CONNECTION SALES OF MASSACHUSETTS, INC.

**1.3 BUILDING.** That certain office building commonly known as the Midway Atrium III located at 14295 Midway Road, in the City of Addison, Dallas County, Texas 75001. The Building and the land on which the Building is situated together with all other buildings, structures, fixtures and other improvements located thereon from time to time are collectively referred to herein as the "Property".

**1.4 LEASED PREMISES.** That portion of the Building highlighted on the Site Plan attached to this Lease as Exhibit "A", on the floor(s) indicated thereon, resulting in an aggregate area hereby deemed to consist of 10,729 rentable square feet in the Building, commonly referred to as Suite 100.

**1.5 LEASE TERM.** Forty-eight (48) months, beginning on the Commencement Date; provided that if the Commencement Date is a date other than the first (1<sup>st</sup>) day of a calendar month, the Lease Term shall be said number of months in addition to the remainder of the calendar month following the Commencement Date.

**1.6 COMMENCEMENT DATE.** The Commencement Date shall be the earliest to occur of (i) the date Tenant takes possession of the Leased Premises for the purpose of conducting its business therefrom, (ii) the Date of Substantial Completion (as defined in the Work Letter attached to this Lease as Exhibit "E" [if any]) or (iii) March 1, 2006. Notwithstanding the foregoing, the Commencement Date shall constitute the commencement of the Lease Term for all purposes, whether or not Tenant has actually taken possession of the Leased Premises.

**1.7 BASE RENT.** Tenant shall pay, in accordance with the terms and provisions of Section 2.2 of this Lease, Base Rent for the lease and use of the Leased Premises at the annual rental rate per rentable square foot of space in the Leased Premises for the specific time periods set forth below:

<u>Time Period</u>	<u>Annual Rental Rate Per Rentable Square Foot</u>	<u>Applicable Monthly Rent</u>
Months 1 – 48	\$ 13.50	\$ 12,070.13

**1.8 SECURITY DEPOSIT.** Twelve Thousand Seventy and 13/100 Dollars (\$12,070.13), due and payable concurrently with the execution of this Lease.

**1.9 ADDRESSES.**

<u>Landlord's Address</u>	<u>Tenant's Address</u>	<u>Manager's Address</u>
RMC Midway Walnut, LP  5944 Luther Lane Suite 501 Dallas, Texas 75225	PC Connection Sales of Massachusetts, Inc. 14295 Midway Road Suite 100 Addison, Texas 75001	R.M. Crowe Property Management, LP 14275 Midway Road Suite 120 Addison, Texas 75001

Landlord, Tenant and Manager, by written notice to the others may change from time to time their respective addresses, and Landlord, by written notice to Tenant, may notify Tenant from time to time of the appointment of a new Manager and such new Manager's address.

**1.10 PERMITTED USE.** To provide general office services and other lawful incidental office uses directly related thereto, but for no other purpose.

**1.11 COMMON AREAS.** Such parking areas, streets, driveways, aisles, sidewalks, curbs, delivery passages, loading areas, lighting facilities, and all other areas situated on or in the Property which are designated by Landlord, from time to time, for use by all tenants of the Property in common.

**1.12 GUARANTOR.** Intentionally deleted.

**1.13 BUILDING STANDARD HOURS.** Under all applicable terms and conditions of this Lease, Building Standard Hours shall be Monday through Friday, 7:00 a.m. through 6:00 p.m. and Saturday 8:00 a.m. through 1:00 p.m.

**ARTICLE 2. GRANTING CLAUSE AND RENT PROVISIONS**

**2.1 GRANT OF PREMISES.** In consideration of the obligation of Tenant to pay the rent and other charges as provided in this Lease and in consideration of the other terms and provisions of this Lease, Landlord hereby leases the Leased Premises to Tenant during the Lease Term, subject to the terms and provisions of this Lease. Tenant's parking rights are set forth in Exhibit "B" attached to this Lease.

**2.2 BASE RENT.** Tenant agrees to pay monthly the Base Rent set forth in Section 1.7 of this Lease, which Base Rent shall be payable by Tenant to Landlord at the address shown in Section 1.9 of the Lease or at such other address as Landlord in writing shall notify Tenant. One (1) monthly installment of Base Rent shall be due and payable on the date of execution of this Lease by Tenant for the first (1<sup>st</sup>) month's Base Rent and a like monthly installment shall be due and payable on or before the first (1<sup>st</sup>) day of each calendar month succeeding the Commencement Date during the Lease Term, without abatement, notice, demand, offset, reduction or counterclaim; provided, however, that if the Commencement Date should be a date other than the first (1<sup>st</sup>) day of a calendar month, the monthly rental set forth above shall be prorated to the end of that calendar month, and all succeeding installments of Base Rent shall be payable on or before the first (1<sup>st</sup>) day of each succeeding calendar month during the Lease Term.

**2.3 OPERATING EXPENSES; UTILITIES; AND TAXES.**

(a) The "Base Year" shall mean the calendar year 2006; provided, however, that in the event that the Property is less than ninety-five percent (95%) occupied during the Base Year, the Operating Expenses (defined below) for the Base Year shall be grossed up as if the Property were ninety-five percent (95%) occupied for the Base Year.

(b) If the Operating Expenses, in any calendar year during the Lease Term exceed the Operating Expenses for the Base Year, Tenant shall pay as additional rent Tenant's Proportionate Share (defined below) of Excess Operating Expenses (defined below). "Tenant's Proportionate Share" shall be the percentage obtained by dividing the number of rentable square feet in the Leased Premises by the total number of rentable square feet in the Property. "Excess Operating Expenses" shall mean the amount by which Operating Expenses in a particular calendar year exceed the Operating Expenses for the Base Year. Landlord may invoice Tenant monthly for Tenant's estimated share of Excess Operating Expenses for each calendar year, subsequent to the Base Year, beginning on the first day of the month of the first subsequent calendar year. Landlord may adjust its estimate by notice to Tenant at any time during the applicable calendar year if actual Operating Expenses are substantially different from the estimate, and thereafter payments by Tenant under this Section shall adjust accordingly. Within approximately one hundred twenty (120) days following the end of each calendar year, Landlord shall provide Tenant an accounting (the "Accounting") showing in reasonable detail all computations of additional rent under this Section. If the Accounting shows that the total of the monthly payments made by Tenant exceeds the amount of additional rent due by Tenant under this Section, the Accounting shall be accompanied by a refund. If the Accounting shows that the total of the monthly payments by Tenant is less than the amount of additional rent due by Tenant under this Section, the Accounting shall be accompanied by an invoice for the additional rent. Notwithstanding any other provisions in this Lease, Landlord, within one (1) year following the expiration of the Lease Term or earlier termination of this Lease, shall have the option to invoice Tenant for Tenant's Proportionate Share of Excess Operating Expenses for the year in which this Lease

terminates based upon that year's actual Operating Expenses. If this Lease shall terminate on a day other than the last day of a calendar year, the amount of any additional rent payable by Tenant applicable to the year in which such termination shall occur shall be prorated on the ratio that the number of days from the commencement of the calendar year to and including the termination date bears to 365. Notwithstanding anything to the contrary contained in this Lease, if the Property is not ninety-five percent (95%) occupied during any calendar year, Tenant's additional rent under this Section and the Operating Expenses shall be determined as if the Property had been ninety-five percent (95%) occupied during such year. Tenant agrees to pay any additional rent due under this Section within thirty (30) days following receipt of the invoice and/or Accounting showing additional rent due.

(c) The term "Operating Expenses" includes all expenses paid by Landlord with respect to the maintenance, servicing, repairing and operation of the Property, including, but not limited to the following: maintenance, repair and replacement costs; fuel, landscaping and pest control; management fees, including those payable to any affiliate of Landlord; wages and benefits payable to employees of Landlord whose duties are directly connected to the operation and maintenance of the Property; all service, supplies, repairs, replacement or other expenses for maintaining and operating the Property including parking and common area; the cost, including interest, amortized over its useful life, of any capital improvement made to the Property by Landlord which is required under any applicable Legal Requirements (defined below); the cost, including interest, amortized over its useful life, of installation of any device or other equipment designed or intended to improve the operating efficiency of any system within the Leased Premises; all other expenses which generally would be regarded as operating and maintenance expenses which would reasonably be amortized over a period not to exceed five (5) years; and all insurance premiums Landlord is required to pay or deems necessary to pay, including public liability insurance and casualty insurance, with respect to the Property. The term "Operating Expenses" does not include the following: Taxes (as hereinafter defined) and Utilities (as hereinafter defined); expenses for repairs, restoration or other work occasioned by fire, wind, the elements or other casualty that are covered by Landlord's insurance; income and franchise taxes of Landlord (except to the extent a tax on the rental income produced from the Property); expenses incurred in leasing to or procuring of tenants, leasing commissions, advertising expenses and expenses for the renovating of space for new tenants; interest or principal payments on any mortgage or other indebtedness of Landlord; any depreciation allowance or expense; or expenses which are the responsibility of Tenant.

(d) The "Tax Base Year" shall mean the calendar year 2006; provided, however, that in the event that the Property is less than ninety-five percent (95%) occupied during the Base Year, the Taxes for the Tax Base Year shall be grossed up as if the Property were ninety-five percent (95%) occupied for the Tax Base Year.

(e) If the Taxes, in any calendar year during the Lease Term exceed the Taxes for the Tax Base Year, Tenant shall pay as additional rent Tenant's Proportionate Share of Excess Taxes (defined below). "Excess Taxes" shall mean the amount by which Taxes

in a particular calendar year exceed the Taxes for the Tax Base Year. Landlord may invoice Tenant monthly for Tenant's estimated share of Excess Taxes for each calendar year, subsequent to the Tax Base Year, beginning on the first day of the month of the first subsequent calendar year. Landlord may adjust its estimate by notice to Tenant at any time during the applicable calendar year if actual Taxes are substantially different from the estimate, and thereafter payments by Tenant under this Section shall adjust accordingly. Landlord and Tenant will follow the procedures for annual Accounting as stated in Section 2.3(b) above. Notwithstanding any other provisions in this Lease, Landlord, within one (1) year following the expiration of the Lease Term or earlier termination of this Lease, shall have the option to invoice Tenant for Tenant's Proportionate Share of Excess Taxes for the year in which this Lease terminates based upon that year's actual Taxes. Notwithstanding anything to the contrary contained in this Lease, if the Property is not ninety-five percent (95%) occupied during any calendar year, Tenant's additional rent under this Section and the Taxes shall be determined as if the Property had been ninety-five percent (95%) occupied during such year. Tenant agrees to pay any additional rent due under this Section within thirty (30) days following receipt of the invoice and/or Accounting showing additional rent due.

The term "Taxes" includes all ad valorem taxes paid by Landlord with respect to the Property, including, but not limited to all real property taxes and installments of special assessments, including dues and assessments by means of deed restrictions and/or owner's associations which accrue against the Property during the Lease Term (including costs of contesting assessed values and/or taxes); governmental levies or charges of any kind or nature assessed or imposed on the Property, whether by state, county, city or any political subdivision thereof.

(f) The "Utilities Base Year" shall mean the calendar year 2006; provided, however, that in the event that the Property is less than ninety-five percent (95%) occupied during the Base Year, the Utilities for the Utilities Base Year shall be grossed up as if the Property were ninety-five percent (95%) occupied for the Utilities Base Year.

(g) If the Utilities, in any calendar year during the Lease Term exceed the Utilities for the Utilities Base Year, Tenant shall pay as additional rent Tenant's Proportionate Share of Excess Utilities (defined below). "Excess Utilities" shall mean the amount by which Utilities in a particular calendar year exceed the Utilities for the Utilities Base Year. Landlord may invoice Tenant monthly for Tenant's estimated share of Excess Utilities for each calendar year, subsequent to the Utilities Base Year, beginning on the first day of the month of the first subsequent calendar year. Landlord may adjust its estimate by notice to Tenant at any time during the applicable calendar year if actual Utilities are substantially different from the estimate, and thereafter payments by Tenant under this Section shall adjust accordingly. Landlord and Tenant will follow the reconciliation and Accounting procedures established in Section 2.3(b) above. Notwithstanding any other provisions in this Lease, Landlord, within one (1) year following the expiration of the Lease Term or earlier termination of this Lease, shall have the option to invoice Tenant for Tenant's Proportionate Share of Excess Utilities for the year in which this Lease terminates based upon that year's actual Utilities.

Notwithstanding anything to the contrary contained in this Lease, if the Property is not ninety-five percent (95%) occupied during any calendar year, Tenant's additional rent under this Section and the Utilities shall be determined as if the Property had been ninety-five percent (95%) occupied during such year. Tenant agrees to pay any additional rent due under this Section within thirty (30) days following receipt of the invoice and/or Accounting showing additional rent due.

(h) The term "Utilities" includes all utility expenses paid by Landlord with respect to the maintenance, servicing, repairing and operation of the Property, including, but not limited to the following: cable, telephone, electricity, water, sewer, gas.

**2.4 ADDITIONAL RENT.** Tenant agrees to pay all rent and other sums of money (whether specified in this Article 2, pursuant to indemnity or reimbursement obligations or otherwise) as shall become due from and payable by Tenant to Landlord under this Lease (collectively, the "Rent") at the times and in the manner provided in this Lease, without abatement, notice, demand, offset, reduction or counterclaim (except as otherwise provided in this Lease). All Rent in addition to Base Rent shall constitute additional rental under this Lease and Landlord shall be entitled to exercise the same rights and remedies provided for in this Lease for the nonpayment of any Rent.

**2.5 LATE PAYMENT CHARGE.** Other remedies for nonpayment of Rent notwithstanding, if any regular monthly installment of Rent is not received by Landlord on or before the fifth (5<sup>th</sup>) day of the month for which such Rent is due, a late payment charge of ten percent (10%) of such past due amount shall become due and payable in addition to any other amounts due and payable. In addition, all Rent owed by Tenant to Landlord under this Lease shall bear interest from the date due until the date received at a rate (the "Interest Rate") equal to the lesser of the highest rate allowable under applicable law or eighteen percent (18%) per annum.

**2.6 INCREASE IN INSURANCE PREMIUMS.** If an increase in any insurance premiums paid by Landlord for the Property is caused by Tenant's use of the Leased Premises in a manner other than as set forth in Section 1.10 of this Lease, or if Tenant vacated the Leased Premises and caused an increase in such premiums, then Tenant shall pay as additional rent the amount of such increase to Landlord. Tenant agrees to pay any amount due under this Section within ten (10) days following receipt of the invoice showing the additional rent due.

**2.7 SECURITY DEPOSIT.** The Security Deposit (if any), as set forth in Section 1.8 of this Lease, shall be paid by Tenant to Landlord, in cash or by certified check, on the date of execution of this Lease by Tenant and shall be held by Landlord as security for the performance of Tenant's covenants and obligations under this Lease, it being expressly understood that the Security Deposit shall not be considered an advance payment of Rent or a measure of Landlord's damages in case of default hereunder by Tenant, and shall be held by Landlord without payment of any interest thereon. Upon the occurrence of any event of default or breach of a covenant by Tenant under this Lease, Landlord may, from time to time, without prejudice to any other remedy, use the Security Deposit to the extent necessary to make good any arrearage of Rent, or to repair any damage or injury, or pay any expense or liability incurred by Landlord as a result of

such event of default or breach of covenant, and any remaining balance of the Security Deposit shall be returned by Landlord to Tenant upon the termination of this Lease. If any portion of the Security Deposit is so used or applied, Tenant shall upon ten (10) days written notice from Landlord, deposit with Landlord, by cash or certified check, an amount sufficient to restore the Security Deposit to its original amount. The Security Deposit may be assigned and transferred by Landlord to the successor in interest of Landlord and, upon acknowledgment by such successor of receipt of such Security Deposit and its assumption of the obligation to account to Tenant for the Security Deposit in accordance with the terms and provisions of this Lease, Landlord shall thereby be discharged of any further obligation relating thereto.

**2.8 HOLDING OVER.** If Tenant does not vacate the Leased Premises upon the expiration or earlier termination of this Lease, as may be extended by Tenant pursuant to Tenant's exercise of the option to extend set forth in Rider "1" attached to this Lease, Tenant shall be deemed to be holding over, and all of the terms and provisions of this Lease shall be applicable during the holdover period, except that (i) the term of Tenant's tenancy shall be terminable at any time by either party and (ii) Tenant shall pay Landlord (in addition to additional rent and any other sums payable under this Lease) as base rental for the period of such holdover an amount equal to two (2) times the greater of (a) the Base Rent which was payable by Tenant during the last month of the initial Lease Term or (b) the then current market rent for the Leased Premises (without waiver of Landlord's right to recover damages as permitted by law). Upon the expiration of this Lease, Tenant agrees to vacate and deliver the Leased Premises (and all keys thereto) in good condition, to Landlord upon delivery to Tenant of notice from Landlord to vacate. The Rent payable during the holdover period shall be payable to Landlord on demand. No holding over by Tenant, whether with or without the consent of Landlord, shall operate to extend the Lease Term. Tenant shall indemnify Landlord against all claims made by any tenant or prospective tenant against Landlord resulting from delay by Landlord in delivering possession of the Leased Premises to such other tenant or prospective tenant.

**2.9 SURRENDER OF LEASED PREMISES.**

(a) Upon the expiration or earlier termination of this Lease, Tenant shall peaceably surrender to Landlord the Leased Premises broom-clean and in the condition the same were in on the Commencement Date, subject only to (i) ordinary and customary wear and tear, and (ii) damage resulting from condemnation, a fire or other casualty.

(b) Notwithstanding anything in this Lease to the contrary, all permanent or built-in fixtures or improvements and all mechanical, electrical and plumbing ("MEP") equipment in the Leased Premises shall be the property of Landlord upon the expiration or earlier termination of this Lease. Except as otherwise provided, all furnishings, equipment, furniture, trade fixtures and other removable equipment installed in the Leased Premises by Tenant and paid for by Tenant shall remain the property of Tenant and shall be removed by Tenant upon the expiration or termination of this Lease. Tenant shall repair any damage caused by such removal. If any of Tenant's furnishings, equipment, furniture, trade fixtures or other removable equipment are not removed on or prior to the expiration or earlier termination of this Lease, then Tenant hereby grants to Landlord the option, exercisable at any time thereafter without the requirement of any

notice to Tenant: (i) to treat such property or any portion thereof as being abandoned by Tenant to Landlord, whereupon Landlord shall be deemed to have full rights of ownership thereof; (ii) to elect to remove and store such property, or any portion thereof, on Tenant's behalf (but without assuming any liability to any person) and at Tenant's sole cost and expense, with reimbursement therefor to be made to Landlord upon demand; and/or (iii) to sell, give away, donate or dispose of as trash or refuse any or all of such property without any responsibility to deliver to Tenant any proceeds therefrom. Landlord shall have no liability of any kind whatsoever to Tenant with respect to the exercise or failure to exercise the options set forth in this Section 2.9(b). Specifically, Tenant shall not have the right to assert against Landlord a claim either for the value, or the use, of any such property, either as an offset against any amount of money owing to Landlord or otherwise.

### **ARTICLE 3. OCCUPANCY, USE AND OPERATIONS**

**3.1 USE.** Tenant warrants and represents to Landlord that the Leased Premises shall be used and occupied only for the purpose as set forth in Section 1.10 of this Lease. Tenant shall occupy the Leased Premises, conduct its business and control its agents, employees, invitees and visitors in such a manner as is lawful, reputable and will not create a nuisance to other tenants in the Property. Tenant shall not solicit business, distribute handbills or display merchandise within the Common Areas. Tenant shall not permit any operation which emits any odor or matter which intrudes into other portions of the Property, use any apparatus or machine which makes undue noise or causes vibration in any portion of the Property or otherwise interfere with, annoy or disturb any other tenant in its normal business operations or Landlord in its management of the Property. Tenant shall neither permit any waste on the Leased Premises nor allow the Leased Premises to be used in any way which would, in the opinion of Landlord, be extra hazardous on account of fire or which would in any way increase the cost of or render void the fire insurance on the Property. Tenant may not use or allow or permit the Leased Premises to be used in any way or for any purpose that is visible from the exterior of the Leased Premises, adversely affects ventilation in other areas of the Building, creates unreasonable elevator loads, causes structural loads to be exceeded, creates unreasonable noise levels, or is in violation of any applicable Legal Requirements (defined below).

**3.2 SIGNS.** No signs of any type or description shall be erected, placed or painted by Tenant on or about the exterior of the Leased Premises without the prior written consent of Landlord. Landlord reserves the right to remove, at Tenant's expense, all exterior signs other than signs approved in writing by Landlord under this Section 3.2, without notice to Tenant, and Landlord shall not be liable to Tenant for damages sustained by Tenant as a result thereof. Tenant shall be permitted to erect signage within the interior of the Leased Premises, provided that all such signage be removed by Tenant upon the expiration or earlier termination of this Lease. Tenant shall repair any damage caused by such removal.

**3.3 COMPLIANCE WITH LAWS, RULES AND REGULATIONS.** Tenant, at Tenant's sole cost and expense, shall comply with all laws, ordinances, orders, rules and regulations of any and all state, federal, municipal and/or other agencies and/or bodies having jurisdiction over the use, condition or occupancy of the Leased Premises, or which are applicable



in the jurisdiction(s) in which the Property is located (all of the foregoing, the "Legal Requirements"). Tenant shall procure at its own expense all permits and licenses required for the transaction of its business in the Leased Premises. Tenant will comply with the Rules and Regulations of the Property adopted by Landlord which are set forth in Exhibit "D" attached to this Lease. If Tenant is not complying with the Rules and Regulations, or if Tenant is in any way not complying with any term or provision of this Article 3, then, notwithstanding anything to the contrary contained herein, Landlord may, at its election, enter the Leased Premises without liability therefor and fulfill Tenant's obligations, provided, however, Tenant may contest same in good faith, provided that such contest is made in a lawful manner. Tenant shall reimburse Landlord on demand for any expenses which Landlord may incur in effecting compliance with Tenant's obligations and agrees that Landlord shall not be liable for any damages resulting to Tenant from such action. Landlord shall have the right at all times to change and amend the Rules and Regulations in any reasonable manner as it may deem advisable for the safety, care, cleanliness, preservation of good order and operation or use of the Property or the Leased Premises. All changes and amendments to the Rules and Regulations of the Property will be forwarded by Landlord to Tenant in writing and shall thereafter be carried out and observed by Tenant.

**3.4 WARRANTY OF POSSESSION.** Landlord and Tenant each hereby warrants to the other that it has the right and authority to execute this Lease, and Landlord warrants to Tenant, that upon payment of the required Rent by Tenant and compliance by Tenant with all the terms, provisions, conditions, covenants and agreements contained in this Lease, Tenant shall have possession of the Leased Premises during the Lease Term, as well as any extension or renewal thereof, without hindrance from Landlord or any person or persons lawfully claiming the Leased Premises by, through or under Landlord (but not otherwise); subject, however, to all mortgages, deeds of trust, leases and agreements to which this Lease is subordinate and to all Legal Requirements.

**3.5 LANDLORD'S RIGHT OF ENTRY.** Without limitation of Landlord's other rights of entry set forth in this Lease, Landlord or its authorized agents, with prior notice to Tenant, shall at any and all reasonable times have the right to enter the Leased Premises during Building Standard Hours to inspect the same, and to supply janitorial service or any other service to be provided by Landlord. Upon prior written notice to Tenant, Landlord may enter the Leased Premises to show the Leased Premises to prospective mortgagees or prospective purchasers. Upon prior written notice to Tenant, and for a period of time beginning ninety (90) calendar days prior to the expiration of the Lease Term, Landlord may enter the Leased Premises to show the Leased Premises to prospective tenants; provided, however, Landlord's right to show the Leased Premises to prospective tenants shall terminate upon Tenant's submission of its notice to extend the Lease Term pursuant to Tenant's exercise of the option to extend set forth in Rider "1". Landlord shall at all times have and retain a key with which to unlock all of the doors in, upon and about the Leased Premises. Notwithstanding anything to the contrary contained herein, Landlord shall have the right at all times to enter the Leased Premises by any means in the event of an emergency without liability therefor.

**3.6 PERSONAL PROPERTY TAXES.** Tenant shall be liable for all taxes levied against leasehold improvements, merchandise, personal property, trade fixtures and all other

taxable property located in the Leased Premises. If any such taxes for which Tenant is liable are levied against Landlord or Landlord's property and if Landlord elects to pay the same or if the assessed value of Landlord's property is increased by inclusion of personal property and trade fixtures placed by Tenant in the Leased Premises and Landlord elects to pay the taxes based on such increase, Tenant shall pay to Landlord, upon demand, that part of such taxes for which the Tenant is primarily liable pursuant to the terms of this Section. Tenant shall pay when due all taxes related to Tenant's use and operation of its business in the Leased Premises.

**3.7 EARLY OCCUPANCY.** If for any reason, Tenant or any of its employees, agents, contractors, guests or invitees enter the Leased Premises prior to the Commencement Date, Tenant acknowledges and agrees that such entrance into the Leased Premises shall be subject to each and every term and provision of this Lease, other than those requiring Tenant to pay Base Rent or additional rent as a result of such occupancy prior to the Commencement Date.

#### **ARTICLE 4. UTILITIES AND SERVICE**

**4.1 BUILDING SERVICES.** Landlord shall furnish Tenant water at those points of supply provided for general use of other tenants in the Building (subject to the terms and provisions of Sections 7.1, 7.2, 8.1 and 8.2 of this Lease), electrical power not to exceed at any given time four (4) watts per rentable square foot of space in the Leased Premises, pest control, and central heating and air conditioning in season, on business days during Building Standard Hours, and at temperatures and in amounts as are considered by Landlord to be standard or in compliance with any applicable Legal Requirements; provided that heating and air conditioning service at times other than Building Standard Hours shall be furnished by way of overtime heating and air conditioning. In accordance with, and subject to, the terms and provisions set forth below in this Section 4.1, Tenant must notify Landlord at least twenty-four (24) hours in advance of Tenant's need for overtime heating and air conditioning and Tenant shall bear the entire cost thereof at the rate established by Landlord from time to time (currently, Fifty and No/100 Dollars (\$50.00) per hour per half-floor) and will be billed monthly by Landlord. Landlord shall provide routine maintenance, painting and electric lighting service for all Common Areas and for any special service areas of the Property (as designated by Landlord) in the manner and to the extent deemed by Landlord to be standard. Landlord may, in its sole discretion, provide additional services not enumerated herein. Failure by Landlord to any extent to provide these defined services or any other services not enumerated, or any cessation thereof, shall not render Landlord liable in any respect for damages to either person or property, be construed as an eviction of Tenant, work as an abatement of Rent or relieve Tenant from fulfillment of any covenant or obligation under this Lease. If any of the equipment or machinery which is useful or necessary for provision of utility services, and for which Landlord is responsible, breaks down or for any cause ceases to function properly, Landlord shall use reasonable diligence to repair the same promptly, but Tenant shall have no claim for abatement of Rent or offset or damages on account of any interruption in service occasioned from such repairs. Landlord reserves the right from time to time to make changes in the utilities and services provided by Landlord to the Property (including the Leased Premises).

**4.2 THEFT OR BURGLARY.** Landlord shall not be liable to Tenant for losses to Tenant's property or personal injury caused by criminal acts or entry by unauthorized persons in the Leased Premises or on the Property.

**4.3 JANITORIAL SERVICE.** Landlord shall furnish janitorial service to the Leased Premises and the Common Areas of the Building five (5) times per week during the Lease Term, excluding holidays. Landlord shall not provide janitorial service to kitchen or storage areas located in the Leased Premises. Should (i) Landlord fail to provide or (ii) Tenant elect not to receive, janitorial or any other building service, Landlord shall not be liable to Tenant in any respect for damages, nor shall such failure or election work as an abatement of Rent or relieve Tenant from fulfillment of any covenant or obligation under this Lease.

**4.4 EXCESSIVE UTILITY CONSUMPTION.** Without limitation of the terms and provisions set forth in Section 2.3 of this Lease, Tenant shall pay all utility costs occasioned by electrodata processing machines, telephone equipment, computers and other equipment of high electrical consumption as determined by Landlord, including (without limitation) the cost of installing, servicing and maintaining any special or additional inside or outside wiring or lines, meters or submeters, transformers, poles, air conditioning costs, or the cost of any other equipment necessary to increase the amount or type of electricity or power available to the Leased Premises. If Tenant's electricity use exceeds the limits specified in Section 4.1 of this Lease or any of Tenant's equipment generates excessive heat, Landlord may also, at its sole option and without any obligation to do so, install supplemental air conditioning units in and/or meters for the Leased Premises to monitor Tenant's excess electricity usage and/or to offset the heat-generating effect of Tenant's excess electricity usage and Tenant's equipment and Tenant shall pay Landlord the installation cost and the cost of operation, use, repair, and replacement of such supplemental air conditioning units and/or meters on demand as additional rent.

**4.5 WINDOW COVERINGS.** Landlord may (but shall not be obligated to) furnish and install window coverings on all exterior windows to maintain a uniform exterior appearance. Tenant shall not remove or replace these window coverings or install any other window covering which would affect the exterior appearance of the Building. Tenant may install lined or unlined over draperies on the interior sides of the Landlord furnished window coverings for interior appearance or in order to reduce light transmission, provided such over draperies do not (in Landlord's determination) affect the exterior appearance of the Building or affect the operation of the Building's heating, ventilating and air conditioning systems.

**4.6 CHARGE FOR SERVICE.** All costs of Landlord for providing the services set forth in this Article 4 shall be subject to the additional rent provisions in Article 2 of this Lease and shall be payable as therein provided.

## **ARTICLE 5. REPAIRS AND MAINTENANCE**

**5.1 LANDLORD REPAIRS.** Landlord shall not be required to make any improvements, replacements or repairs of any kind or character in or to the Leased Premises during the Lease Term except as set forth in this Section. Landlord shall maintain only the roof, foundation, parking and Common Areas, elevators, the structural soundness of the exterior walls,

doors, corridors, windows, and other structures or equipment servicing the Leased Premises. Landlord's cost of maintaining and repairing the items set forth in this Section are subject to the provisions set forth in Section 2.3 of this Lease. Landlord shall not be liable to Tenant, except as expressly provided in this Lease, for any damage or inconvenience, and Tenant shall not be entitled to any damages nor to any abatement, offset or reduction of Rent by reason of any repairs, alterations or additions made by Landlord under this Lease.

**5.2 TENANT REPAIRS.** Tenant, at its own costs and expense, shall maintain the Leased Premises in a first-class condition (except for those items that are the responsibility of Landlord under Section 5.1 of this Lease) and shall repair, maintain and/or replace any damage or injury to all or any part of the Leased Premises and/or the Property caused by any act or omission of Tenant or Tenant's agents, employees, invitees, licensees or visitors. All repairs and replacements must be equal in quality and class to the original work. If Tenant fails to commence any such repairs and/or replacements within five (5) days after written notice from Landlord, and thereafter diligently proceed with such repair until completion, then Landlord may at its option make the repairs and replacements and Tenant shall pay Landlord on demand as additional rent the costs incurred by Landlord plus any administrative fee equal to fifteen percent (15%) of the costs. If Tenant requests Landlord to perform any maintenance or repairs to the Leased Premises, over and above the services required to be performed by Landlord pursuant to Article 4 of this Lease, Tenant shall pay the actual cost thereof, plus an administrative fee equal to fifteen percent (15%) of the actual cost thereof, to Landlord as additional rent within five (5) business days after demand.

**5.3 REQUEST FOR REPAIRS.** All requests for repairs or maintenance that are the responsibility of Landlord pursuant to any provision of this Lease must be made in writing to Landlord at the address in Section 1.9 of this Lease.

**5.4 TENANT DAMAGES.** Tenant shall not allow any damage to be committed on any portion of the Leased Premises or the Property, and at the termination of this Lease, by lapse of time or otherwise, Tenant shall deliver the Leased Premises to Landlord in accordance with all terms and provisions of Section 2.9 of this Lease in as good condition as existed at the Commencement Date of this Lease, reasonable wear and tear and casualty excepted. The cost and expense of any repairs necessary to restore the condition of the Leased Premises shall be borne by Tenant.

## ARTICLE 6. ALTERATIONS AND IMPROVEMENTS

### 6.1 CONSTRUCTION.

(a) If any construction or tenant improvements are to be performed in or to the Leased Premises in connection with Tenant's initial occupancy of the Leased Premises under this Lease, then such construction shall be accomplished, and the cost of such construction shall be borne by Landlord and/or Tenant in accordance with the terms and provisions of the Work Letter attached hereto as Exhibit "E" (if any), and Landlord and Tenant hereby agree to comply with all terms and provisions of the same.

(b) Tenant has made a complete examination and inspection of the Leased Premises and, except as may be expressly provided to the contrary in Exhibit "E" (if any), Tenant accepts the Leased Premises in its current condition, as-is, where-is and with all faults, without recourse to Landlord, and Landlord shall have no obligation to complete any improvements in or to the Leased Premises. ADDITIONALLY, LANDLORD SHALL MAKE NO WARRANTIES, EXPRESS OR IMPLIED, WITH RESPECT TO THE LEASEHOLD IMPROVEMENTS IN THE LEASED PREMISES. ALL IMPLIED WARRANTIES WITH RESPECT THERETO, INCLUDING BUT NOT LIMITED TO THOSE OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE, ARE EXPRESSLY NEGATED AND WAIVED. Furthermore, subject to the terms of Exhibit "E" (if any), Tenant hereby waives any defects in the Leased Premises and acknowledges and accepts (1) the Leased Premises as suitable for the purpose for which they are leased and (2) the Property and every part and appurtenance thereof as being in good and satisfactory condition. Upon the request of Landlord, Tenant shall deliver to Landlord a completed acceptance of premises memorandum in Landlord's standard form.

**6.2 TENANT IMPROVEMENTS.** Tenant shall not make or allow to be made any alterations, physical additions or improvements to the Leased Premises without first obtaining the written consent of Landlord, which consent may in the sole and absolute discretion of Landlord be denied. If Landlord is requested to make any such alterations, physical additions or improvements for Tenant, Tenant shall pay to Landlord, in addition to the cost of such work, a fee equal to fifteen percent (15%) of the cost of such work. Any alterations, physical additions or improvements to the Leased Premises made by or installed by either party hereto shall remain upon and be surrendered with the Leased Premises and become the property of Landlord upon the expiration or earlier termination of this Lease without credit to Tenant; provided, however, Landlord at its option may require Tenant to remove any physical improvement or additions and/or repair any alterations in order to restore the Leased Premises to the condition existing at the time Tenant took possession (all cost of such removal and/or repairs to be borne by Tenant). The foregoing sentence shall not apply to moveable equipment, furniture, or movable trade fixtures owned by Tenant, which items may be removed by Tenant at the end of the Lease Term if Tenant is not then in default and if such equipment and furniture are not then subject to any other rights, liens and interests of Landlord. Tenant shall have no authority or power, express or implied, to create or cause any mechanic's or materialmen's lien, charge or encumbrance of any kind against the Leased Premises, the Property or any portion thereof. Tenant shall promptly cause any such liens that have arisen by reason of any work claimed to have been undertaken by or through Tenant to be released by payment, bonding or otherwise within thirty (30) days after request by Landlord, and shall indemnify Landlord against losses arising out of any such claim or claims (including, without limitation, legal fees and costs of court). Alterations, improvements, and additions in and to the Leased Premises requested by Tenant must be made in accordance with complete and accurate plans and specifications and construction documents (including, without limitation, complete MEP requirements) prepared by Tenant and approved in advance by Landlord. All work must be performed at Tenant's expense either by Landlord or by contractors and/or subcontractors approved in advance by Landlord. Tenant shall ensure that all workers are cooperative with Property personnel and comply with all Property rules and regulations. Tenant must deliver to Landlord evidence that Tenant has obtained all necessary governmental permits and approvals for the improvements or alterations prior to starting any work. All construction

must be done in a good and workmanlike manner and is subject to approval by Landlord during and after construction to determine compliance with the approved plans and specifications and construction documents, in Landlord's sole discretion. Tenant must use Landlord's fire protection contractor and must either (1) use Landlord's MEP engineer to prepare the MEP portions of the plans and specifications and construction documents, or (2) reimburse the cost of one review by Landlord's MEP engineer of the plans and specifications and construction documents. All alterations and improvements by Tenant must comply with all Legal Requirements. If Tenant's use of or alterations or additions to the Leased Premises cause Landlord to make any alterations or improvements to the Property to comply with the provisions of the Americans With Disabilities Act of 1990 (as amended), the Texas Architectural Barriers Act (as amended) [Tex. Rev. Civ. Stat. Ann. Art. 9102], and/or any other similar law, rule or regulation relating to access by disabled persons to the Leased Premises or the Property, Tenant shall reimburse Landlord for the cost of the alterations or improvements (plus a fee equal to fifteen percent (15%) of such costs) upon demand as additional rent.

**6.3 COMMON AND SERVICE AREA ALTERATIONS.** Landlord shall have the right (i) to decorate and to make repairs, alterations, additions, changes or improvements, whether structural or otherwise, in, about or on the Property or any part thereof, (ii) to change, alter, relocate, remove or replace Common Areas and any special service areas of the Property (as designated by Landlord), (iii) to place, inspect, repair and replace in the Leased Premises (below floors, above ceilings or next to columns) utility lines, pipes and the like in order to serve other areas of the Property outside the Leased Premises and (iv) to otherwise alter or modify the Property, and for such purposes (set forth in subclauses (i) through (iv) above) Landlord shall have the right to enter upon the Leased Premises and, during the continuance of any such work, to take such measures for safety or for the expediting of such work as may be required, in Landlord's judgment, all without affecting any of Tenant's obligations hereunder, and without entitling Tenant to any damages or to any abatement, offset or reduction of Rent.

## ARTICLE 7. CASUALTY AND INSURANCE

**7.1 SUBSTANTIAL DESTRUCTION.** If in the determination of Landlord (i) the Leased Premises should be totally destroyed by fire or other casualty, (ii) the Leased Premises should be damaged so that rebuilding cannot be substantially completed within one hundred eighty (180) working days after Landlord's receipt of written notification by Tenant of such damage, or (iii) the Leased Premises are damaged or destroyed by casualty not covered by Landlord's fire and extended coverage insurance, then, at Landlord's sole option, this Lease may be terminated. If the Property or the Building is so damaged by fire or other casualty that substantial alteration or reconstruction of the Property or the Building is, in Landlord's sole opinion, required (whether or not the Leased Premises are damaged) or if any mortgagee under a mortgage or deed of trust covering the Property requires that the insurance proceeds payable as a result of the fire or other casualty be used to pay down or retire the mortgage debt, Landlord may, at its sole option, terminate this Lease. If Landlord terminates this Lease under this Section, Rent shall be abated for the unexpired portion of the Lease, effective as of the date of Tenant's written notification to Landlord of the applicable destruction and/or damage.

**7.2 PARTIAL DESTRUCTION.** In the event that the Leased Premises, or any portion thereof, shall be damaged by fire or other casualty, Tenant shall provide Landlord written notice of the same as soon as practicable thereafter. If following damage or destruction to the Leased Premises by fire or other casualty, this Lease is not terminated pursuant to Section 7.1 of this Lease, Landlord shall proceed, to the extent of insurance proceeds actually received by Landlord after the exercise by a mortgagee of the Property of an option to apply proceeds against Landlord's debt to such mortgagee, with reasonable diligence to rebuild or repair the Building or other improvements to substantially the same conditions in which they existed prior to such damage or destruction. If the Leased Premises are to be rebuilt or repaired and are untenantable in whole or in part following the damage, and the damage or destruction was not caused or contributed to by act or negligence of Tenant, its agents, employees, invitees or others for whom Tenant is responsible, the Rent payable under this Lease during the period for which the Leased Premises are untenantable shall be reduced to an amount determined by multiplying the Base Rent that would otherwise be payable but for this provision by the ratio that the portion of Leased Premises not rendered untenantable bears to the total net rentable area of the Leased Premises prior to the casualty. Landlord's obligation to rebuild or restore under this Section shall be limited to restoring the Leased Premises to substantially the condition in which the same existed prior to the casualty, exclusive of improvements for which Tenant is responsible under the terms of Exhibit "E" (if any) described in Section 6.1 of this Lease, and Tenant shall, promptly after the completion of such work by Landlord, proceed with reasonable diligence (and at Tenant's sole cost and expense) to restore those improvements for which Tenant is responsible under the terms of Exhibit "E" (if any) to substantially the condition in which the same existed prior to the casualty and to otherwise make the Leased Premises suitable for Tenant's use. Landlord shall in no event be obligated to expend for such repair or replacements any amount in excess of the insurance proceeds actually received by Landlord (i.e. after the exercise by a mortgagee of the Property of an option to apply proceeds against Landlord's debt to such mortgagee). If the cost of repair and replacements for the leasehold improvements (based on Landlord's or its contractor's estimate of the cost) exceeds the insurance proceeds received by Landlord from Tenant's insurance carrier (which Tenant shall cause its insurance carrier to pay to Landlord), the shortfall shall be paid by Tenant to Landlord prior to Landlord's repair of the damage (to the extent to which Landlord is required to perform such repairs and replacements under the terms and provisions of this Section 7.2 and/or Exhibit "E" [if any]). Landlord is not liable for any inconvenience or annoyance to Tenant or injury to the business of Tenant resulting in any way from casualty damage or any repairs related to the same. If Landlord has failed to substantially complete the repairs and/or replacements required by this Section 7.2 and/or Exhibit "E" (if any) within two hundred seventy (270) working days from the date of Landlord's receipt of written notification by Tenant of the applicable damage or destruction at issue, Tenant may at its option terminate this Lease by delivering written notice of such termination to Landlord prior to the date on which Landlord has substantially completed Landlord's work under this Section 7.2 and/or Exhibit "E" (if any).

**7.3 PROPERTY INSURANCE.** Landlord shall at all times during the Lease Term insure the Property against all risk of direct physical loss in such amounts and with such deductibles as Landlord considers appropriate; provided, Landlord shall not be obligated in any way or manner to insure any personal property (including, but not limited to, any furniture, machinery, goods or supplies) of Tenant upon or within the Leased Premises, any fixtures

installed or paid for by Tenant upon or within the Leased Premises, or any improvements which Tenant may construct on the Leased Premises. Tenant shall have no right in or claim to the proceeds of any policy of insurance maintained by Landlord even if the cost of such insurance is borne by Tenant as set forth in Article 2 of this Lease. Landlord shall have the right to self-insure. At all times during the Lease Term, Tenant shall, at its own expense, keep in full force and effect insurance against fire and such other risks as are from time to time included in standard all-risk insurance (including coverage against vandalism and malicious mischief) for the full insurable value of Tenant's trade fixtures, furniture, supplies and all items of personal property of Tenant located upon or within the Leased Premises. Landlord shall be named as an additional insured on said policy.

**7.4 WAIVER OF SUBROGATION.** ANYTHING IN THIS LEASE TO THE CONTRARY NOTWITHSTANDING, LANDLORD AND TENANT HEREBY WAIVE AND RELEASE EACH OTHER OF AND FROM ANY AND ALL RIGHTS OF RECOVERY, CLAIM, ACTION OR CAUSE OF ACTION, AGAINST EACH OTHER, THEIR AGENTS, OFFICERS AND EMPLOYEES, FOR ANY LOSS OR DAMAGE THAT MAY OCCUR TO THE LEASED PREMISES, IMPROVEMENTS TO THE PROPERTY, OR PERSONAL PROPERTY WITHIN THE PROPERTY **REGARDLESS OF CAUSE OR ORIGIN, INCLUDING THE NEGLIGENCE OF LANDLORD OR TENANT AND/OR THE AGENTS, OFFICERS AND/OR EMPLOYEES OF EITHER,** IF SUCH LOSS OR DAMAGE IS COVERED BY INSURANCE. LANDLORD AND TENANT AGREE IMMEDIATELY TO GIVE THEIR RESPECTIVE INSURANCE COMPANIES WHICH HAVE ISSUED POLICIES OF INSURANCE COVERING ALL RISK OF DIRECT PHYSICAL LOSS, WRITTEN NOTICE OF THE TERMS OF THE MUTUAL WAIVERS CONTAINED IN THIS SECTION, AND TO HAVE THE INSURANCE POLICIES PROPERLY ENDORSED, IF NECESSARY TO PREVENT THE INVALIDATION OF THE INSURANCE COVERAGE BY REASON OF THE MUTUAL WAIVERS.

**7.5 HOLD HARMLESS.** Landlord shall not be liable to Tenant or to Tenant's customers, employees, agents, guests or invitees, or to any other person whomever, for any injury to persons or damage to property on or about the Leased Premises or the Common Areas, including but not limited to, consequential damage, (1) caused by any act or omission of Tenant, its employees, subtenants, licensees and concessionaires or of any other person entering the Property or the Leased Premises by express or implied invitation of Tenant, or (2) arising out of the use of the Leased Premises or the Property by Tenant, its employees, subtenants, licensees, concessionaires or invitees, or (3) arising out of any breach or default by Tenant in the performance of its obligations hereunder, or (4) caused by the improvements located in the Leased Premises becoming out of repair or by any defect in or failure of equipment, pipes, or wiring, or by broken glass, or by the backing of drains, or by gas, water, steam, electricity or oil leaking, escaping or flowing into the Leased Premises or the Property, or (5) arising out of the failure or cessation of any service provided by Landlord (including, without limitation, security services and devices), and Tenant hereby agrees to indemnify Landlord and hold Landlord harmless from any liability, loss, expense or claim (including, without limitation, reasonable attorney's fees and costs of court) arising out of any such damage or injury. Landlord shall not be liable to Tenant for any loss or damage that may be occasioned by or through the acts or omissions of Tenant or of any other persons whomsoever. Further, Tenant specifically agrees to



be responsible for and to indemnify and hold Landlord harmless from any and all damages or expenses of whatever kind arising out of or caused by burglary, theft, vandalism, malicious mischief or any other illegal act performed in, at or from the Leased Premises.

**7.6 LIABILITY INSURANCE.** Tenant at all times during the Lease Term shall, at its own expense, keep in full force and effect comprehensive general liability insurance with "personal injury" coverage and contractual liability coverage, within minimum limits of Two Million and No/100 Dollars (\$2,000,000.00) on account of bodily injuries to, or death of, one or more than one person as the result of any one accident or occurrence and Five Hundred Thousand and No/100 Dollars (\$500,000.00) on account of damage to property as the result of any one accident or occurrence. Landlord and Landlord's lenders shall be named as additional insureds on such policy, and such policy shall provide that (i) such insurance shall be primary and shall not contribute with any insurance carried by Landlord and (ii) the insurance company issuing the same shall notify Landlord thirty (30) days prior to the expiration date of the policy if the policy is not renewed prior to such date. All insurance policies or duly executed certificates for the same required to be carried by Tenant under this Lease, together with satisfactory evidence of the payment of the premiums thereof, shall be deposited with Landlord on the date Tenant first occupies the Leased Premises and upon renewals of such policies not less than fifteen (15) days prior to the expiration of the term of the same. All insurance required to be carried by Tenant under this Lease shall be in form and content, and written by insurers, reasonably acceptable to Landlord. If Tenant shall fail to comply with any of the requirements contained herein relating to insurance, Landlord may obtain such insurance and Tenant shall pay to Landlord, on demand, as additional rent hereunder, one hundred fifteen percent (115%) of the premium cost thereof.

**7.7 BOILER INSURANCE.** At all times when a "boiler," as that term is defined for the purposes of boiler insurance, is located within the Leased Premises, Tenant shall carry, at its expense, boiler insurance with policy limits of not less than One Hundred Thousand and No/100 Dollars (\$100,000.00) insuring both Landlord and Tenant against loss or liability caused by the operation or malfunction of such boiler. If no so-called boiler is located within the Leased Premises, then this Section 7.7 shall not apply to Tenant.

**7.8 ENVIRONMENTAL MATTERS.** Throughout the Lease Term, Tenant shall comply with all applicable Legal Requirements regarding health, safety and/or the environment and shall prevent the presence, use, generation, release, discharge, storage, disposal, or transportation of any Hazardous Materials (defined below) on, under, in, above, to, or from the Property and/or the Leased Premises other than in strict compliance with all applicable Legal Requirements. For purposes of this provision, the term "Hazardous Materials" shall mean and refer to any wastes, materials, or substances of any kind or character that are or become regulated as hazardous or toxic waste or substances, or which require special handling or treatment, under any applicable Legal Requirements (including, without limitation, under the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as now or later amended, the Resource Conservation and Recovery Act, as now or later amended, and/or the Toxic Substance Control Act of 1976, as now or later amended). To the extent to which the same may result from Tenant's failure to comply with the terms and provisions of this Section 7.8, Tenant shall indemnify, defend, and hold Landlord harmless from and against (i) any loss, cost, expense, claim, or liability arising out of any investigation, monitoring, enforcement action, clean-up,

containment, removal, storage, or remediation work (herein called "Remediation") required by any applicable Legal Requirements, or by any government agency, authority, or political subdivision having jurisdiction over the Leased Premises, or which may be incurred by Landlord or any other person or party in a reasonable belief that such Remediation is or will be required by any applicable Legal Requirements, or by any government agency, authority, or political subdivision having jurisdiction over the Leased Premises, and (ii) any claims of third parties for loss, injury, expense, or damage arising out of the presence, release, or discharge of any Hazardous Materials on, under, in, above, to, or from the Leased Premises. In the event any Remediation is so required under any applicable Legal Requirements, Tenant shall promptly perform or cause to be performed such Remediation in compliance with such Legal Requirements. In the event Tenant shall fail to commence the Remediation in a timely fashion, or shall fail to prosecute diligently the Remediation to completion, such failure shall constitute an event of default on the part of Tenant under this Lease, and Landlord, in addition to any other rights or remedies afforded it under this Lease, may, but shall not be obligated to, cause the Remediation to be performed, and Tenant shall promptly reimburse Landlord for the cost and expense thereof upon demand.

#### ARTICLE 8. CONDEMNATION

**8.1 CONDEMNATION.** If the Leased Premises shall be taken or condemned (or sold in lieu thereof) for any public purpose to such an extent as to render the Leased Premises untenable, either party shall have the right to terminate this Lease by giving notice of such election to terminate to the other party within ten (10) days from the date of such condemnation or taking (or sale in lieu thereof), which termination shall be effective on the date of the transfer of possession of the Leased Premises to the condemning authority. If only a portion thereof shall be so taken so as not to render the remainder untenable, this Lease shall not terminate, and Base Rent shall be diminished by an equitable amount (based upon the number of rentable square feet of the Leased Premises so taken) and Landlord shall, to the extent practicable, restore the Leased Premises so that the remaining portion of the Leased Premises shall be partitioned off from the portion so taken or condemned; however, Landlord shall be obligated to restore or rebuild the damaged property only to the extent the holder of any mortgage or deed of trust or the landlord under any ground lease makes the proceeds of such taking available to Landlord for the purposes of rebuilding and restoration, or if no mortgage or ground lease then affects the Building or the Property, then only to the extent of the net proceeds of such taking. If all or substantially all of the Building or the Property (whether or not the Leased Premises are affected), or a portion of the Building or the Property (whether or not the Leased Premises are affected) as to cause the remainder of the Building or the Property not to be economically feasible to operate, as reasonably determined by Landlord, should be taken or condemned (or sold in lieu thereof) for any public purpose, then this Lease, at the option of Landlord upon the giving of notice to Tenant within ten (10) days from the date of such condemnation or taking (or sale in lieu thereof), shall cease and terminate effective on the date of the transfer of possession of the Leased Premises to the condemning authority. If this Lease is terminated in accordance with this Section 8.1, Base Rent shall be apportioned on a per diem basis and shall be payable through the effective date of the termination.

**8.2 TEMPORARY TAKING.** In the event of any taking or condemnation for any public purpose of the Leased Premises or any portion thereof occurs for one hundred eighty (180) days or less, then it shall be deemed a temporary taking, this Lease shall continue in full force and effect, Landlord shall be under no obligation to make any repairs or alterations, and at Landlord's option either (i) there shall be no abatement of Base Rent and all proceeds of such taking relating to the Lease Term occurring during such taking shall belong to Tenant, or (ii) Base Rent shall be diminished by an equitable amount (based upon the number of rentable square feet so taken) for the period of time the Leased Premises are so taken and Landlord shall be entitled to the proceeds of such taking.

**8.3 CONDEMNATION PROCEEDS.** All proceeds from any taking or condemnation (or sale in lieu thereof) of the Leased Premises or any portion of the Property shall belong to and be paid to Landlord, and Tenant shall not be entitled to any portion of such award (except that Tenant shall have all rights permitted under the laws of the state in which the Property is located to appear, claim and prove in proceedings relative to such taking (i) the value of any fixtures, furnishings, and other personal property which are taken but which under the terms and provisions of this Lease Tenant is permitted to remove at the end of the Lease Term, (ii) the unamortized cost [such costs having been amortized on a straight line basis over the Lease Term excluding any renewal terms] of Tenant's leasehold improvements which are taken that Tenant is not permitted to remove at the end of the Lease Term and which were installed solely at Tenant's expense [i.e. not paid for by Landlord or purchased with allowances provided by Landlord], and (iii) relocation and moving expenses, but not the value of Tenant's leasehold estate created by this Lease and only so long as such claims in no way diminish the award Landlord receives from the condemning authority).

## ARTICLE 9. ASSIGNMENT OR SUBLEASE

### 9.1 TENANT ASSIGNMENT.

(a) Tenant shall not assign, in whole or in part, this Lease, or allow it to be assigned, in whole or in part, by operation of law or otherwise (including without limitation by merger, dissolution or transfer of a controlling interest in any partnership or corporate Tenant, which merger, dissolution or transfer shall be deemed an assignment) or mortgage or pledge the same, or sublet the Leased Premises, in whole or in part, without the prior written consent of Landlord, and in no event shall any such assignment or sublease ever release Tenant from any obligation or liability hereunder. No assignee or sublessee of the Leased Premises or any portion thereof may assign or sublet the Leased Premises or any portion thereof. Notwithstanding anything in this Section 9.1 to the contrary, Tenant may assign its interest in this Lease to any entity controlled by and majority owned by PC Connection, Inc., a Delaware corporation, with a principal address of 730 Milford Road, Merrimack, New Hampshire 03054.

(b) For the purposes hereof, (A) the transfer of the ownership or voting rights in a controlling interest of the voting stock of Tenant (if Tenant is a corporation), (B) the transfer of any general partnership interest or the transfer of twenty-five percent (25%) of the limited partnership interest in Tenant (if Tenant is a partnership), (C) the transfer of

any ownership or membership interest in Tenant (if Tenant is a limited liability company), (D) the merger or consolidation of Tenant with or into any other corporation or entity, or (E) a sale or transfer of fifty percent (50%) or more of Tenant's assets, at any time during the Lease Term shall be deemed to be an assignment of this Lease.

**9.2 CONDITIONS OF TENANT ASSIGNMENT.** Except as otherwise permitted within Section 9.1 of this Lease, if Tenant desires to assign or sublet all or any part of the Leased Premises, it shall so notify Landlord in writing at least thirty (30) days in advance of the date on which Tenant desires to make such assignment or sublease. Tenant shall provide Landlord with a copy of the proposed assignment or sublease and such information as Landlord might request concerning the proposed sublessee or assignee to allow Landlord to make informed judgments as to the financial condition, reputation, operations and general desirability of the proposed sublessee or assignee. Within fifteen (15) days after Landlord's receipt of Tenant's proposed assignment or sublease and all required information concerning the proposed sublessee or assignee, Landlord shall have the following options: (1) cancel this Lease as to the Leased Premises or portion thereof proposed to be assigned or sublet; (2) consent to the proposed assignment or sublease, and if the rent due and payable by an assignee or sublessee under any such permitted assignment or sublease (or a combination of the rent payable under such assignment or sublease plus any bonus or any other consideration or any payment incident thereto) exceeds the Rent payable under this Lease for such space, Tenant shall pay to Landlord all such excess rent and other excess consideration within ten (10) days following receipt thereof by Tenant; or (3) refuse, in its sole and absolute discretion and judgment, to consent to the proposed assignment or sublease, which refusal shall be deemed to have been exercised unless Landlord gives Tenant written notice stating otherwise. Landlord's consent to any assignment, subletting, or reorganization is not a waiver of Landlord's right to approve or disapprove any subsequent assignment, subletting, or reorganization. Tenant shall remain liable for the payment of Rent and performance of all other obligations under this Lease after any assignment or subletting. Receipt by Landlord of rent from any assignee, sublessee, or occupant of the Leased Premises is not a waiver of the covenant against assignment and subletting or a release of Tenant. In no event shall the following be considered as suitable assignees or sublessees under this Lease: any governmental body, agency or bureau (of the United States, any state, county, municipality or any subdivision thereof); any foreign government or subdivision thereof; any health care professional or health care service organization; schools or similar organizations; employment agencies; radio, television or other communication stations; restaurants; and retailers offering retail services from the Leased Premises. Notwithstanding the giving by Landlord of its consent to any sublease or assignment with respect to the Leased Premises, no sublessee or assignee may exercise any renewal options, expansion options, preferential rights to lease (i.e. rights of first offer or rights of first refusal) or similar rights under this Lease. Tenant may not exercise any renewal options, expansion options, preferential rights to lease (i.e. rights of first offer or rights of first refusal) or similar rights under this Lease if Tenant has assigned any portion of its interest in this Lease or subleased any portion of the Leased Premises. Upon the occurrence of an event of default of Tenant under this Lease, if all or any part of the Leased Premises are then assigned or sublet, Landlord, in addition to any other remedies provided by this Lease or provided by law, may at its option, collect directly from the assignee or sublessee all rents becoming due to Tenant by reason of the assignment or sublease, and Landlord, in addition to any other remedies provided by this Lease or provided by law, may, at its option, collect directly from the assignee

or sublessee all rents becoming due to Tenant by reason of the assignment or sublease, and Landlord shall have a security interest in all properties belonging to Tenant on the Leased Premises to secure payment of such sums. No collection directly by Landlord from the assignee or sublessee shall be construed to constitute a novation or a release of Tenant from the further performance of its obligations under this Lease. If Landlord agrees to an assignment of the Lease or sublease of the Leased Premises, Tenant shall pay Landlord (i) One Thousand Five Hundred and No/100 Dollars (\$1,500.00) to reimburse Landlord for the administrative costs associated with such assignment or sublease and (ii) an amount equal to all legal fees and expenses incurred by Landlord in connection with the review by Landlord of Tenant's requested assignment or sublease pursuant to this Section, together with any legal fees and disbursements incurred by Landlord in the preparation and/or review of any documentation. Tenant shall be required to pay such amounts within five (5) days of demand for payment thereof, as additional rent under this Lease.

**9.3 LANDLORD ASSIGNMENT.** Landlord shall have the right to sell, transfer or assign, in whole or in part, its rights and obligations under this Lease and in the Property. Any such sale, transfer or assignment shall operate to release Landlord from any and all liabilities under this Lease arising after the date of such sale, assignment or transfer.

**9.4 RIGHTS OF MORTGAGEE.** Tenant accepts this Lease subject and subordinate to any recorded Lease, mortgage or deed of trust lien presently existing, if any, or hereafter encumbering the Property and to all existing ordinances and recorded restrictions, covenants, easements, and agreements with respect to the Property. Landlord hereby is irrevocably vested with full power and authority to subordinate Tenant's interest under this Lease to any mortgage or deed of trust lien hereafter placed on the Property. Upon any foreclosure, judicially or non-judicially, of any such mortgage or lien, or the sale of the Property in lieu of foreclosure, or any other transfer of Landlord's interest in the Property, whether or not in connection with a mortgage or lien (any of foregoing forms of transfer, a "Transfer"), Tenant hereby does, and hereafter agrees to attorn to the purchaser at such foreclosure or to any other transferee of Landlord's interest, and shall recognize such purchaser, grantee, or other transferee as Landlord under this Lease, and no further attornment or other agreement shall be required to effect or evidence Tenant's attornment to and recognition of such purchaser or grantee as Landlord hereunder. Such agreement of Tenant to attorn shall survive any such foreclosure sale, trustee's sale, conveyance in lieu thereof, or any other transfer of Landlord's interest in the Property. Tenant, upon demand, at any time before or after any such foreclosure sale, trustee's sale, conveyance in lieu thereof, or other transfer shall execute, acknowledge and deliver to the prospective transferee and/or mortgagee a subordination and attornment agreement in a form acceptable to such mortgagee, and any additional written instruments and certificates evidencing such attornment as the mortgagee or other prospective transferee may reasonably require, and Tenant hereby irrevocably appoints Landlord as Tenant's agent and attorney-in-fact for the purpose of executing, acknowledging, and delivering any such instruments and certificates. Notwithstanding anything to the contrary set forth or implied in this Section: (a) any mortgagee under any mortgage shall have the right at any time to subordinate any such mortgage to this Lease on such terms and subject to such conditions as the mortgagee in its discretion may consider appropriate (specifically, without limitation, any such mortgagee may require that the casualty and condemnation provisions of this Lease remain subordinate to any applicable

mortgage even in the event that such mortgagee chooses to subordinate the remainder of such mortgage to this Lease); and (b) no transferee of Landlord's interest in this Lease by way of any Transfer shall be responsible for or liable with respect to any representation, warranty, act, omission or default by Landlord under this Lease, or for the return of any Security Deposit (except to the extent to which such Security Deposit has been actually received by such transferee).

**9.5 ESTOPPEL CERTIFICATE.** Tenant agrees to furnish, from time to time, within ten (10) business days after receipt of a request from Landlord or Landlord's mortgagee, a statement certifying, if applicable, the following: Tenant is in possession of the Leased Premises; the Lease is in full force and effect; the Lease is unmodified (except as disclosed in such statement); Tenant claims no present charge, lien, or claim of offset against Rent; all Rent is paid for the current month, but is not prepaid for more than one (1) month and will not be prepaid for more than one (1) month in advance; there is no existing default by reason of any act or omission by Landlord; that Landlord has performed all inducements required of Landlord in connection with this Lease, including construction obligations, and Tenant accepts the Leased Premises as constructed; an acknowledgment of the assignment of rentals and other sums due hereunder to the mortgagee and agreement to be bound thereby; an agreement requiring Tenant to advise the mortgagee of damage to or destruction of the Leased Premises by fire or other casualty requiring reconstruction; an agreement by Tenant to give the mortgagee written notice of Landlord's default hereunder and to permit the mortgagee to cure such default within a reasonable time after such notice before exercising any remedy Tenant might possess as a result of such default; and such other matters as may be reasonably required by Landlord or Landlord's mortgagee. Tenant's failure to deliver such statement, in addition to being a default under this Lease, shall be deemed to establish conclusively that this Lease is in full force and effect except as declared by Landlord, that Landlord is not in default of any of its obligations under this Lease, and that Landlord has not received more than one (1) month's Rent in advance.

## **ARTICLE 10. LIENS**

### **10.1 RESERVED.**

## **ARTICLE 11. DEFAULT AND REMEDIES**

**11.1 DEFAULT BY TENANT.** The following shall be deemed to be events of default by Tenant under this Lease: (1) Tenant shall fail to pay when due any installment of Rent or any other payment required pursuant to this Lease; (2) Tenant shall abandon any substantial portion of the Leased Premises; (3) Tenant shall file a petition or be adjudged bankrupt or insolvent under any applicable federal or state bankruptcy or insolvency law or admit that it cannot meet its financial obligations as they become due, or a receiver or trustee shall be appointed for all or substantially all of the assets of Tenant; (4) Tenant shall make a transfer in fraud of creditors or shall make an assignment for the benefit of creditors; (5) Tenant shall do or permit to be done any act which results in a lien being filed against the Leased Premises or the Property; (6) the liquidation, termination, dissolution or (if the Tenant is a natural person) the death of Tenant; or (7) Tenant shall be in default of any other term, provision or covenant of this Lease, other than those specified in subparts (1) through (6) above, and such default is not cured within ten (10) days after written notice thereof to Tenant.

**11.2 REMEDIES FOR TENANT'S DEFAULT.** Upon the occurrence of any event of default set forth in this Lease, which default is not cured within thirty (30) calendar days of Tenant's receipt of Landlord's written notice of default, provided, however, that if such default is, by nature, not susceptible to cure during said thirty (30) calendar day period, then the cure period shall be extended as needed (but not for a period in excess of sixty (60) calendar days from the date of the above-referenced notice of default) to accommodate the efforts of Tenant to effectuate a cure. Thereafter, Landlord shall have the option to pursue any one or more of the remedies set forth in this Section 11.2 (immediately or at any time after such event of default) without additional notice or demand:

(a) Without declaring the Lease terminated, Landlord may enter upon and take possession of the Leased Premises, by picking or changing locks if necessary, and lock out, expel or remove Tenant and any other person who may be occupying all or any part of the Leased Premises without being liable for any claim or damages arising therefrom, and correct or repair any condition which shall constitute a failure on Tenant's part to keep, observe, perform, satisfy or abide by any term, condition, covenant, agreement or obligation of this Lease and Tenant shall fully reimburse and compensate Landlord on demand for the costs incurred by Landlord in doing so.

(b) Without declaring the Lease terminated, Landlord may terminate Tenant's right of possession (but not this Lease) and may repossess the Leased Premises by forcible entry or detainer suit or otherwise, or by picking or changing locks if necessary, without demand or notice of any kind and without being liable for any claim or damages arising therefrom, and remove all persons or property therefrom, using such force as may be necessary (Tenant hereby waiving any claim by reason of such reentry, repossession or removal or by issuance of any distress warrant or writ of sequestration), in which event Landlord may (but shall be under no obligation to do so unless required by law), relet the Leased Premises or any part thereof for the account of Tenant for such rent and upon such terms as shall be satisfactory to Landlord (however, to the extent Landlord is so required by law to relet the Leased Premises, Landlord shall be under no obligation to relet the Leased Premises or any portion thereof in preference to any other space in the Property or on terms unsatisfactory to Landlord). For the purpose of such reletting Landlord is authorized to decorate or to make any repairs, changes, alterations or additions in or to the Leased Premises, or provide leasing inducements or brokerage commissions that may be necessary or convenient, and (i) if Landlord shall fail or refuse to relet the Leased Premises, or (ii) if relet and a sufficient sum shall not be realized from such reletting (after paying the unpaid amounts due hereunder earned but unpaid at the time of reletting plus interest thereon at the Interest Rate, the cost of recovering possession [including, without limitation, attorney's fees and cost of court], all of the costs and expenses of such decorations, repairs, changes, alterations and additions and all other expenses of such reletting [including, without limitation, leasing inducements and brokerage commission] and of the collection of the rent accruing therefrom) to satisfy the Rent provided for in this Lease to be paid, then Tenant shall pay to Landlord as damages a sum equal to the

amount of the Rent reserved in this Lease for such period or periods or, if the Leased Premises have been relet, Tenant shall satisfy and pay any such deficiency upon demand therefor from time to time as the same accrues or becomes due. Tenant agrees that Landlord may file suit to recover any sums falling due under the terms of this Section from time to time on one or more occasions without Landlord being obligated to wait until expiration of the Lease Term, and no delivery or recovery of any portion due Landlord hereunder shall be any defense in any action to recover any amount not theretofore reduced to judgment in favor of Landlord, nor shall such reletting be construed as an election on the part of Landlord to terminate this Lease unless a written notice of such intention be given to Tenant by Landlord. Notwithstanding any such reletting without termination, Landlord may at any time thereafter elect to terminate this Lease for such previous breach. If Landlord re-enters the Leased Premises or terminates this Lease pursuant to any of the provisions of this Lease, Tenant hereby waives all claims for damages which may be caused by such re-entry or termination by Landlord. No such re-entry or termination shall be considered or construed to be a forcible entry.

(c) Landlord may terminate this Lease, in which event Tenant shall immediately surrender the Leased Premises to Landlord, and if Tenant fails to surrender the Leased Premises, Landlord may, without prejudice to any other remedy which it may have for possession or arrearage in Rent, enter upon and take possession of the Leased Premises, by picking or changing locks if necessary, and lock out, expel or remove Tenant and any other person who may be occupying all or any part of the Leased Premises without being liable for any claim for damages. Tenant agrees to pay on demand the amount of all loss and damage which Landlord may suffer for any reason due to the termination of this Lease under this Section, including (without limitation) (i) loss and damage due to the failure of Tenant to maintain and/or repair the Leased Premises as required hereunder, (ii) the cost of recovering the Leased Premises (including, without limitation, attorney's fees and costs of court), (iii) the cost as reasonably estimated by Landlord of any alterations of, or repairs to, the Leased Premises which are necessary or proper to prepare the same for reletting, (iv) the unpaid Rent owed at the time of termination, plus interest thereon from due date at the Interest Rate, (v) the present value of the balance of the Rent for the remainder of the Lease Term less the present value of the fair market rental value (and in computing the fair market value the factors taken into account shall include without limitation the market rental concessions and the time necessary to relet the Leased Premises) of the Leased Premises for said period (in each case using a discount rate of eight percent (8%) per annum), and (vi) any other sum of money and damages owed by Tenant to Landlord.

(d) Interrupt or cause the interruption of any utility service serving the Leased Premises, deactivate Tenant's parking access cards, suspend elevator service to the Leased Premises, remove, alter, or change any door, window, attic hatchway cover to the Leased Premises, or any lock, latch, hinge, hinge pin, doorknob, or other mechanism connected to any door, window, or attic hatchway cover to the Leased Premises, and intentionally prevent Tenant from entering the Leased Premises without resort to judicial process. Landlord is under no obligation to restore any door, window, or attic hatchway cover of any lock, latch, hinge, hinge pin, doorknob, or other mechanism attached thereto.



No repossession of or reentering all or any part of the Leased Premises, and no reletting of the Leased Premises or any part thereof, shall relieve Tenant, all of which shall survive any such repossession, re-entering or reletting by Landlord (except as otherwise expressly set forth in this Lease). If Landlord repossesses or re-enters all or any part of the Leased Premises after an event of default, Tenant shall pay to Landlord all Rent then required to be paid by Tenant. In addition to other remedies provided under this Lease, Landlord is entitled, to the extent permitted by applicable law, to injunctive relief in case of the violation, or attempted or threatened violation, of any of the terms of this Lease, or to a decree compelling specific performance of the terms of this Lease.

Notwithstanding anything in this Lease to the contrary, if Landlord is deemed to have a duty to mitigate its damages arising from a default by Tenant under this Lease, then Landlord's duty to mitigate shall be limited to using reasonable and good faith efforts to relet the Leased Premises, which duty to relet the Leased Premises shall not (i) require Landlord to give priority to the Leased Premises over other premises owned or managed by Landlord or its affiliates, (ii) require Landlord to relet for less than market rent, or (iii) require Landlord to relet to a tenant (or for a use) which is not in keeping with the first-class character of the Property.

Landlord's exercise, following an event of default on behalf of Tenant under this Lease, of any right granted hereunder or under any applicable law to lock or change the locks securing the Leased Premises shall not impose upon Landlord any duty to notify Tenant of the name and address or telephone number of the individual or company from whom a new key may be obtained, nor shall Landlord have any duty to provide Tenant with a new key or any other means of access to the Leased Premises. Landlord and Tenant agree that the parties hereto intend that all rights and remedies of Landlord under this Lease or otherwise available to Landlord under applicable law shall supersede any conflicting provisions of Chapters 91, 92 and 93 of the Texas Property Code, and any amendments, modifications, recodification or other changes thereto.

Notwithstanding any other remedy set forth in this Lease, if Landlord has made Rent concessions of any type or character, or waived any Base Rent, and Tenant fails to take possession of the Leased Premises on the Commencement Date or otherwise defaults at any time during the Lease Term, the rent concessions, including any waived Base Rent, shall be canceled and the amount of the Base Rent or other rent concessions shall be due and payable immediately as if no rent concessions or waiver of any Base Rent had ever been granted. A rent concession or waiver of the Base Rent shall not relieve Tenant of any obligation to pay any other charge due and payable under this Lease, including, without limitation, any sum due under Section 2.3 of this Lease. Notwithstanding anything contained in this Lease to the contrary, this Lease may be terminated by Landlord only by written notice of such termination to Tenant given in accordance with Section 13.7 below, and no other act or omission of Landlord shall be construed as a termination of this Lease.

**11.3 REMEDIES CUMULATIVE.** All rights and remedies of Landlord herein or existing at law or in equity are cumulative, and the exercise of one or more rights or remedies shall not be taken to exclude or waive the right to the exercise of any other.

**11.4 DEFAULT BY LANDLORD.** If Landlord defaults in the performance of any term, covenant or condition required to be performed by Landlord under this Lease, Landlord shall have thirty (30) days following the receipt of written notice from Tenant specifying such default to cure such default, provided that if Landlord has commenced actions to cure such default within said thirty (30) day period, then the cure period shall be extended as needed (but not for a period in excess of sixty (60) days from the date of the above-referenced notice of default) to accommodate the efforts of Landlord to effectuate a cure.

**11.5 REMEDIES FOR LANDLORD'S DEFAULT.** Upon the occurrence of any default on behalf of Landlord under this Lease and subsequent failure by Landlord to cure or commence actions to cure as provided in Section 11.4, Tenant shall, as Tenant's sole remedy, have the right to maintain an action against Landlord, for actual damages suffered as a result of Landlord's default.

**11.6 NOTICE TO MORTGAGEES.** Provided that Tenant has received prior written notice of the name and address of such lender, Tenant shall serve written notice of any claimed default or breach by Landlord under this Lease upon any lender which is a beneficiary under any deed of trust or mortgage against the Leased Premises, and no notice to Landlord shall be effective against Landlord unless such notice is served upon said lender. Notwithstanding anything to the contrary contained herein, Tenant shall allow such lender the same period following lender's receipt of such notice to cure such default or breach as is afforded Landlord, plus such longer period of time as may be reasonably necessary under the circumstances (but in no event less than thirty (30) days) for such lender to cure such default or breach.

**11.7 WAIVER BY TENANT.** Tenant waives and surrenders for itself and all persons or entities claiming by, through, and under it, including creditors of all kinds: (i) any right and privilege which it or any of them has under any present or future constitution, statute, or rule of law to redeem the Leased Premises or to have a continuance of this Lease for the Lease Term after termination of Tenant's right of occupancy by order or judgment of any court, or by any legal process or writ, or under the terms of this Lease; (ii) the benefits of any present or future constitution, statute, or rule of law that exempts property from liability for debt or for distress for rent; (iii) any provision of law relating to notice or delay in levy of execution in case of eviction of a tenant for nonpayment of rent; (iv) any rights, privileges, and liens set out under Sections 91.004 and 93.003 of the Texas Property Code (as amended), and Tenant exempts Landlord from any liability or duty thereunder; and (v) any rights of Tenant to contest reappraisals of the Property (but not ad valorem taxes on Tenant's personal property in the Leased Premises) under Sections 41.143 and 42.015 of the Texas Tax Code (as amended).

## ARTICLE 12. RELOCATION

### 12.1 RESERVED.

## ARTICLE 13. MISCELLANEOUS

**13.1 WAIVER.** Failure of Landlord to declare an event of default immediately upon its occurrence, or delay in taking any action in connection with an event of default, shall not constitute a waiver of the default, but Landlord shall have the right to declare the default at any

time and take such action as is lawful or authorized under this Lease. Pursuit of any one or more of the remedies set forth in Article 11 above shall not preclude pursuit of any one or more of the other remedies provided elsewhere in this Lease or provided by law, nor shall pursuit of any remedy hereunder or at law constitute forfeiture or waiver of any Rent or damages accruing to Landlord by reason of the violation of any of the terms, provisions or covenants of this Lease. Failure by Landlord to enforce one or more of the remedies provided hereunder or at law upon any event of default shall not be deemed or construed to constitute a waiver of the default or of any other violation or breach of any of the terms, provisions and covenants contained in this Lease. Landlord may collect and receive Rent due from Tenant without waiving or affecting any rights or remedies that Landlord may have at law or in equity or by virtue of this Lease at the time of such payment. Institution of a forcible detainer action to re-enter the Leased Premises shall not be construed to be an election by Landlord to terminate this Lease.

**13.2 ACT OF GOD.** Landlord shall not be required to perform any covenant or obligation in this Lease, or be liable in damages to Tenant, so long as the performance or non-performance of the covenant or obligation is delayed, caused or prevented by an Act of God, Force Majeure or by Tenant. For the purposes of this Lease, an “Act of God” or “Force Majeure” shall mean strikes, lockouts, sitdowns, material or labor restrictions by any governmental authority, unusual transportation delays, riots, floods, washouts, explosions, earthquakes, fire, storms, weather (including wet grounds or inclement weather which prevents construction), acts of the public enemy, wars, insurrections, and/or any other cause not reasonably within the control of Landlord or which by the exercise of due diligence Landlord is unable wholly or in part to prevent or overcome.

**13.3 ATTORNEY’S FEES.** If any party defaults in the performance of any terms, covenants, agreements or conditions contained in this Lease and the other party places in the hands of any attorney the enforcement of all or any part of this Lease, then the party which does not prevail agrees to pay the reasonable fees and costs of the prevailing party’s attorneys, whether suit is actually filed or not.

**13.4 SUCCESSORS.** This Lease shall be binding upon and inure to the benefit of Landlord and Tenant and their respective heirs, successors and assigns.

**13.5 RENT TAX.** If applicable in the jurisdiction where the Leased Premises are situated, Tenant shall pay and be liable for all rental, sales and use taxes or other similar taxes, if any, levied or imposed by any city, state, county or other governmental body having authority, such payments to be in addition to all other payments required to be paid to Landlord by Tenant under the terms of this Lease; provided, however, nothing in this Section 13.5 shall require Tenant to pay any of Landlord’s income taxes. Any such payment shall be paid concurrently with the payment of the Rent, operating expenses or other charge(s) upon which the tax is based as set forth above.

**13.6 INTERPRETATION.** The captions appearing in this Lease are for convenience only and in no way define, limit, construe or describe the scope or intent of any Section. Grammatical changes required to make the provisions of this Lease apply (i) in the plural sense where there is more than one tenant and (ii) to either corporations, associations, partnerships or

individuals, males or females, shall in all instances be assumed as though in each case fully expressed. The laws of the State of Texas shall govern the validity, performance and enforcement of this Lease. This Lease shall not be construed more or less favorably with respect to either party as a consequence of the Lease or various provisions hereof having been drafted by one of the parties hereto.

**13.7 NOTICES.** All payments required to be made by Landlord to Tenant shall be payable to Tenant at Tenant's address set forth in Section 1.9 of this Lease. Any notice or document (other than Rent) required or permitted to be delivered by the terms of this Lease shall be deemed to be delivered upon the earlier to occur of (i) actual receipt or (ii) whether or not actually received, three (3) days after deposit in the United States Mail, postage prepaid, certified mail, return receipt requested or (iii) one (1) day after deposit with a nationally recognized overnight delivery service (e.g. FedEx), addressed to the applicable party at the applicable address set forth in Section 1.9 of this Lease (or, in the case of Tenant, at the Leased Premises), or to such other addresses as the parties may have designated by written notice to each other, with copies of notices to Landlord being sent to Landlord's address as shown in Section 1.9 of this Lease. Manager shall be a co-addressee with Landlord on all notices sent to Landlord by Tenant hereunder, and any notice sent to Landlord and not to Manager also, in accordance with this Section, shall be deemed ineffective at the option of Landlord.

**13.8 SUBMISSION OF LEASE.** Submission of this Lease to Tenant for signature does not constitute a reservation of space or an option to lease. This Lease is not effective until execution by and delivery to both Landlord and Tenant.

**13.9 CORPORATE AUTHORITY.** If Tenant executes this Lease as a corporation or a partnership (general or limited), each person executing this Lease on behalf of Tenant hereby personally represents and warrants that: Tenant is a duly authorized and existing corporation or partnership (general or limited); Tenant is qualified to do business in the state in which the Leased Premises are located; the corporation or partnership (general or limited) has full right and authority to enter into this Lease; each person signing on behalf of the corporation or partnership (general or limited) is authorized to do so; and the execution and delivery of the Lease by Tenant will not result in any breach of, or constitute a default under, any mortgage, deed of trust, lease, loan, credit agreement, partnership agreement, or other contract or instrument to which Tenant is a party or by which Tenant may be bound. If any representation or warranty contained in this Section is false, each person who executes this Lease shall be liable individually as Tenant hereunder.

**13.10 MULTIPLE TENANTS.** If this Lease is executed by more than one person or entity as "Tenant," each such person or entity shall be jointly and severally liable hereunder. It is expressly understood that any one of the named Tenants shall be empowered to execute any modification, amendment, exhibit, floor plan, or other document herein referred to and bind all of the named Tenants thereto; and Landlord shall be entitled to rely on same to the same extent as if all of the named Tenants had executed same.

### **13.11 TENANT'S FINANCIAL STATEMENTS.**

(a) Tenant represents and warrants to Landlord that, as of the date of execution of this Lease by Tenant, the financial statements of Tenant provided to Landlord prior to or simultaneously with the execution of this Lease accurately represent the financial condition of Tenant as of the dates and for the periods indicated therein, such financial statements are true and do not contain any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements included therein not misleading, and there has been no material adverse change in the financial condition or business prospects of Tenant since the respective dates of such financial statements. If there is a material adverse change in Tenant's financial condition, Tenant will give immediate notice of such material adverse change to Landlord. If Tenant fails to give such immediate notice to Landlord, such failure shall be deemed an event of default under this Lease.

(b) If Landlord intends to sell all or any portion of the Building or the Property (or any interest therein), or obtain a loan secured by the Building or the Property (or any interest therein), then Tenant shall, within fifteen (15) days of Landlord's written request (but not more frequently than three (3) times in any calendar year), furnish Landlord with financial statements, dated no earlier than one (1) year before such request, certified as accurate by Tenant, or, if available, audited financial statements prepared by an independent certified public accountant with copies of the auditor's statement, reflecting Tenant's then current financial condition, or the financial condition of the individuals compromising Tenant, in such form and detail as Landlord may reasonably request.

**13.12 SEVERABILITY.** If any provision of this Lease or the application thereof to any person or circumstances shall be invalid or unenforceable to any extent, the remainder of this Lease and the application of such provisions to other persons or circumstances shall not be affected thereby and shall be enforced to the greatest extent permitted by law. Each covenant and agreement contained in this Lease shall be construed to be a separate and independent covenant and agreement, and any default or breach of the terms of this Lease by Landlord shall not discharge or relieve Tenant from Tenant's obligation to perform each and every covenant and agreement of this Lease to be performed by Tenant.

**13.13 LANDLORD'S LIABILITY.** If Landlord shall be in default under this Lease and, if as a consequence of such default, Tenant shall recover a money judgment against Landlord, such judgment shall be satisfied only out of the right, title and interest of Landlord in the Property as the same may then be encumbered and neither Landlord nor any person or entity comprising Landlord shall be liable for any deficiency. In no event shall Tenant have the right to levy execution against any property of Landlord nor any person or entity comprising Landlord other than its interest in the Property as herein expressly provided.

**13.14 SALE OF PROPERTY.** Upon any conveyance, sale or exchange of the Leased Premises or assignment of this Lease, Landlord shall be and is hereby entirely free and relieved of all liability under any and all of its covenants and obligations contained in or derived from this Lease arising out of any act, occurrence, or omission relating to the Leased Premises or this Lease occurring after the consummation of such sale or exchange and assignment.

**13.15 TIME IS OF THE ESSENCE.** The time of the performance of all of the covenants, conditions and agreements of this Lease is of the essence.

**13.16 SUBTENANCIES.** At Landlord's option the voluntary or other surrender of this Lease by Tenant, or a mutual cancellation thereof, shall not work a merger of estates and shall operate as an assignment of any or all permitted subleases or subtenancies.

**13.17 BROKERAGE; MUTUAL INDEMNITIES.**

(a) Tenant warrants that it has had no dealings with any broker or agent in connection with the negotiation or execution of this Lease other than R.M. Crowe Leasing, LLC ("**Broker**"). Tenant shall indemnify, defend, and hold Landlord harmless against all costs, expenses, attorneys' fees, or other liability for commission or other compensation or charges claimed by any broker or agent other than Broker claiming by, through, or under Tenant with respect to this Lease or any renewal or extension of the same or with respect to any expansion of the Leased Premises.

(b) Landlord warrants that it has had no dealings with any broker or agent in connection with the negotiations or execution of this Lease other than Broker. Landlord shall indemnify, defend, and hold Tenant harmless against all costs, expenses, attorneys' fees, or other liability for commissions or other compensation or charges claimed by any broker or agent, including Broker, claiming by, through or under Landlord with respect to this Lease or any renewal or extension of the same or with respect to any expansion of the Leased Premises.

(c) Any brokerage commission payable to Broker is payable by Landlord pursuant to the terms of separate agreements between Landlord and Broker.

**13.18 WAIVER OF TRIAL RIGHTS.** Landlord and Tenant hereby waive trial by jury (i) in any action, proceeding or counterclaim brought by Landlord or Tenant against the other, (ii) in any matter whatsoever arising out of or in any way connected with this Lease, the relationship of Landlord to Tenant, the use or occupancy of the Leased Premises by Tenant or any person claiming through or under Tenant, and (iii) with respect to any claim of injury or damage and/or any emergency or other statutory remedy; provided, however, the foregoing waiver shall not apply to any action for personal injury or property damage. If Landlord commences any summary or other proceeding for nonpayment of Rent or the recovery of possession of the Leased Premises, Tenant shall not interpose any counterclaim of whatever nature or description in any such proceeding, unless the failure to raise the same would constitute a waiver thereof.

**ARTICLE 14. AMENDMENT AND LIMITATION OF WARRANTIES**

**14.1 ENTIRE AGREEMENT.** IT IS EXPRESSLY AGREED BY TENANT, AS A MATERIAL CONSIDERATION FOR THE EXECUTION OF THIS LEASE, THAT THIS

LEASE, WITH THE SPECIFIC REFERENCES TO EXTRINSIC DOCUMENTS, IS THE ENTIRE AGREEMENT OF LANDLORD AND TENANT; THAT THERE ARE, AND WERE, NO VERBAL REPRESENTATIONS, WARRANTIES, UNDERSTANDINGS, STIPULATIONS, AGREEMENTS OR PROMISES PERTAINING TO THE SUBJECT MATTER OF THIS LEASE OR OF ANY EXPRESSLY MENTIONED EXTRINSIC DOCUMENTS THAT ARE NOT INCORPORATED IN WRITING IN THIS LEASE.

**14.2 AMENDMENT.** THIS LEASE MAY NOT BE ALTERED, WAIVED, AMENDED, OR EXTENDED EXCEPT BY AN INSTRUMENT OF A DATE SUBSEQUENT HERETO IN WRITING SIGNED BY LANDLORD AND TENANT.

**14.3 LIMITATION OF WARRANTIES.** LANDLORD AND TENANT EXPRESSLY AGREE THAT THERE ARE AND SHALL BE NO IMPLIED WARRANTIES OF MERCHANTABILITY, HABITABILITY, SUITABILITY, FITNESS FOR A PARTICULAR PURPOSE OR OF ANY OTHER KIND ARISING OUT OF THIS LEASE, AND THERE ARE NO WARRANTIES WHICH EXTEND BEYOND THOSE EXPRESSLY SET FORTH IN THIS LEASE. WITHOUT LIMITING THE GENERALITY OF THE FOREGOING, TENANT EXPRESSLY ACKNOWLEDGES THAT LANDLORD HAS MADE NO WARRANTIES OR REPRESENTATIONS CONCERNING ANY HAZARDOUS MATERIALS OR OTHER ENVIRONMENTAL MATTERS AFFECTING ANY PART OF THE PROPERTY, AND LANDLORD HEREBY EXPRESSLY DISCLAIMS AND TENANT WAIVES ANY EXPRESS OR IMPLIED WARRANTIES WITH RESPECT TO ANY SUCH MATTERS.

**14.4 WAIVER AND RELEASES.** TENANT SHALL NOT HAVE THE RIGHT TO WITHHOLD OR TO OFFSET RENT OR TERMINATE THIS LEASE EXCEPT AS EXPRESSLY PROVIDED HEREIN. TENANT WAIVES AND RELEASES ANY AND ALL STATUTORY LIENS AND OFFSET RIGHTS.

**14.5 NON-DISCLOSURE OF LEASE TERMS.** EXCEPT IF OTHERWISE REQUIRED BY LAW, TENANT SHALL NOT DISCLOSE ANY MATERIAL TERMS OR PROVISIONS OF THIS LEASE. IF TENANT DISCLOSES ANY OF THE MATERIAL TERMS AND/OR PROVISIONS OF THIS LEASE, EXCEPT AS MAY BE REQUIRED BY LAW, INCLUDING BUT NOT LIMITED TO THE BASE RENT, THE PERCENTAGE RENT, TENANT'S COMMON AREA COSTS AND/OR OPERATING EXPENSES OR ANY CAPS ON SUCH COSTS OR EXPENSES, MERCHANT ASSOCIATION FEES, TENANT FINISH ALLOWANCE, TENANT'S PROPORTIONATE SHARE OF GENERAL TAXES OR ANY CAP ON SUCH EXPENSE, TENANT'S PROPORTIONATE SHARE OF INSURANCE PREMIUMS OR ANY CAP ON SUCH EXPENSE, OR THE LEASE TERM TO ANY PERSON OR ENTITY NOT A PARTY TO THIS LEASE EXCEPT TENANT'S ATTORNEY, THEN TENANT SHALL BE LIABLE FOR ALL DAMAGES OR INJURY TO LANDLORD RESULTING FROM TENANT'S FAILURE TO KEEP SUCH INFORMATION CONFIDENTIAL AND TENANT SHALL INDEMNIFY AND HOLD LANDLORD HARMLESS FROM ANY DAMAGE, LOSS OR INJURY OCCASIONED THEREBY. IN THE ALTERNATIVE, AND AT LANDLORD'S SOLE OPTION, IF DAMAGES ARE DIFFICULT TO CALCULATE, TENANT SHALL PAY LIQUIDATED DAMAGES EQUAL TO ONE (1) MONTH'S BASE RENT AS DEFINED IN ARTICLE 1 HEREOF.

**14.6 SECURITY DISCLAIMER.** ANY SECURITY MEASURES PROVIDED BY LANDLORD MAY NOT BE TREATED BY TENANT AS A GUARANTEE AGAINST CRIME. LANDLORD DOES NOT MAKE, AND TENANT WAIVES, ANY GUARANTY OR WARRANTY, EXPRESSED OR IMPLIED, WITH RESPECT TO SECURITY AT THE PROPERTY OR IN THE BUILDING, OR THAT ANY SECURITY MEASURES WILL PREVENT OCCURRENCES OR CONSEQUENCES FOR CRIMINAL ACTIVITY. ANY MECHANICAL SECURITY DEVICES CAN BE RENDERED INOPERATIVE ANY TIME. LANDLORD IS NOT RESPONSIBLE FOR A TEMPORARY FAILURE OF SUCH DEVICES. IF SUCH DEVICES ARE IN NEED OF REPAIR, TENANT WAIVES ALL WARRANTIES, EXPRESS OR IMPLIED, WITH RESPECT TO LANDLORD'S REPAIR OF SUCH DEVICES. LANDLORD'S INSTALLATION OR USE OF ANY SECURITY MEASURE DOES NOT CONSTITUTE A VOLUNTARY UNDERTAKING OR AGREEMENT BY LANDLORD TO PROVIDE SECURITY TO TENANT OR ANY TENANT-RELATED PARTY OR ANY PROPERTY OF THE SAME. LANDLORD MAY MODIFY, REDUCE OR ELIMINATE THE USE OF ANY SECURITY MEASURE AT ANY TIME WITHOUT NOTICE TO TENANT. NEITHER LANDLORD NOR ITS AGENTS, EMPLOYEES OR REPRESENTATIVES ARE LIABLE IN ANY WAY FOR ANY DISRUPTION IN THE OPERATION OR PERFORMANCE OF ANY SECURITY MEASURE. LANDLORD DOES NOT MAKE, AND TENANT WAIVES, ANY GUARANTY OR WARRANTY THAT THE PRESENCE OF ANY SECURITY MEASURE AT THE PROPERTY OR IN THE BUILDING IN ANY WAY INCREASES THE PERSONAL SECURITY OF TENANT OR ANY TENANT-RELATED PARTY OR ANY PROPERTY OF THE SAME. LANDLORD IS NOT LIABLE TO TENANT OR ANY TENANT-RELATED PARTY FOR ANY INJURY, DAMAGE OR LOSS WHATSOEVER WHICH IS CAUSED (I) AS A RESULT OF ANY PROBLEM, DEFECT, MALFUNCTION OR FAILURE OF THE PERFORMANCE OF ANY SECURITY MEASURE OR (II) BY ANY PERSON ENGAGED IN ANY CRIMINAL ACTIVITY.

*[The signature page follows immediately hereafter.]*



**LANDLORD:**

**RMC MIDWAY WALNUT, LP**

a Texas limited partnership

By: RMC Midway Walnut GP, LLC  
its general partner

By: /s/ Maurice Crowe \_\_\_\_\_  
R. Maurice Crowe, Jr.  
Manager

**TENANT:**

**PC CONNECTION SALES OF MASSACHUSETTS, INC.**

a Delaware corporation

By: /s/ Timothy J. McGrath \_\_\_\_\_  
Name: Timothy McGrath  
Title: President

**List of Exhibits:**

- Exhibit "A" – Site Plan
- Exhibit "A-1" – Additional Space
- Exhibit "B" – Parking
- Exhibit "C" – Intentionally Deleted
- Exhibit "D" – Rules and Regulations
- Exhibit "E" – Landlord Work Letter
- Rider "1" – Option to Extend (Two-Time)
- Rider "2" – Tenant's Preferential Right to Lease
- Rider "3" – Termination Option

---

**EXHIBIT "A"**  
**TO OFFICE LEASE**  
**SITE PLAN**  
[See Attached]

---

**EXHIBIT "A-1"**  
**TO OFFICE LEASE**  
**ADDITIONAL SPACE**

[See Attached]

**EXHIBIT "B"**  
**TO OFFICE LEASE**  
**PARKING**

**TENANT:**

1. Throughout the Lease Term, subject to availability, Tenant shall be able to lease from Landlord parking spaces in the parking facilities related to the Property. All such parking spaces shall be leased by Tenant on an unassigned basis except as provided below, and shall be used in common with the other tenants. Landlord shall have the right to reserve parking spaces in the parking facilities as it elects, and to condition the use thereof on such terms as it elects.
2. Throughout the Lease Term, to the extent that the same may be required pursuant to the terms and provisions of paragraph 3 below, Tenant shall pay to Landlord as monthly rent (the "Parking Rent") for parking spaces an amount equal to the product of (i) the then current monthly rate for parking in the parking facilities (as established by Landlord from time to time) times (ii) the number of parking spaces used by Tenant. All Parking Rent shall be paid by Tenant to Landlord in advance without demand on the first day of each month, with partial months prorated as applicable, commencing with the Commencement Date.
3. Tenant shall have the right to use (i) forty-three (43) unreserved surface parking spaces at the rate of Zero and No/100 Dollars (\$0.00) per space per month (plus applicable sales tax) and (ii) zero (0) designated reserved parking spaces at the rate of Zero and No/100 Dollars (\$0.00) per space per month (plus applicable sales tax). Such amounts shall be deemed Parking Rent as set forth in paragraph 2 above, payable as provided therein.
4. Lost parking access cards or parking permits will be replaced on request with a charge of Fifteen and No/100 Dollars (\$15.00) per card/permit.
5. Tenant shall cooperate fully in Landlord's efforts to maintain the designated use of the various parking facilities and parking areas, and shall follow all traffic, security, safety, and other rules and regulations issued by the Landlord with respect thereto.
6. Landlord shall have the right to: make a reasonable charge for public parking, control access to the parking facilities, add below grade parking, parking decks, change curb cuts, change traffic patterns, re-stripe the parking facilities and parking surfaces as to size and location of spaces, temporarily displace vehicles (for the purpose of improving and expanding parking facilities and with appropriate rebate of Parking Rent), abandon any parking areas and add or delete acceleration/deceleration lanes on adjacent roads and alleys.
7. Prior to issuance of the parking access cards or parking permits, Tenant must deliver to Landlord a list of the automobile license numbers of Tenant's employees who will be

using the cards or parking permits, together with Landlord's then current per card/permit deposit. This deposit is forfeited to Landlord if any card or parking permit, is lost or damaged or not returned to Landlord on request and a new deposit must be delivered to Landlord before a replacement card or parking permit is issued to Tenant.

8. Tenant is not assigned designated unreserved parking spaces, but is permitted to use whatever unreserved stalls are available, on a first-come, first-served basis in areas designated for tenant parking from time to time by Landlord. If for any reason Landlord fails or is unable to provide parking spaces to Tenant, this failure or inability is not a default by Landlord under this Lease.
9. During any renewal or extension of the Lease Term or during any holdover after the termination of this Lease, Landlord reserves the right to charge Tenant the Parking Rent (plus any applicable sales tax) then imposed by Landlord for parking in the parking facilities related to the Property.

---

**EXHIBIT "C"**  
**TO OFFICE LEASE**  
Intentionally Deleted

**EXHIBIT "D"**

**TO OFFICE LEASE**

**RULES AND REGULATIONS**

1. Landlord agrees to furnish Tenant with two (2) keys (of every sort that Tenant may require to access the Leased Premises and the Common Areas) without charge. Additional keys will be furnished at a nominal charge. Tenant shall not change locks or install additional locks on doors without prior written consent of Landlord. Tenant shall not make or cause to be made duplicates of keys procured from Landlord without prior written approval of Landlord. All keys to the Leased Premises shall be surrendered to Landlord upon termination of the Lease.
2. Tenant will refer all contractors, contractor's representatives and installation technicians rendering any service on or to the Leased Premises for Tenant to Landlord for Landlord's approval before performance of any such contractual service. Tenant's contractors, contractor's representatives and installation technicians shall comply with Landlord's rules and regulations pertaining to construction and installation, including without limitation, providing Landlord with a certificates of insurance that meet Landlord's requirements. This provision shall apply to all work performed on or about the Property and/or the Leased Premises, including installation of telephones, telegraph equipment, electrical devices and attachments and installations of any nature affecting floors, walls, woodwork, trim, windows, ceilings and equipment or any other physical portion of the Leased Premises or the Property.
3. Tenant shall not at any time occupy any part of the Leased Premises as sleeping or lodging quarters.
4. Tenant shall not place, install or operate on the Leased Premises or in any part of the Property any electrical floor heater, engine, stove or machinery, or conduct mechanical operations or cook thereon or therein, or place or use in or about the Leased Premises or the Property any explosives, gasoline, kerosene, oil, acids, caustics, or any flammable, explosive or hazardous material without written consent of Landlord.
5. Landlord will not be responsible for lost or stolen merchandise, trade fixtures, furniture, furnishings, personal property, equipment, money or jewelry from the Leased Premises or the Property regardless of whether such loss occurs when the area is locked against entry.
6. No dogs, cats, fowl or other animals shall be brought into or kept in or about the Leased Premises or the Property.
7. Employees of Landlord shall not receive or carry messages for or to any Tenant or other person, nor shall they contract with or render free or paid services to Tenant or to any of Tenant's agents, employees or invitees.

8. None of the parking, plaza or recreational lawn areas, entries, passages, doors, elevators, hallways or stairways shall be blocked or obstructed or any rubbish, litter, trash or material of any nature placed, emptied or thrown into these areas or such area used by Tenant's agents, employees or invitees at any time for purposes inconsistent with their designation by Landlord.
9. The water closets and other water fixtures shall not be used for any purpose other than those for which they were constructed, and any damage resulting to them from misuse and any damage, defacing or injury to any other part of the Property shall be the responsibility of (with related costs to be borne by) the person who shall occasion it. No person shall waste water by interfering with the faucets or otherwise.
10. No person shall disturb occupants of the Property by the use of any radios, record players, tape recorders, musical instruments, the making of unseemly noises or any unreasonable use.
11. Nothing shall be thrown out of the windows of the Property or down the stairways or other passages.
12. Tenant and its employees, agents and invitees shall park their vehicles only in those parking areas designated by Landlord. Tenant shall furnish Landlord with state automobile license numbers of Tenant's vehicles and its employees' vehicles within five (5) days after taking possession of the Leased Premises and shall notify Landlord of any changes within five (5) days after such change occurs. Tenant shall not leave any vehicle in a state of disrepair (including without limitation, flat tires, out of date inspection stickers or licenses plates) on the Leased Premises or on the Property. If Tenant or its employees, agents or invitees park their vehicles in areas other than the designated parking areas or leave any vehicle in a state of disrepair, Landlord, after giving written notice to Tenant of such violation, shall have the right (but not the obligation) to remove such vehicles at Tenant's expense.
13. Parking in the parking facilities related to the Property shall be in compliance with all parking rules and regulations including any sticker or other identification system established by Landlord. Failure to observe the rules and regulations shall terminate Tenant's right to use such parking facilities and subject the vehicle in violation of the parking rules and regulations to removal and impoundment. No termination of parking privileges or removal or impoundment of a vehicle shall create any liability on Landlord or be deemed to interfere with Tenant's right to possession of the Leased Premises. Vehicles must be parked entirely within the stall lines and all direction signs, arrows and posted speed limits must be observed. Parking is prohibited in areas not striped for parking, in areas marked as "Customer" or "Visitor" Parking, in aisles, where "No Parking" signs are posted, on ramps, in cross hatched areas, and in other areas as may be designated by Landlord. Parking stickers or other forms of identification supplied by Landlord shall remain the property of Landlord and shall not become the property of Tenant and are not transferable. Every person is required to park and lock his or her own vehicle. All responsibility for damage to vehicles or persons is assumed by the owner of the vehicle and its driver.



14. Movement in or out of the Property of furniture, office supplies and equipment, or dispatch or receipt by Tenant of any merchandise or materials which requires use of elevators or stairways, or movement through the Property entrances or lobby shall be restricted to hours designated by Landlord. All such movement shall be under supervision of Landlord and carried out in the manner agreed between Tenant and Landlord by prearrangement before performance. Such prearrangement will include determination by Landlord of time, method, and routing of movement and limitations imposed by safety or other concerns which may prohibit any article, equipment or any other item from being brought in to the Property. Tenant assumes, and shall indemnify Landlord against, all risks and claims of damage to persons and properties arising in connection with any said movement.
15. Landlord shall not be liable for any damages from the stoppage of elevators for necessary or desirable repairs or improvements or delays of any sort or duration in connection with elevator service.
16. Tenant shall not lay floor covering within the Leased Premises without written approval of Landlord. The use of cement or other similar adhesive materials not easily removed with water is expressly prohibited.
17. Tenant agrees to cooperate and assist Landlord in the prevention of canvassing, soliciting and peddling at the Property. Tenant shall not, without the prior written consent of Landlord, place any signs or other advertising materials (i) in any of the Common Areas or (ii) in any portion of the Leased Premises visible from any of the Common Areas.
18. During all hours other than Building Standard Hours, Landlord reserves the right to exclude from the Property, all persons who are not known to the Property security personnel and who do not present a pass to the Property signed by Tenant. Each Tenant shall be responsible for all persons to whom Tenant supplies a pass.
19. If any governmental license or permit shall be required for the proper and lawful conduct of Tenant's business, Tenant, before occupying the Leased Premises shall procure and maintain such license or permit and submit it to Landlord for inspection. Tenant shall at all times comply with all terms of any such license or permit.
20. Except with the prior written consent of Landlord, Tenant (i) shall not sell or permit the sale from the Leased Premises of, or (ii) use or permit the use of any sidewalk or mail area adjacent to the Leased Premises for, the sale of newspapers, magazines, periodicals, theater tickets or any other goods or merchandise. Furthermore, Tenant shall not carry on, or permit or allow any employee or other person to carry on, business in or from the Leased Premises for the service or accommodation of occupants of any other portion of the Building, nor shall the Leased Premises be used for manufacturing of any kind, or for any business or activity other than that specifically provided for in the Lease.

21. Tenant shall not install any radio or television antenna, loudspeaker or other device on the exterior walls of the Building.
22. Tenant shall not use in any space, or in the Common Areas, any hand trucks except those equipped with rubber tires and side guards or such other material handling equipment as Landlord may approve. No other vehicles of any kind shall be brought by Tenant into the Building or kept in or about the Leased Premises without prior written approval of Landlord.
23. Tenant shall store all its trash and garbage within the Leased Premises until removal of same by janitorial service to such location on the Property as may be designated from time to time by Landlord. No material shall be placed in the Building trash boxes or receptacles if such material is of such nature that it may not be disposed of in the ordinary and customary manner of removing and disposing of trash and garbage in the city in which the Leased Premises is located without being in violation of any applicable Legal Requirements.
24. Tenant shall not permit the use or the operation of any coin operated machines on the Leased Premises, including without limitation, vending machines, video games, pinball machines, or pay telephones without the prior written consent of Landlord.
25. As used in the Lease, "business days" means Monday through Saturday (except holidays); "Building Standard Hours" means 7:00 a.m. to 6:00 p.m. on weekdays and 8:00 a.m. to 1:00 p.m. on Saturdays; and "holidays" means New Years Day, Memorial Day, Fourth of July, Labor Day, Thanksgiving Day and Christmas Day, together with such other holidays as are designated by Landlord consistent with those holidays designated by landlords of comparable office buildings located in the county in which the Building is located.
26. Landlord desires to maintain the Property in the highest standard of dignity and good taste consistent with comfort and convenience for Tenants. Any action or condition not meeting this high standard should be reported directly to Landlord. Your cooperation will be mutually beneficial and sincerely appreciated. Landlord reserves the right to make such other and further reasonable rules and regulations as in its judgment may from time to time be necessary, for the safety, care and cleanliness of the Leased Premises and the Property and for the preservation of good order therein.
27. Tenant acknowledges and agrees that the Property is a non-smoking facility and that smoking is prohibited in the Property including the Leased Premises, restrooms, stairwells, hallways and other portions of the Common Areas. Tenant shall cause its employees, agents, contractors, visitors and invitees to comply with this and all other Rules and Regulations.

In the event of any conflict between the terms and provisions of these Rules and Regulations and any terms and provisions of the Lease, the terms and provisions of the Lease shall control.

**EXHIBIT "E"**  
**TO OFFICE LEASE**  
**LANDLORD WORK LETTER**

1. Construction.

(a) Landlord agrees to construct certain leasehold improvements (the "Finish Work") in a good and workmanlike manner in and upon the Leased Premises in accordance with construction drawings approved by both Landlord and Tenant ("Final Working Drawings"). Subject to the other applicable terms and conditions of this Exhibit and of the Lease, Landlord shall be responsible for all Costs of Construction (defined below) up to an aggregate amount (the "Finish Allowance") equal to Fourteen and No/100 Dollars (\$14.00) per rentable square foot in the Leased Premises. The Finish Allowance shall be used solely for the purpose of completing the Finish Work in the Leased Premises. Notwithstanding the foregoing, to the extent that there is any unused portion of the Finish Allowance remaining (the "Remaining Allowance") after completion of all Finish Work agreed to by and between Landlord and Tenant as set forth above, then up to an aggregate amount equal to Two and No/100 Dollars (\$2.00) per rentable square foot in the Leased Premises of the Remaining Allowance shall be credited to Tenant evenly over the first (1<sup>st</sup>) twelve (12) calendar months of the Lease Term against Base Rent owing monthly under the Lease. Notwithstanding anything to the contrary contained herein, in no event shall Landlord be obligated under this subparagraph (a) for any amount in excess of the Finish Allowance. Additionally, Landlord shall be permitted to offset against the Finish Allowance any amounts past due to Landlord by Tenant under the Lease.

(b) Landlord will employ a qualified, licensed contractor to construct the Finish Work and will require in any construction contract that such contractor construct the Finish Work in a good and workmanlike manner and in compliance with all Legal Requirements; provided, however, Tenant will be solely responsible for determining whether or not Tenant is a public accommodation under The Americans with Disabilities Act and whether or not the Final Working Drawings comply with such law and the regulations thereunder. The parties acknowledge that (i) Landlord is not an architect or engineer, and that the Finish Work will be designed and performed by independent architects, engineers and contractors ("Third Parties"), and (ii) Landlord does not guarantee or warrant that the plans or Final Working Drawings will be free from errors or omission, or that the Finish Work will be free from defects (provided, however, that Landlord agrees to use reasonable efforts to cooperate in any action Tenant desires to bring against applicable Third Parties).

2. Costs.

(a) Tenant shall be obligated to pay to Landlord the amount by which the Costs of Construction exceed the Finish Allowance (the "Tenant Amounts") as follows: (i) fifty

percent (50%) of the Tenant Amounts shall be payable at such time, and from time to time, as the Costs of Construction are determined by Landlord to be in excess of the Finish Allowance, and (ii) the remaining actual Tenant Amounts shall be payable to Landlord at such time as the applicable Tenant Amounts are payable by Landlord (and Tenant shall make such payments in clauses (i) and (ii) immediately above to Landlord within ten (10) days after Landlord provides Tenant with an invoice therefor). Notwithstanding the foregoing, costs arising out of change orders requested by Tenant and approved by Landlord after construction has commenced and which increase the Costs of Construction shall be paid by Tenant to Landlord within five (5) days of receipt of an invoice therefor from Landlord.

(b) All installations and improvements now or hereafter placed in the Leased Premises other than building standard improvements shall be for Tenant's account and at Tenant's cost (and Tenant shall pay ad valorem taxes and increased insurance thereon or attributable thereto), which cost shall be payable by Tenant to Landlord upon demand as additional rent.

(c) Tenant further agrees to pay Landlord's construction management company a fee (the "Construction Management Fee") of five percent (5%) of the Costs of Construction as compensation for its supervision of the construction and installation of the Finish Work no later than the commencement of construction thereof. Landlord and Tenant agree that the Construction Management Fee may be paid out of the Finish Allowance to the extent funds are available for such purpose. Tenant agrees that in the event of default of payment thereof, Landlord (in addition to all other remedies) shall have the same rights as in the event of default of payment of Rent under the Lease.

3. Substantial Completion. When Landlord considers the Finish Work to be Substantially Complete (defined below), it shall deliver to Tenant notice thereof (the "Notice of Substantial Completion") which will (i) stipulate any so called "punch list" items which in Landlord's determination remain incomplete, and (ii) set forth the Date of Substantial Completion (defined below).
4. Warranties. LANDLORD SHALL MAKE NO WARRANTIES, EXPRESS OR IMPLIED, WITH RESPECT TO THE FINISH WORK. ALL IMPLIED WARRANTIES WITH RESPECT THERETO, INCLUDING BUT NOT LIMITED TO THOSE OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE, ARE EXPRESSLY NEGATED AND WAIVED. WITHOUT LIMITING THE FOREGOING, LANDLORD SHALL NOT BE RESPONSIBLE FOR FAILURE OF THE FINISH WORK. Landlord will assign to Tenant, without recourse, any warranties obtained from contractors, subcontractors, suppliers and other Third Parties to the extent such warranties are assignable (provided that in no event shall Landlord be obligated under any such warranties).
5. Landlord Liability. Notwithstanding anything to the contrary set forth in the Lease or in this Exhibit, if the Commencement Date is delayed for any reason (including without limitation, the failure by any current tenant or occupant of any portion of the Leased

Premises to vacate any portion of the Leased Premises), Landlord shall not be liable or responsible for any claims, damages or liabilities in connection therewith or by reason thereof, nor shall such delay constitute a default by Landlord hereunder.

6. Time is of the Essence. It is stipulated that time is of the essence in connection with Landlord's and Tenant's compliance with the terms of this Exhibit. Without limitation of the foregoing, it is also stipulated and agreed that Landlord's obligation to undertake any Finish Work or other leasehold improvements (other than "punch list" items) under this Exhibit and Landlord's obligations with respect to the Finish Allowance shall terminate automatically (and without further act or instrument) upon Substantial Completion.

7. Definitions.

(a) "Costs of Construction" shall mean all costs and expenses of any kind whatsoever related to or arising out of the Finish Work, including, without limitation, (i) all amounts payable to contractors, subcontractors, artisans, laborers, architects, construction managers (including Landlord's construction management company), suppliers of materials and/or manufacturers of materials and engineers with respect to the Finish Work, (ii) all costs and expenses of space planning and design (including, without limitation, costs and expenses directly attributable to space plans and construction drawings, including the Final Working Drawings), and (iii) the cost of an asbestos survey.

(b) "Date of Substantial Completion" shall mean the date which is the earlier of: (i) the date on which the Finish Work is Substantially Complete, or (ii) the date on which the Finish Work would have been Substantially Complete but for a Tenant Delay, both as reasonably determined by Landlord.

(c) "Substantially Complete" and "Substantial Completion" shall mean (i) that the Finish Work has been performed in the Leased Premises in substantial accordance with the Final Working Drawings (exclusive of any "punch list" items), (ii) all construction debris has been removed from the Leased Premises and the Leased Premises are clean, and (iii) the Leased Premises may reasonably be used and occupied by Tenant for general office purposes and/or for the Permitted Use.

(d) "Tenant Delay." shall mean the number of days Substantial Completion is delayed as a result of (i) Tenant's failure to meet any dates established in the Lease or this Exhibit, (ii) any changes to the Finish Work requested to be made by Tenant (and approved by Landlord), (iii) Tenant's failure to sufficiently respond to any of Landlord's inquiries or demands, (iv) any breach by Tenant of its obligations under the Lease, including without limitation, the failure to comply with this Exhibit, and (v) any other delay or delays caused by Tenant or Tenant's engineers, architects, consultants, employees, agents, contractors and subcontractors.

**RIDER "1"**  
**OPTION TO EXTEND**  
**(Two-Time)**

Tenant, at its option, may extend the Lease Term for two (2) successive additional periods of forty-eight (48) months each (the first such period, the "First Extension Period," the second such period, the "Second Extension Period," and each, an "Extension Period"). In order to exercise its option to extend as provided for in this Rider, (i) Tenant must provide Landlord with written notice of its intent to extend the Lease Term at least six (6) months prior to the expiration of the Lease Term (which, in the case of Tenant's exercise of its option with respect to the Second Extension Period, shall be six (6) months prior to the expiration of the First Extension Period), and (ii) Tenant must not be in default (taking into account any applicable notice and cure periods) of its obligations under the Lease either at the time it sends such notice to Landlord or at the time that the applicable Extension Period commences. Upon the service of such notice and subject to the conditions set forth in the preceding sentence, Landlord shall, within ten (10) business days after receipt of Tenant's written notice, notify Tenant in writing of Landlord's determination of the Prevailing Market Rate (defined below) for the Leased Premises during the applicable Extension Period. The "Prevailing Market Rate" for the applicable Extension Period shall be the prevailing rental rate for properties of equivalent quality, size, and utility, in the office submarket in which the Building is located, with the length of the lease term, Landlord concessions, and the credit standing of Tenant to be taken into account. Tenant shall, within thirty (30) business days of receipt of Landlord's written notice of Landlord's determination of the Prevailing Market Rate, notify Landlord in writing of its acceptance, dispute, or rejection of Landlord's determination of the Prevailing Market Rate. If Tenant rejects Landlord's determination or does not timely respond, then the Lease will terminate at the end of the Lease Term (without renewal, or further renewal [as the case may be]). If Tenant disputes Landlord's determination of the Prevailing Market Rate, and Landlord and Tenant are not able to reach a mutual agreement as to the Prevailing Market Rate during the following thirty (30) business day period, then the Lease will terminate at the end of the Lease Term. If Tenant accepts Landlord's determination, or Tenant and Landlord otherwise agree upon the Prevailing Market Rate, this Lease shall be extended without the necessity of the execution of any further instrument or document. Such Extension Period shall (A) commence upon the expiration date of the Lease Term (which, in the case of the Second Extension Period, shall be the date upon which the First Extension Period expires), (B) expire upon the same day of the forty-eighth (48) calendar month thereafter, and (C) be upon the same terms, covenants, and conditions as provided in the Lease for the initial Lease Term, except that the Base Rent payable during an Extension Period shall be at the Prevailing Market Rate as determined above beginning at the commencement of the applicable Extension Period. Payment of all additional rent and other charges required to be made by Tenant under the Lease for the initial Lease Term shall continue to be made during the applicable Extension Period in accordance with the terms and provisions of the Lease. Any assignment of the Lease or subletting of the Leased Premises by Tenant shall terminate the option(s) to extend the Lease Term contained herein. Notwithstanding the foregoing, in no event shall Base Rent for an Extension Period be less than the Base Rent during the last year of the initial Lease Term (which, in the case of the Second Extension Period, shall

be the last year of the First Extension Period). Notwithstanding any provision to the contrary contained in this Rider, Tenant shall not have the option to extend the Lease Term for the Second Extension Period unless it has properly exercised its option to extend the Lease Term for the First Extension Period.

**RIDER "2"**

**TENANT'S PREFERENTIAL RIGHT TO LEASE**

1. Prior to Landlord's leasing that certain contiguous space on the first (1<sup>st</sup>) floor of the Building, designated on Exhibit "A-1" as the additional space (the "Additional Space"), to third parties (other than (i) the tenant then in possession of the Additional Space or (ii) any tenant currently holding a right to expand into, or right of first refusal on, the Additional Space), Landlord shall first offer to lease to Tenant the Additional Space before leasing such space to any third party. Such offer shall be in writing and specify the lease terms for the Additional Space, including the rent to be paid for the Additional Space, the term therefor, and the date on which the Additional Space shall be included in the Leased Premises (the "Offer Notice"). Tenant shall notify Landlord in writing whether Tenant elects to lease the entire Additional Space on the terms set forth in the Offer Notice, within five (5) days after the day on which Landlord delivers to Tenant the Offer Notice. If Tenant timely elects to lease the Additional Space, then Landlord and Tenant shall execute an amendment to the Lease, effective as of the date the Additional Space is to be included in the Leased Premises. Such amendment shall specify the terms set forth in the Offer Notice to the extent not inconsistent with the terms of this Lease; however, Tenant shall accept the Additional Space in its "AS-IS, WHERE-IS, WITH ALL FAULTS" condition, and Landlord shall not provide to Tenant any allowance (e.g. moving allowance, construction allowance, and the like) or other tenant inducements except as specifically provided in the Offer Notice. If Tenant fails to timely notify Landlord of its acceptance of the Offer Notice, Tenant shall be deemed to have rejected the same.

Notwithstanding the foregoing, if prior to Landlord's delivery to Tenant of the Offer Notice, Landlord has received an offer to lease all or part of the Additional Space from a third party (a "Third Party Offer") and such Third Party Offer includes space in excess of the Additional Space, Tenant must exercise its right hereunder, if at all, as to all of the space contained in the Third Party Offer. If Tenant fails or is unable to timely exercise its right hereunder, then such right shall lapse, time being of the essence with respect to the exercise thereof, and Landlord may lease all or any portion of the Additional Space to third parties on such terms as Landlord may elect. Tenant may not exercise its rights under this Rider if an event of default under the Lease exists or, if after the Commencement Date, Tenant is not then occupying the entire Leased Premises. For purposes hereof, if an Offer Notice is delivered for less than all of the Additional Space but such notice provides for an expansion, right of first refusal, or other preferential right to lease some of the remaining portion of the Additional Space, then such remaining portion of the Additional Space shall thereafter be excluded from the provisions of this Rider.

2. Furthermore, Tenant's rights under this Rider shall terminate if (a) the Lease or Tenant's right to possession of the Leased Premises is terminated; (b) Tenant assigns any of its interest in the Lease or sublets any portion of the Leased Premises, other than in conjunction with a Permitted Affiliate; or (c) Tenant rejects (or is deemed to have rejected) any Offer Notice or Third Party Offer.



**RIDER "3"**  
**TERMINATION OPTION**

Subject to the terms of this Rider, Tenant shall have the option ("Termination Option") to terminate this Lease effective upon the date (the "Termination Date") which is the last day of the twenty-fourth (24<sup>th</sup>) full calendar month during the Lease Term by: (i) notifying Landlord (the "Notification") in writing of Tenant's exercise of the Termination Option at least four (4) months prior to the Termination Date; and (ii) paying to Landlord, in cash or its equivalent, concurrently with delivery of the Notification, a termination fee equal to the sum of all unamortized leasing costs (bearing interest at ten percent (10%) per annum compounded monthly) incurred by Landlord with respect to the Lease and/or Tenant's occupancy of the Leased Premises. Should Tenant exercise the Termination Option in accordance with the foregoing terms and provisions, the Lease shall terminate on the Termination Date, and neither Landlord nor Tenant shall have any further liability or obligation under the Lease after the Termination Date; provided, however, that neither Landlord nor Tenant shall be relieved of or from any of its obligations, covenants and/or liabilities arising under the Lease, or in any way relating to the Leased Premises, which accrue on or prior to the Termination Date, including without limitation any obligation of indemnity or reimbursement arising under the Lease.

If Tenant fails to exercise the Termination Option in accordance with all terms and provisions of the foregoing paragraph, then the Termination Option shall be deemed void and Tenant shall have automatically and forever waived Tenant's right to exercise the Termination Option. Notwithstanding any provision of the Lease or of this Rider to the contrary, Tenant shall not be entitled to exercise the Termination Option if: (i) any event of default exists either at the time of the Notification or on the Termination Date; (ii) Tenant is not then occupying the entire Leased Premises; and/or (iii) Tenant has assigned any of its interest in this Lease or sublet any portion of the Leased Premises.

### Summary of Compensation for Executive Officers

Following is a description of the compensation arrangements for each of PC Connection, Inc.'s (the "Company's") named executive officers. The Company's named executive officers consist of: (i) Patricia Gallup, President, Chief Executive Officer, and Chairman; (ii) Robert Wilkins, Executive Vice President; (iii) Peter Cannone, Senior Vice President, Sales Subsidiaries; (iv) Jack Ferguson, Vice President, Treasurer and Chief Financial Officer, and (v) Bradley Mousseau, Vice President, Human Resources.

The Compensation Committee annually sets the compensation of the Chief Executive Officer. The Compensation Committee also reviews the recommendations of the Chief Executive Officer regarding the compensation of the Company's other executive officers. The Compensation Committee seeks to achieve three broad goals in connection with the Company's compensation philosophy and decisions regarding compensation. First, the Company is committed to providing executive compensation designed to attract, retain, and motivate executives who contribute to the long-term success of the Company and are capable of leading the Company in achieving its business objectives in the competitive and rapidly changing industry in which the Company operates. Second, the Company wants to reward executives for the achievement of business objectives of the Company and/or the individual executive's particular area of responsibility. By tying compensation in part to achievement, the Company believes that a performance-oriented environment is created for the Company's executives. Finally, compensation is intended to provide executives with an equity interest in the Company so as to link a meaningful portion of the compensation of the Company's executives with the performance of the Company's Common Stock.

Each executive's total compensation depends upon the executive's performance against specific objectives. These objectives include both quantitative factors related to the Company's short-term financial objectives and qualitative factors such as (a) demonstrated leadership ability, (b) management development, (c) compliance with Company policies, and (d) anticipation of and response to changing market and economic conditions, to enhance the Company's ability to operate profitably. Compensation for the Company's executives generally consists of three elements:

- salary—levels are generally set by reviewing compensation for competitive positions in the market and considering the executive's level of responsibility, qualifications, and experience, as well as the Company's financial performance and the individual's performance;
- bonus—amounts are generally based on achievement of the Company's performance goals in any given year; and
- stock option grants—options provide long-term incentives to promote and identify long-term interests between the Company's employees and its stockholders and to assist in the retention of executives.

In 2005, the Company granted Jack L. Ferguson an option to purchase 40,000 shares of the Company's common stock upon his appointment as Vice President and Chief Financial Officer. The exercise price of the option was \$5.38. This option was fully vested upon grant date and expires in ten years. There were no other stock options awarded in 2005 to the Company's named executive officers.

The following table lists the 2005 annual base salaries and bonuses of the Company's named executive officers:

	<u>Salary</u>	<u>Bonus</u>
Patricia Gallup President, Chief Executive Officer, and Chairman	\$432,115	—
Robert Wilkins <sup>(1)</sup> Executive Vice President	\$418,904	\$10,000
Peter Cannone Senior Vice President, Sales Subsidiaries	\$360,631	\$10,000
Jack Ferguson <sup>(2)</sup> Vice President, Treasurer and Chief Financial Officer	\$299,408	\$10,000
Bradley Mousseau Vice President, Human Resources	\$231,692	\$10,000

(1) Mr. Wilkins resigned as Executive Vice President, effective March 30, 2006.

(2) Mr. Ferguson was appointed Chief Financial Officer on December 30, 2005. Mr. Ferguson had been serving as interim chief financial officer since October 21, 2004, upon the resignation of Mark A. Gavin, the Company's former Senior Vice President of Finance and Chief Financial Officer.

**Summary Compensation for Non-Employee Directors**

PC Connection, Inc.'s (the "Company's") non-employee directors currently consist of: (i) Bruce Barone; (ii) Joseph Baute; and (iii) Donald Weatherson. In 2005, non-employee directors of the Company received an annual retainer. In addition to this retainer, non-employee directors were entitled to receive a fee for each regularly scheduled board meeting attended in person and a fee for each committee meeting attended. The table below sets forth the annual retainer, per board meeting fees and per committee meeting fees paid to our non-employee directors in 2005:

<u>Director</u>	<u>Annual Retainer<sup>(1)</sup></u>	<u>Fee Per Board Meeting Attended</u>	<u>Fee Per Committee Meeting Attended<sup>(3)</sup></u>
Bruce Barone	\$ 22,000	\$ 1,500	\$ 1,500
Joseph Baute	\$ 22,000	\$ 1,500	\$ 1,500
Donald Weatherson	\$ 12,833 <sup>(2)</sup>	\$ 1,500	\$ 1,500

(1) In addition, the non-employee directors receive reimbursement for all reasonable expenses incurred in attending board and committee meetings.

(2) Represents the pro-rata portion of a \$22,000 annual retainer commencing on June 9, 2005.

The Company did not grant any stock options to non-employee directors in 2005.

**CORPORATE ORGANIZATIONAL STRUCTURE:**

PC Connection, Inc., a Delaware corporation, is the parent company of the following wholly owned subsidiaries:

1. PC Connection Sales Corporation, a Delaware corporation.
2. PCSC, Inc., a Delaware corporation (subsidiary of PC Connection Sales Corporation).
3. Merrimack Services Corporation, a Delaware corporation.
4. GovConnection, Inc. a Maryland corporation.
5. MoreDirect, Inc., a Florida corporation.
6. MD Professional Services, Inc., a Delaware corporation (subsidiary of MoreDirect, Inc.).

**CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We consent to the incorporation by reference in Registration Statement Nos. 333-40172, 333-50845, 333-50847, 333-66450, 333-69981, 333-83943, 333-91584, 333-106652, and 333-130389 on Form S-8 of our report dated March 30, 2006, relating to the financial statements and financial statement schedules of PC Connection, Inc. appearing in this Annual Report on Form 10-K of PC Connection, Inc. for the year ended December 31, 2005.

Deloitte & Touche LLP

Boston, Massachusetts

March 30, 2006

## CERTIFICATIONS

I, Patricia Gallup, certify that:

1. I have reviewed this Annual Report on Form 10-K of PC Connection, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) [Not Applicable];
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 30, 2006

/s/ PATRICIA GALLUP

---

Patricia Gallup  
Chairman and Chief Executive Officer

## CERTIFICATIONS

I, Jack Ferguson, certify that:

1. I have reviewed this Annual Report on Form 10-K of PC Connection, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) [Not Applicable];
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 30, 2006

/s/ JACK FERGUSON

---

**Jack Ferguson**  
**Vice President, Treasurer and Chief Financial Officer**



CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,

AS ADOPTED PURSUANT TO

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the annual report on Form 10-K of PC Connection, Inc. (the "Company") for the year ended December 31, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Patricia Gallup, Chief Executive Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, that:

- (1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 30, 2006

/s/ PATRICIA GALLUP

---

**Patricia Gallup**  
**Chairman and Chief Executive Officer**

## CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,

## AS ADOPTED PURSUANT TO

## SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the annual report on Form 10-K of PC Connection, Inc. (the "Company") for the year ended December 31, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Jack Ferguson, Treasurer, Vice President and Chief Financial Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, that:

- (1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 30, 2006

/s/ JACK FERGUSON

---

**Jack Ferguson**  
**Vice President, Treasurer and Chief Financial Officer**