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SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

**FORM 10-Q**

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

For the Fiscal Quarter Ended November 27, 2005, or

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

For the Transition period from \_\_\_ to \_\_\_.

Commission file number: 0-27446

**LANDEC CORPORATION**

(Exact name of registrant as specified in its charter)

**California**  
(State or other jurisdiction of  
incorporation or organization)

**94-3025618**  
(IRS Employer  
Identification Number)

**3603 Haven Avenue**  
**Menlo Park, California 94025**  
(Address of principal executive offices)

Registrant's telephone number, including area code:  
**(650) 306-1650**

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 at least the past 90 days.

Yes  No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

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

Yes  No

As of December 20, 2005, there were 24,866,403 shares of Common Stock outstanding.

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**LANDEC CORPORATION**  
FORM 10-Q For the Fiscal Quarter Ended November 27, 2005  
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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

LANDEC CORPORATION  
CONSOLIDATED BALANCE SHEETS  
(In thousands)

	November 27, 2005 (Unaudited)	May 29, 2005*
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 6,451	\$ 12,871
Marketable securities	—	1,968
Accounts receivable, less allowance for doubtful accounts of \$363 and \$313 at November 27, 2005 and May 29, 2005	18,237	15,405
Accounts receivable, related party	555	476
Inventory	19,725	9,917
Notes and advances receivable	1,142	419
Notes receivable, related party	55	89
Prepaid expenses and other current assets	1,570	2,042
Assets held for sale	1,190	1,190
Total Current Assets	48,925	44,377
Property and equipment, net	17,504	17,275
Goodwill, net	28,894	25,987
Trademarks net	13,248	11,570
Other intangibles, net	868	58
Notes receivable	325	426
Notes receivable, related party	—	7
Other assets	178	375
Total Assets	<u>\$ 109,942</u>	<u>\$ 100,075</u>
Current Liabilities:		
Accounts payable	\$ 18,607	17,513
Related party payables	398	793
Accrued compensation	2,189	1,907
Other accrued liabilities	2,298	2,141
Deferred revenue	3,618	557
Lines of credit	7,272	—
Current maturities of long term debt	196	548
Total Current Liabilities	34,578	23,459
Long term debt, less current maturities	1,947	2,540
Other liabilities	—	550
Minority interest	1,454	1,466
Total Liabilities	37,979	28,015
Shareholders' Equity:		
Common stock, \$0.001 par value; 50,000,000 shares authorized; 24,383,954 and 24,086,368 shares issued and outstanding at November 27, 2005 and May 29, 2005, respectively	123,411	121,950
Accumulated deficit	(51,448)	(49,890)
Total Shareholders' Equity	71,963	72,060
Total Liabilities and Shareholders' Equity	<u>\$ 109,942</u>	<u>\$ 100,075</u>

\* Amounts as of May 29, 2005 are derived from the May 29, 2005 audited consolidated financial statements.

See accompanying notes.

**LANDEC CORPORATION**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(Unaudited)**  
**(In thousands, except per share amounts)**

	Three Months Ended		Six Months Ended	
	November 27, 2005	November 28, 2004	November 27, 2005	November 28, 2004
<b>Revenues:</b>				
Product sales	\$ 52,560	\$ 49,696	\$ 100,888	\$ 95,263
Services revenue, related party	922	876	2,093	2,027
License fees	172	22	294	44
Royalty revenues, related party	58	54	134	128
Research, development and royalty revenues	—	23	8	63
<b>Total revenues</b>	<b>53,712</b>	<b>50,671</b>	<b>103,417</b>	<b>97,525</b>
<b>Cost of revenue:</b>				
Cost of product sales	44,861	42,748	85,706	81,236
Cost of product sales, related party	1,166	1,506	2,829	3,395
Cost of services revenue	596	421	1,203	1,158
<b>Total cost of revenue</b>	<b>46,623</b>	<b>44,675</b>	<b>89,738</b>	<b>85,789</b>
<b>Gross profit</b>	<b>7,089</b>	<b>5,996</b>	<b>13,679</b>	<b>11,736</b>
<b>Operating costs and expenses:</b>				
Research and development	820	685	1,579	1,489
Selling, general and administrative	7,154	5,946	13,335	11,321
<b>Total operating costs and expenses</b>	<b>7,974</b>	<b>6,631</b>	<b>14,914</b>	<b>12,810</b>
<b>Operating loss</b>	<b>(885)</b>	<b>(635)</b>	<b>(1,235)</b>	<b>(1,074)</b>
Interest income	130	9	250	19
Interest expense	(177)	(87)	(250)	(205)
Minority interest expense	(101)	(124)	(316)	(276)
Other (expense) income	(4)	29	(7)	36
<b>Net loss</b>	<b>\$ (1,037)</b>	<b>\$ (808)</b>	<b>\$ (1,558)</b>	<b>\$ (1,500)</b>
<b>Basic and diluted net loss per share</b>	<b>\$ (0.04)</b>	<b>\$ (0.03)</b>	<b>\$ (0.06)</b>	<b>\$ (0.06)</b>
<b>Shares used in computing basic and diluted net loss per share</b>	<b>24,350</b>	<b>23,595</b>	<b>24,233</b>	<b>23,396</b>

*See accompanying notes.*

**LANDEC CORPORATION**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Unaudited)**  
**(In thousands)**

	Six Months Ended	
	November 27, 2005	November 28, 2004
Cash flows from operating activities:		
Net loss	\$ (1,558)	\$ (1,500)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	1,529	1,703
Loss on sale of property and equipment	16	42
Minority interest	316	276
Changes in current assets and current liabilities, net of effects of acquisition of assets of Heartland Hybrids, Inc.:		
Accounts receivable, net	(2,562)	(395)
Inventory	(8,890)	(6,029)
Issuance of notes and advances receivable	(1,064)	(854)
Collection of notes and advances receivable	329	940
Prepaid expenses and other current assets	498	(210)
Accounts payable	(1,143)	1,506
Related party payables	(395)	(237)
Accrued compensation	282	83
Other accrued liabilities	120	342
Deferred revenue	2,511	2,386
Net cash used in operating activities	<u>(10,011)</u>	<u>(1,947)</u>
Cash flows from investing activities:		
Purchases of property and equipment	(1,533)	(2,089)
Purchase of marketable securities	(991)	—
Proceeds from maturities of marketable securities	2,959	—
Issuance of notes and advances receivable	(18)	(15)
Collection of notes and advances receivable	172	340
Increase in other assets	—	(180)
Acquisition of assets of Heartland Hybrids, Inc., net of cash acquired	(3,630)	—
Net cash used in investing activities	<u>(3,041)</u>	<u>(1,944)</u>
Cash flows from financing activities:		
Proceeds from sale of common stock	501	4,441
Decrease (increase) in other assets	199	(38)
Borrowings on lines of credit	11,103	55,936
Payments on lines of credit	(3,831)	(57,061)
Payments on long term debt	(1,011)	(280)
Proceeds from issuance of long term debt	—	1,200
Distributions to minority interest	(329)	(550)
Net cash provided by financing activities	<u>6,632</u>	<u>3,648</u>
Net decrease in cash and cash equivalents	(6,420)	(243)
Cash and cash equivalents at beginning of period	12,871	6,458
Cash and cash equivalents at end of period	<u>\$ 6,451</u>	<u>\$ 6,215</u>

*See accompanying notes.*

**LANDEC CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**

**1. Basis of Presentation**

Landec Corporation and its subsidiaries (“Landec” or the “Company”) design, develop, manufacture, and sell temperature-activated and other specialty polymer products for a variety of food products, agricultural products, and licensed partner applications. The Company directly markets and distributes hybrid corn seed to farmers through its Landec Ag, Inc. (“Landec Ag”) subsidiary and specialty packaged fresh-cut vegetables and whole produce to retailers and club stores, primarily in the United States and Asia through its Apio, Inc. (“Apio”) subsidiary.

The accompanying unaudited consolidated financial statements of Landec have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions for Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments (consisting of normal recurring accruals) have been made which are necessary to present fairly the financial position at November 27, 2005 and the results of operations and cash flows for all periods presented. Although Landec believes that the disclosures in these financial statements are adequate to make the information presented not misleading, certain information normally included in financial statements and related footnotes prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted per the rules and regulations of the Securities and Exchange Commission. The accompanying financial data should be reviewed in conjunction with the audited financial statements and accompanying notes included in Landec’s Annual Report on Form 10-K for the fiscal year ended May 29, 2005.

The results of operations for the three and six months ended November 27, 2005 are not necessarily indicative of the results that may be expected for an entire fiscal year. For instance, due to the cyclical nature of the corn seed industry, a significant portion of Landec Ag revenues and profits will be concentrated over a few months during the spring planting season (generally during Landec’s third and fourth fiscal quarters). In addition, Landec Ag purchases corn seed and collects cash deposits from farmers in advance of shipping the corn during the Company’s third and fourth quarters. The increased levels of inventory and deferred revenue at November 27, 2005 compared to May 29, 2005 reflect the seasonal nature of Landec Ag’s seed business.

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported results of operations during the reporting period. Actual results could differ materially from those estimates.

For instance, the carrying value of notes and advances receivable, are impacted by current market prices for the related crops, weather conditions and the fair value of the underlying security obtained by the Company, such as, liens on property and crops. The Company recognizes losses when it estimates that the fair value of the related crops or security is insufficient to cover the advance or note receivable.

**Recent Accounting Pronouncements**

In December 2004, the FASB issued Statement No. 123 (revised 2004), *Share-Based Payment*, or SFAS No. 123R, which is a revision of SFAS No. 123, and supersedes APB Opinion 25. SFAS 123R requires all share-based payments to employees and directors, including grants of stock options, to be recognized in the statement of operations based on their fair values. On April 14, 2005, the SEC adopted a new rule that amended the compliance dates for SFAS 123R such that the Company is now allowed to adopt the new standard effective in the second quarter of fiscal year 2007. The pro forma disclosures previously permitted under SFAS 123 will no longer be an alternative to financial statement recognition. As permitted by SFAS 123, the Company currently accounts for share-

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based payments to employees using APB Opinion 25's intrinsic value method and, as such, recognizes no compensation cost for employee stock options.

Under SFAS 123R, the Company must determine the appropriate fair value model and related assumptions to be used for valuing share-based payments, the amortization method for compensation cost and the transition method to be used at the date of adoption. The transition methods include modified prospective and retroactive adoption options. Under the retroactive option, prior periods may be restated either as of the beginning of the year of adoption or for all periods presented. The modified prospective method requires that compensation expense be recorded for all unvested stock options and restricted stock at the beginning of the first quarter of adoption of SFAS 123R, while the retroactive method would record compensation expense for all unvested stock options and restricted stock beginning with the first period restated. The Company is currently evaluating the requirements of SFAS 123R as well as option valuation methodologies related to its stock option plans. Although the Company has not yet determined the method of adoption or the effect of adopting SFAS 123R, the Company expects that the adoption of SFAS 123R may have a material impact on the Company's consolidated results of operations. The impact of adoption of SFAS 123R cannot be predicted at this time because it will depend on, among other things, the levels of share-based payments granted in the future, the method of adoption and the option valuation method used. SFAS 123R also requires the benefits of tax deductions in excess of recognized compensation costs to be reported as a financing cash flow, rather than as an operating cash flow as required under current literature. This requirement will reduce net operating cash flows and increase net financing cash flows in periods after adoption.

### **Reclassifications**

Certain reclassifications have been made to prior period financial statements to conform to the current period presentation.

### **2. Purchase of Heartland Hybrids Assets**

On August 29, 2005, Landec Corporation, through its agricultural seed subsidiary, Landec Ag, Inc. acquired the assets of Heartland Hybrids, Inc. ("Heartland"), which is based in Dassel, MN, for \$6.0 million. The consideration at closing consisted of 152,186 shares of Landec Common Stock valued at \$1.0 million and cash of \$3.65 million. In addition, the agreement provides for future payments to the former owners of Heartland of up to \$1.35 million. These payments consist of a cash earn-out of \$1.2 million based on Heartland achieving certain financial targets for fiscal years 2006 and 2007 and a \$150,000 holdback for any post closing adjustments. Any amounts remaining in the holdback reserve will be paid out in May 2006. Heartland operations are included in Landec's consolidated results of operations commencing August 29, 2005. The purchase price has been allocated to the acquired assets and liabilities based on their relative fair market values, subject to final adjustments predominantly related to earn-out payments. These allocations are based on independent valuations and other studies.

The following is a summary of the purchase price allocation (in thousands):

Net assets and liabilities	\$ (757)
Customer base	800
Trademark	1,700
Goodwill	<u>2,907</u>
	\$ 4,650

In June 2001, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 141, *Business Combinations*, and No. 142, *Goodwill and Other Intangible Assets* (SFAS 142), effective for fiscal years beginning after December 15, 2001. Under the new rules, goodwill and intangible assets deemed to have indefinite lives, such as trademarks, are no longer amortized but are subject to annual impairment tests in accordance with the Statements. The customer base intangible is not an indefinite life intangible and is being amortized over ten years.

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No proforma information is deemed necessary as the operations of Heartland Hybrids are immaterial to Landec's revenues and results of operations.

### 3. Net Loss Per Diluted Share

For the three months ended November 27, 2005 and November 28, 2004, the computation of the diluted net loss per share excludes the impact of options to purchase 472,000 shares and 545,197 shares of Common Stock, respectively, as such impacts would be antidilutive for these periods.

For the six months ended November 27, 2005 and November 28, 2004, the computation of the diluted net loss per share excludes the impact of options to purchase 759,136 shares and 573,079 shares of Common Stock, respectively, as such impacts would be antidilutive for these periods.

### 4. Stock-Based Compensation

As permitted by Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation," (SFAS 123), as amended by Statement of Financial Accounting Standards No. 148, "Accounting for Stock-Based Compensation – Transition and Disclosure," (SFAS 148), the Company elected to continue to apply the provisions of Accounting Principle Board Opinion No. 25, "Accounting for Stock Issued to Employees," (APB 25) and related interpretations in accounting for its employee stock option and stock purchase plans. The Company is not required under APB 25 and related interpretations to recognize compensation expense in connection with its employee stock option and stock purchase plans, unless the exercise price of the Company's employee stock options is less than the market price of the underlying stock at the date of grant.

Pro forma information regarding net loss and net loss per share is required by SFAS 148 and has been determined as if the Company had accounted for its employee stock options under the fair value method prescribed by SFAS 123. The fair value for these options was estimated at the date of grant using the Black-Scholes option valuation model with the following weighted average assumptions: risk-free interest rates ranging from 3.93% to 4.52% for the three months ended November 27, 2005, 3.35% to 3.47% for the three months November 28, 2004; 3.69% to 4.52% for the six months ended November 27, 2005, and 3.35% to 3.93% for the six months ended November 28, 2004; a dividend yield of 0.0% for the three and six months ended November 27, 2005 and November 28, 2004; a volatility factor of the expected market price of the Company's common stock of 0.54 and 0.59 as of November 27, 2005 and November 28, 2004, respectively; and a weighted average expected life of the options of 4.01 years and 4.61 years for the three and six months ended November 27, 2005 and November 28, 2004, respectively.

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the vesting period of the options using the straight-line method. The Company's pro forma information follows (in thousands except for per share data):

	Three Months Ended		Six Months Ended	
	November 27, 2005	November 28, 2004	November 27, 2005	November 28, 2004
Net loss	\$ (1,037)	\$ (808)	\$ (1,558)	\$ (1,500)
Deduct:				
Stock-based employee expense determined under SFAS 123	(428)	(487)	(665)	(664)
Pro forma net loss	\$ (1,465)	\$ (1,295)	\$ (2,223)	\$ (2,164)
Basic and diluted net loss per share — as reported	\$ (0.04)	\$ (0.03)	\$ (0.06)	\$ (0.06)
Basic and diluted pro forma net loss per share	\$ (0.06)	\$ (0.05)	\$ (0.09)	\$ (0.09)



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The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. These amounts do not necessarily represent the effects of employee stock options on reported net income (loss) for future years.

### 5. Goodwill and Other Intangibles

The Company is required under SFAS 142 to review goodwill and indefinite lived intangible assets at least annually. During the six months ended November 27, 2005, the Company completed its annual impairment review. The review is performed by grouping the net book value of all long-lived assets for reporting entities, including goodwill and other intangible assets, and comparing this value to the related estimated fair value. The determination of fair value is based on estimated future discounted cash flows related to these long-lived assets. The discount rate used was based on the risks associated with the reporting entities. The determination of fair value was performed by management using the services of an independent appraiser. The review concluded that the fair value of the reporting entities exceeded the carrying value of their net assets and thus no charge was warranted as of November 27, 2005.

### 6. Inventories

Inventories are stated at the lower of cost (first-in, first-out method) or market and consisted of the following (in thousands):

	November 27, 2005	May 29, 2005
Finished goods	\$ 13,387	\$ 6,132
Raw material	6,265	3,655
Work in process	73	130
Total	<u>\$ 19,725</u>	<u>\$ 9,917</u>

### 7. Purchase and Pending Sale of Fruit Land

On January 14, 2005, the Company entered into an agreement to purchase approximately 155 acres of fruit land from an individual for \$812,500. This amount was paid to the seller through the funding of an escrow account on March 23, 2005. In a separate unrelated transaction, on January 31, 2005, the Company entered into an agreement to sell approximately 45 acres of grape land to an individual for \$452,500. The Company received \$28,000 in cash and promissory notes receivable for \$424,500, \$56,000 of which is due by December 31, 2005 and the remainder to be paid from net profits from the sale of grapes produced from this property with a final payment due on December 31, 2009. Interest accrues at the prime rate and is payable quarterly. The sale closed on January 3, 2006. In another transaction, the Company has an accepted offer from an individual to purchase the remaining 110 acres for \$936,000, net of sales commissions. The sale of the remaining acreage is also expected to close during January 2006. The cost of the land and the fruit of \$1.2 million is recorded as an asset held for sale in the accompanying Consolidated Balance Sheets. The Company estimates that these sales will result in a gain, the timing of recognition and the amount of the gain is yet to be finalized.

### 8. Debt

On November 1, 2005, Apio amended its revolving line of credit that was scheduled to expire on August 31, 2006, with Wells Fargo Bank N.A. The line was reduced from \$10.0 million to \$7.0 million and outstanding amounts under the line of credit now bear interest at either the prime rate less .25% or the LIBOR adjustable rate plus 1.75% (5.96% at November 27, 2005). The line of credit contains certain restrictive covenants, which require Apio to meet certain financial tests including minimum levels of net income, maximum leverage ratio, minimum net worth and maximum capital expenditures. The line of credit also affects the ability of Landec to receive payments on debt owed by Apio to Landec. Landec has pledged substantially all of the assets of Apio to secure the line with Wells Fargo Bank. At November 27, 2005, no amounts were outstanding under Apio's line of credit.

## 9. Licensing and Supply Agreement

In July 2005, the Company amended the supply agreement with Alcon, Inc. to change the expiration date of the agreement from November 1, 2012 to May 28, 2006. As a result, all of the deferred revenue has been reclassified as a current liability in the accompanying Consolidated Balance Sheets. In addition, in accordance with Staff Accounting Bulletin No. 104, *Revenue Recognition (a replacement of SAB 101)*, the entire amount of the deferred revenue of \$638,000 as of May 29, 2005, will be recognized as “recycled” revenue during fiscal year 2006. For the three and six months ended November 27, 2005, \$172,000 and \$294,000, respectively, of the related deferred revenue was recognized as “recycled” license revenue.

## 10. Related Party

Apio provides cooling and distributing services for farms in which the Chief Executive Officer of Apio (the “Apio CEO”) has a financial interest and purchases produce from those farms. Apio also purchases produce from Apio Fresh LLC (“Apio Fresh”) for sale to third parties. Apio Fresh is owned by a group of entities and persons that supply produce to Apio. One of the owners of Apio Fresh is the Apio CEO. Revenues, cost of product sales and the resulting payable and the note receivable from advances for ground lease payments, crop and harvesting costs, are classified as related party in the accompanying financial statements as of November 27, 2005 and May 29, 2005 and for the three and six months ended November 27, 2005 and November 28, 2004.

Apio leases, for approximately \$429,000 on an annual basis, agricultural land that is either owned, controlled or leased by the Apio CEO. Apio, in turn, subleases that land at cost to growers who are obligated to deliver product from that land to Apio for value added products. There is generally no net statement of operations impact to Apio as a result of these leasing activities but Apio creates a guaranteed source of supply for the value added business. Apio has loss exposure on the leasing activity to the extent that it is unable to sublease the land. For the three and six months ended November 27, 2005 the Company subleased all of the land leased from the Apio CEO and received sublease income of \$154,000 and \$321,000, respectively, which is equal to the amount the Company paid to lease that land for the period.

Apio’s domestic commodity vegetable business was sold to Apio Fresh, effective June 30, 2003. The Apio CEO is a 12.5% owner in Apio Fresh. During the three and six months ended November 27, 2005, the Company recognized revenues of \$27,000 and \$70,000, respectively, from the sale of products to Apio Fresh and royalty revenue of \$58,000 and \$134,000, respectively, from the use by Apio Fresh of Apio’s trademarks. The related accounts receivable from Apio Fresh are classified as related party in the accompanying financial statements as of November 27, 2005 and May 29, 2005.

In addition, the Apio CEO has a 6% ownership interest in Apio Cooling LP, a limited partnership in which Apio is the general partner with a 60% ownership interest. Included in the minority interest liability as of November 27, 2005 and May 29, 2005 is \$205,000 and \$201,000, respectively, owed to the Apio CEO.

All related party transactions are monitored quarterly by the Company and approved by the Audit Committee of the Board of Directors.

## 11. Comprehensive Income / Loss

The comprehensive loss of Landec is the same as the net loss.

## 12. Shareholders’ Equity

During the three and six months ended November 27, 2005, 55,342 and 145,400 shares of Common Stock, respectively, were issued upon the exercise of options under the Company’s stock option plans and the Company’s Employee Stock Purchase Plan. In addition, the Company issued to the former owners of Heartland 152,186 shares of Landec Common Stock on August 29, 2005 in connection with the purchase of Heartland assets (see Note 2).

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On October 14, 2005, following shareholder approval at the Annual Meeting of Shareholders of the Company, the 2005 Stock Incentive Plan (the "Plan") became effective and replaced the Company's four then existing equity plans. Employees (including officers), consultants and directors of the Company and its subsidiaries and affiliates are eligible to participate in the Plan.

The Plan provides for the grant of stock options (both nonstatutory and incentive stock options), stock grants, stock units and stock appreciation rights. Awards under the Plan will be evidenced by an agreement with the Plan participant. 861,038 shares of the Company's common stock ("Shares") are available for awards under the Plan. Under the Plan no recipient may be awarded any of the following during any fiscal year: (i) stock options covering in excess of 500,000 Shares; (ii) stock grants and stock units covering in excess of 250,000 Shares in the aggregate; or (iii) stock appreciation rights covering more than 500,000 Shares. In addition, awards to non-employee directors are discretionary. However, a non-employee director may not be granted awards covering in excess of 30,000 Shares in the aggregate during any fiscal year.

### 13. Business Segment Reporting

Landec operates in two business segments: the Food Products Technology segment and the Agricultural Seed Technology segment. The Food Products Technology segment markets and packs specialty packaged whole and fresh-cut vegetables that incorporate the Intelimer® based specialty packaging for the retail grocery, club store and food services industry. The Agricultural Seed Technology segment markets and distributes hybrid seed corn and seed coatings using Landec's patented Intelimer polymers to the farming industry. The Food Products Technology and Agricultural Seed Technology segments include charges for corporate services allocated from the Corporate and Other segment. Corporate and other amounts include non-core operating activities and corporate operating costs. All of the assets of the Company are located within the United States of America.

Operations by Business Segment (in thousands):

	Food Products Technology	Agricultural Seed Technology	Corporate and Other	TOTAL
<b>Three months ended November 27, 2005</b>				
Net revenues	\$ 53,403	\$ 20	\$ 289	\$ 53,712
International sales	\$ 19,921	\$ □	\$ □	\$ 19,921
Gross profit	\$ 6,869	\$ 19	\$ 201	\$ 7,089
Net income (loss)	\$ 2,398	\$ (3,188)	\$ (247)	\$ (1,037)
Interest expense	\$ 75	\$ 101	\$ 1	\$ 177
Interest income	\$ 109	\$ 14	\$ 7	\$ 130
Depreciation and amortization	\$ 624	\$ 173	\$ 23	\$ 820
<b>Three months ended November 28, 2004</b>				
Net revenues	\$ 50,594	\$ 7	\$ 70	\$ 50,671
International sales	\$ 18,465	\$ □	\$ □	\$ 18,465
Gross profit	\$ 5,865	\$ 76	\$ 55	\$ 5,996
Net income (loss)	\$ 1,474	\$ (2,320)	\$ 38	\$ (808)
Interest expense	\$ 29	\$ 58	\$ □	\$ 87
Interest income	\$ 7	\$ □	\$ 2	\$ 9
Depreciation and amortization	\$ 718	\$ 116	\$ 25	\$ 859
<b>Six months ended November 27, 2005</b>				
Net revenues	\$ 102,901	\$ 20	\$ 496	\$ 103,417
International sales	\$ 36,642	\$ □	\$ □	\$ 36,642
Gross profit	\$ 13,330	\$ 19	\$ 330	\$ 13,679
Net income (loss)	\$ 4,282	\$ (5,313)	\$ (527)	\$ (1,558)
Interest expense	\$ 148	\$ 101	\$ 1	\$ 250
Interest income	\$ 198	\$ 26	\$ 26	\$ 250
Depreciation and amortization	\$ 1,200	\$ 279	\$ 50	\$ 1,529
<b>Six months ended November 28, 2004</b>				
Net revenues	\$ 97,269	\$ 105	\$ 151	\$ 97,525
International sales	\$ 36,183	\$ □	\$ □	\$ 36,183
Gross profit	\$ 11,520	\$ 96	\$ 120	\$ 11,736
Net income (loss)	\$ 2,808	\$ (4,354)	\$ 46	\$ (1,500)
Interest expense	\$ 134	\$ 71	\$ □	\$ 205
Interest income	\$ 15	\$ 1	\$ 3	\$ 19
Depreciation and amortization	\$ 1,420	\$ 232	\$ 51	\$ 1,703

During the six months ended November 27, 2005 and November 28, 2004, sales to the Company's top five customers accounted for approximately 47% and 45%, respectively, of revenues, with the Company's top customers from the Food Products Technology segment, Costco Wholesale Corp., accounting for approximately 15% and 14%, respectively, and Pomina Enterprise Co. LTD, accounting for approximately 11% and 10%, respectively of revenues. The Company expects that, for the foreseeable future, a limited number of customers may continue to account for a significant portion of its net revenues. Virtually all of the Company's international sales are to Asia.

#### **14. Subsequent Events**

On December 23, 2005, Landec entered into an exclusive licensing agreement with a medical device company. This company paid the Company an upfront license fee of \$250,000 for the exclusive rights to use Landec's Intelimer® materials technology in a specific device field worldwide. Landec will also receive royalties on future product sales. In addition, the Company received shares of preferred stock initially valued at \$1.5 million which represents a 16.7% ownership interest in the medical device company. Landec's ownership interest could increase to as high as 19.9% based on certain milestones being achieved.

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

The following discussion should be read in conjunction with the unaudited consolidated financial statements and accompanying notes included in Part I —Item 1 of this Form 10-Q and the audited consolidated financial statements and accompanying notes and Management's Discussion and Analysis of Financial Condition and Results of Operations included in Landec's Annual Report on Form 10-K for the fiscal year ended May 29, 2005.

Except for the historical information contained herein, the matters discussed in this report are forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934. These forward-looking statements involve certain risks and uncertainties that could cause actual results to differ materially from those in the forward-looking statements. Potential risks and uncertainties include, without limitation, those mentioned in this report and, in particular the factors described below under "Additional Factors That May Affect Future Results," and those mentioned in Landec's Annual Report on Form 10-K for the fiscal year ended May 29, 2005. Landec undertakes no obligation to update or revise any forward-looking statements in order to reflect events or circumstances that may arise after the date of this report.

#### **Critical Accounting Policies and Use of Estimates**

There have been no material changes to the Company's critical accounting policies which are included and described in the Form 10-K for the fiscal year ended May 29, 2005 filed with the Securities and Exchange Commission on August 2, 2005.

#### **The Company**

Landec Corporation and its subsidiaries ("Landec" or the "Company") design, develop, manufacture and sell temperature-activated and other specialty polymer products for a variety of food products, agricultural products, and licensed partner applications. This proprietary polymer technology is the foundation, and a key differentiating advantage, upon which Landec has built its business.

Landec's core polymer products are based on its patented proprietary Intelimer□ polymers, which differ from other polymers in that they can be customized to abruptly change their physical characteristics when heated or cooled through a pre-set temperature switch. For instance, Intelimer polymers can change within the range of one or two degrees Celsius from a non-adhesive state to a highly tacky, adhesive state; from an impermeable state to a highly permeable state; or from a solid state to a viscous state. These abrupt changes are repeatedly reversible and can be tailored by Landec to occur at specific temperatures, thereby offering substantial competitive advantages in Landec's target markets.

Landec has two core businesses — Food Products Technology and Agricultural Seed Technology, in addition to our Technology Licensing/Research and Development business which is included in Corporate and Other for segment disclosure purposes (see note 13).

Our Food Products Technology business is operated through a subsidiary, Apio, Inc., and combines our proprietary food packaging technology with the capabilities of a large national food supplier and value-added produce processor. Value-added processing incorporates Landec's proprietary packaging technology with produce

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that is processed by washing, and in some cases cutting and mixing, resulting in packaged produce to achieve increased shelf life and reduced shrink (waste) and to eliminate the need for ice during the distribution cycle. This combination was consummated in December 1999 when the Company acquired Apio, Inc. and certain related entities (collectively, “Apio”).

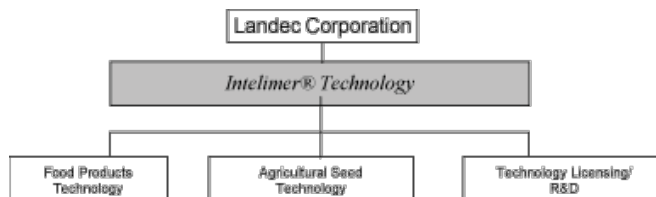
Our Agricultural Seed Technology business is operated through a subsidiary, Landec Ag, Inc., (“Landec Ag”) and combines our proprietary Intellicoat® seed coating technology with our unique e-commerce, direct marketing and consultative selling capabilities which we obtained when we acquired Fielder’s Choice Direct (“Fielder’s Choice”), a direct marketer of hybrid seed corn, in September 1997.

In addition to our two core businesses, the Company also operates a Technology Licensing/Research and Development business that licenses and/or supplies products outside of our core businesses to industry leaders such as Akzo Nobel and L’Oreal of Paris.

Landec was incorporated in California on October 31, 1986. We completed our initial public offering in 1996 and our Common Stock is listed on the Nasdaq National Market under the symbol “LNDC.” Our principal executive offices are located at 3603 Haven Avenue, Menlo Park, California 94025 and our telephone number is (650) 306-1650.

### **Description of Core Business**

Landec participates in two core business segments—Food Products Technology and Agricultural Seed Technology. In addition to these two core segments, we license technology and conduct ongoing research and development through our Technology Licensing/Research and Development Business.



### ***Food Products Technology Business***

The Company began marketing in early 1996 our proprietary Intelimer-based specialty packaging for use in the fresh-cut produce market, one of the fastest growing segments in the produce industry. Our proprietary packaging technology, when combined with produce that is processed by washing, and in some cases cut and mixed, results in packaged produce with increased shelf life, reduced shrink (waste) and without the need for ice during the distribution cycle, which we refer to as our “value-added” products. In December 1999, we acquired Apio, our largest customer at that time in the Food Products Technology business and one of the nation’s leading marketers and packers of produce and specialty packaged fresh-cut vegetables. Apio provides year-round access to produce, utilizes state-of-the-art fresh-cut produce processing technology and distributes products to the top U.S. retail grocery chains and major club stores and, has recently begun expanding its product offerings to the foodservice industry. Our proprietary Intelimer-based packaging business has been combined with Apio into a wholly owned subsidiary that retains the Apio, Inc. name. This vertical integration within the Food Products Technology business gives Landec direct access to the large and growing fresh-cut produce market.

Based in Guadalupe, California, Apio, when acquired in December 1999, consisted of two major businesses — first, the “fee-for-service” selling and marketing of whole produce and second, the specialty packaged fresh-cut and whole value-added processed products that are washed and packaged in our proprietary BreatheWay™ packaging.

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The “fee-for-service” business historically included field harvesting and packing, cooling and marketing of vegetables and fruit on a contract basis for growers in California’s Santa Maria, San Joaquin and Imperial Valleys as well as in Arizona and Mexico. The Company exited this business and certain assets associated with the business were sold in June 2003 to Apio Fresh, LLC (“Apio Fresh”). Apio Fresh is owned by a group of entities and persons that supply produce to Apio, including Nicholas Tompkins, Apio’s President and Chief Executive Officer. Under the terms of the sale, Apio Fresh purchased certain equipment and carton inventory from Apio in exchange for approximately \$410,000. In connection with the sale, Apio Fresh will pay Apio an on-going royalty fee per carton sold for the use of Apio’s brand names and Apio Fresh and its growers entered into a long-term supply agreement with Apio to supply produce to Apio for its fresh-cut value-added products. The fresh-cut value-added processed products business markets a variety of fresh-cut and whole vegetables to the top retail grocery chains and club stores. During the fiscal year ended May 29, 2005, Apio shipped more than sixteen million cartons of produce to leading supermarket retailers, wholesalers, foodservice suppliers and club stores throughout the United States and internationally, primarily in Asia.

There are five major distinguishing characteristics of Apio that provide competitive advantages in the Food Products Technology market:

- **Value-Added Supplier:** Apio has structured its business as a marketer and seller of fresh-cut and whole value-added produce. It is focused on selling products under its Eat Smart® brand and other brands for its fresh-cut and whole value-added products. As retail grocery and club store chains consolidate, Apio is well positioned as a single source of a broad range of products.
- **Reduced Farming Risks:** Apio reduces its farming risk by not taking ownership of farmland, and instead, contracts with growers for produce. The year-round sourcing of produce is a key component to the fresh-cut and whole value-added processing business.
- **Lower Cost Structure:** Apio has strategically invested in the rapidly growing fresh-cut and whole value-added business. Apio’s 60,000 square foot value-added processing plant is automated with state-of-the-art vegetable processing equipment. Virtually all of Apio’s value-added products utilize Apio’s proprietary BreatheWay™ packaging technology. Apio’s strategy is to operate one large central processing facility in one of California’s largest, lowest cost growing regions (Santa Maria Valley) and use packaging technology to allow for the nationwide delivery of fresh produce products.
- **Export Capability:** Apio is uniquely positioned to benefit from the growth in export sales to Asia and Europe over the next decade with its export business, CalEx. Through CalEx, Apio is currently one of the largest U.S. exporters of broccoli to Asia and is selling its iceless products to Asia using proprietary BreatheWay packaging technology.
- **Expanded Product Line Using Technology:** Apio, through the use of its BreatheWay packaging technology, is introducing on average twelve new value-added products each year. These new product offerings range from various sizes of fresh-cut bagged products, to vegetable trays, to whole produce products. During the last twelve months, Apio has introduced 19 new products.

### *Agricultural Seed Technology Business*

Landec Ag’s strategy is to build a vertically integrated seed technology company based on Intellicoat seed coating technology and its e-commerce, direct marketing and consultative selling capabilities.

For the coating technology the strategy is to develop a patented, functional polymer coating technology that will be broadly licensed to the seed industry. The company will initially commercialize products for the corn and soybean markets and then broaden its applications to other seed crops. Landec Ag will use its Fielder’s Choice Direct marketing and sales company to launch its applications for corn to build awareness for this technology and then broadly license its applications to the rest of the industry.

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Landec Ag's Intellicoat seed coating applications are designed to control seed germination timing, increase crop yields, reduce risks and extend crop-planting windows. These coatings are currently available on hybrid corn, soybeans and male inbred corn used for seed production. In fiscal year 2000, Landec Ag launched its first commercial product, Pollinator Plus<sup>®</sup> coatings, which is a coating application used by seed companies as a method for spreading pollination to increase yields and reduce risk in the production of hybrid seed corn. There are approximately 650,000 acres of seed production in the United States and in 2005 Pollinator Plus was used by 38 seed companies on approximately 15% of the seed production acres in the U.S.

In 2003, Landec Ag commercialized Early Plant<sup>®</sup> corn by selling the product directly to farmers through its Fielder's Choice Direct<sup>®</sup> brand. This application allows farmers to plant into cold soils without the risk of chilling injury, and enables farmers to plant as much as four weeks earlier than normal. With this capability, farmers are able to utilize labor and equipment more efficiently, provide flexibility during the critical planting period and avoid yield losses caused by late planting. In 2005, nine seed companies offered Intellicoat on their hybrid seed corn offerings and sales increased by 20% over 2004.

The third commercial application is the Relay<sup>™</sup> Cropping system of wheat and Intellicoat coated soybeans, which allows farmers to plant and harvest two crops in the same year on the same ground in geographic areas where double cropping is not possible. This provides significant financial benefit especially to farmers in the corn belt who grow wheat as a single crop.

Based in Monticello, Indiana, Fielder's Choice Direct offers a comprehensive line of corn hybrids and alfalfa to more than 12,000 farmers in over forty states through direct marketing programs. The success of Fielder's Choice comes, in part, from its expertise in selling directly to the farmer, bypassing the traditional and costly farmer-dealer system. We believe that this direct channel of distribution provides up to a 35% cost advantage compared to the farmer-dealer system.

In order to support its direct marketing programs, Fielder's Choice has developed a proprietary e-commerce, direct marketing, and consultative selling information technology that enables state-of-the-art methods for communicating with a broad array of farmers. This proprietary direct marketing information technology includes a current database of over 104,000 farmers.

On August 29, 2005, Landec Ag closed the acquisition of Heartland Hybrids, Inc., the second largest direct marketer of seed corn after Landec Ag's Fielder's Choice Direct brand. With complementary strengths in geographic areas and sales channels, the new combined organization has the opportunity to develop the most efficient and effective sales, marketing and distribution system in the seed industry, expanding Landec Ag's sales of both uncoated seed and Intellicoat coated seed.

Due to the cyclical nature of the corn seed industry, a significant portion of Landec Ag revenues and profits will be concentrated over a few months during the spring planting season (generally during Landec's third and fourth fiscal quarters). In addition, Landec Ag purchases corn seed and collects cash deposits from farmers in advance of shipping the corn during the Company's third and fourth quarters.

### ***Technology Licensing/Research and Development Businesses***

We believe our technology has commercial potential in a wide range of industrial, consumer and medical applications beyond those identified in our core businesses. For example, our core patented technology, Intelimer materials, can be used to trigger the release of small molecule drugs, catalysts, pesticides or fragrances just by changing the temperature of the Intelimer materials or to activate adhesives through controlled temperature change. In order to exploit these opportunities, we have entered into and will enter into licensing and collaborative corporate agreements for product development and/or distribution in certain fields. However, given the infrequency and unpredictability of when the Company may enter into any such licensing and research and development arrangements, the Company is unable to disclose its financial expectations in advance of entering into such arrangements.



[Table of Contents](#)**Results of Operations**

Revenues (in thousands):

	<i>Three months ended 11/27/05</i>	<i>Three months ended 11/28/04</i>	<i>Change</i>	<i>Six months ended 11/27/05</i>	<i>Six months ended 11/28/04</i>	<i>Change</i>
<i>Apio Value Added</i>	\$ 30,479	\$ 28,859	6%	\$ 60,136	\$ 55,223	9%
<i>Apio Trading</i>	22,841	21,735	5%	42,678	42,046	2%
<i>Apio Tech</i>	83	□	N/M	87	□	N/M
<i>Total Apio</i>	53,403	50,594	6%	102,901	97,269	6%
<i>Landec Ag</i>	20	7	186%	20	105	(81%)
<i>Corporate</i>	289	70	313%	496	151	228%
<i>Total Revenues</i>	\$ 53,712	\$ 50,671	6%	\$ 103,417	\$ 97,525	6%

*Apio Value Added*

Apio's value-added revenues consist of revenues generated from the sale of specialty packaged fresh-cut and whole value-added processed vegetable products that are washed and packaged in our proprietary packaging and sold under Apio's Eat Smart brand, the Dole brand and various private labels. In addition, value-added revenues include the revenues generated from Apio Cooling, LP, a vegetable cooling operation in which Apio is the general partner with a 60% ownership position.

The increase in Apio's value-added revenues for the three and six months ended November 27, 2005 compared to the same periods last year is due to increased product offerings, increased sales to existing customers, the addition of new customers and product mix changes to higher priced products. Specifically, sales of Apio's value-added 12-ounce specialty packaged retail product line grew 14% and 13%, respectively, during the three and six months ended November 27, 2005 compared to the same periods last year. In addition, sales of Apio's value-added vegetable tray products grew 11% and 22%, respectively, during the three and six months ended November 27, 2005 compared to the same periods last year. Overall value-added unit sales volume increased 3% during the second quarter of fiscal year 2005 compared to the same period last year and 4% for the six months ended November 27, 2005 compared to the same period of the prior year.

*Apio Trading*

Apio trading revenues consist of revenues generated from the purchase and sale of primarily whole commodity fruit and vegetable products to Asia through Apio's export company, Cal-Ex and from the purchase and sale of whole commodity fruit and vegetable products domestically to Wal-Mart. The export portion of trading revenues for the three and six months ended November 27, 2005 were \$19.9 million and \$36.6 million, respectively or 87% and 86%, respectively, of total trading revenues.

The increase in revenues in Apio's trading business for the three and six months ended November 27, 2005 compared to the same periods last year was primarily due to export unit volume increases of 8% and 1%, respectively.

*Apio Tech*

Apio Tech consists of Apio's packaging technology business using its BreatheWay membrane technology. The first commercial application included in Apio Tech is our banana packaging technology. Current revenues generated from Apio Tech are from the sale of our proprietary packaging for bananas.

The increase in revenues at Apio Tech during the three and six months ended November 27, 2005 compared to the same periods last year was not material to consolidated Landec revenues.

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### *Landec Ag*

Landec Ag revenues consist of revenues generated from the sale of hybrid seed corn to farmers under the Fielder's Choice Direct<sup>®</sup> brand and from the sale of Intellicoat coated corn and soybean seeds to farmers and seed companies. Virtually all of Landec Ag's revenues are generated during the Company's third and fourth quarters.

The change in revenues at Landec Ag during the three and six months ended November 27, 2005 compared to the same periods last year was not material to consolidated Landec revenues.

### *Corporate*

Corporate revenues consist of revenues generated from partnering with others under research and development agreements and supply agreements and from fees for licensing our proprietary Intelimer technology to others and from the corresponding royalties from these license agreements.

The increase in Corporate revenues for the three and six months ended November 27, 2005 compared to the same periods of the prior year was not material to consolidated Landec revenues.

### **Gross Profit** (in thousands):

	<i>Three months ended 11/27/05</i>	<i>Three months ended 11/28/04</i>	<i>Change</i>	<i>Six months ended 11/27/05</i>	<i>Six months ended 11/28/04</i>	<i>Change</i>
<i>Apio Value Added</i>	\$ 5,488	\$ 4,767	15%	\$ 11,002	\$ 9,237	19%
<i>Apio Trading</i>	1,321	1,098	20%	2,266	2,283	(1%)
<i>Apio Tech</i>	60	□	N/M	62	□	N/M
<i>Total Apio</i>	6,869	5,865	17%	13,330	11,520	16%
<i>Landec Ag</i>	19	76	(75%)	19	96	(80%)
<i>Corporate</i>	201	55	265%	330	120	175%
<b>Total Gross Profit</b>	<b>\$ 7,089</b>	<b>\$ 5,996</b>	<b>18%</b>	<b>\$ 13,329</b>	<b>\$ 11,736</b>	<b>14%</b>

### *General*

There are numerous factors that can influence gross profits including product mix, customer mix, manufacturing costs, volume, sale discounts and charges for excess or obsolete inventory, to name a few. Many of these factors influence or are interrelated with other factors. Therefore, it is difficult to precisely quantify the impact of each item individually. The Company includes in cost of sales all the costs related to the sale of products in accordance with generally accepted accounting principles. These costs include the following: raw materials (including produce, seeds and packaging), direct labor, overhead (including indirect labor, depreciation, and facility related costs) and shipping and shipping related costs. The following discussion surrounding gross profits includes management's best estimates of the reasons for the changes for the three and six months ended November 27, 2005, compared to the same periods last year as outlined in the table above.

### *Apio Value-Added*

The increase in gross profits for Apio's value-added specialty packaged vegetable business for the three and six months ended November 27, 2005 compared to the same periods last year was due to (1) the increase in value-added sales which increased 6% for the quarter and 9% for the first six months of fiscal year 2006, (2) product mix changes to higher margin products and (3) improved processing yields and operational efficiencies driven largely by improved raw material quality during the first half of fiscal year 2006 compared to the same period last year.

### *Apio Trading*

Apio's trading business is a buy/sell business that realizes a commission-based margin in the 4-6% range. The increase in gross profits during the three months ended November 27, 2005 compared to the same period last year was primarily due to a 5% increase in trading revenues and a mix change to higher margin vegetable exports

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from lower margin fruit exports. For the six months ended November 27, 2005, trading margins were virtually unchanged from the same period last year due to revenues being virtually flat.

*Apio Tech, Landec Ag and Corporate*

The change in gross profits for Apio Tech, Landec Ag and Corporate for the three and six months ended November 27, 2005 compared to the same periods last year was not material to consolidated Landec gross profits.

**Operating Expenses** (in thousands):

	<i>Three months ended 11/27/05</i>	<i>Three months ended 11/24/04</i>	<i>Change</i>	<i>Six months ended 11/27/05</i>	<i>Six months ended 11/28/04</i>	<i>Change</i>
<b>Research and Development:</b>						
<i>Apio</i>	\$ 275	\$ 255	8%	\$ 541	\$ 543	0%
<i>Landec Ag</i>	154	192	(20%)	307	418	(27%)
<i>Corporate</i>	391	238	64%	731	528	38%
<b>Total R&amp;D</b>	\$ 820	\$ 685	20%	\$ 1,579	\$ 1,489	6%
<b>Selling, General and Administrative:</b>						
<i>Apio</i>	\$ 3,497	\$ 3,346	5%	\$ 6,918	\$ 6,498	6%
<i>Landec Ag</i>	2,587	1,849	40%	4,216	3,369	25%
<i>Corporate</i>	1,070	751	42%	2,201	1,454	51%
<b>Total S,G&amp;A</b>	\$ 7,154	\$ 5,946	20%	\$ 13,335	\$ 11,321	18%

*Research and Development*

Landec's research and development expenses consist primarily of expenses involved in the development and process scale-up initiatives. Research and development efforts at Apio are focused on the Company's proprietary BreatheWay membranes used for packaging produce, with recent focus on extending the shelf life of bananas and other shelf-life sensitive vegetables and fruit. At Landec Ag, the research and development efforts are focused on the Company's proprietary Intellicoat coatings for seeds, primarily corn seed. At Corporate, the research and development efforts are focused on uses for the proprietary Intelimer polymers outside of food and agriculture.

The increase in research and development expenses for the three months and six months ended November 27, 2005 compared to the same periods last year was primarily due to higher research and development expenses at Corporate associated with a greater emphasis on developing strategic collaborations with corporate partners.

*Selling, General and Administrative*

Selling, general and administrative expenses consist primarily of sales and marketing expenses associated with Landec's product sales and services, business development expenses and staff and administrative expenses.

The increase in selling, general and administrative expenses for the three months and six months ended November 27, 2005 compared to the same periods last year was primarily due to (1) increases in selling and marketing expenses at Apio and Landec Ag to generate increases in revenues, (2) selling, general and administrative expenses of \$529,000 at Heartland Hybrids which was acquired at the beginning of our fiscal second quarter, (3) accrued bonuses at Apio and Corporate based on meeting or beating our plan which is currently being exceeded (whereas in the prior fiscal year, bonuses were not recorded until the end of the fiscal year due to uncertainty) and (4) an increase in general and administrative expenses at Corporate for business development consulting fees, legal fees and Sarbanes-Oxley related accounting fees.

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**Other** (in thousands):

	<i>Three months ended 11/27/05</i>	<i>Three months ended 11/28/04</i>	<i>Change</i>	<i>Six months ended 11/27/05</i>	<i>Six months ended 11/28/04</i>	<i>Change</i>
<b>Interest Income</b>	\$ 130	\$ 9	N/M	\$ 250	\$ 19	N/M
<b>Interest Expense</b>	(177)	(87)	103%	(250)	(205)	22%
<b>Minority Int. Exp.</b>	(101)	(124)	(19%)	(316)	(276)	14%
<b>Other Expense</b>	(4)	29	N/M	(7)	36	N/M
<b>Total Other</b>	\$ (152)	\$ (173)	(12%)	\$ (323)	\$ (426)	(24%)

*Interest Income*

The increase in interest income for the three and six month periods ended November 27, 2005 compared to the same periods last year was due to the increase in cash available for investing.

*Interest Expense*

The increase in interest expense during the three and six months ended November 27, 2005 compared to the same periods last year was due to Landec Ag drawing on its line of credit earlier this year than in the prior year as a result of the acquisition of Heartland Hybrids on August 29, 2005.

*Minority Interest Expense*

The minority interest expense consists of the minority interest associated with the limited partners' equity interest in the net income of Apio Cooling, LP.

The decrease in the minority interest for the three months ended November 27, 2005 compared to the same period of last year was due to lower sales volumes and thus lower profits generated from Apio Cooling during this year compared to the prior year. The increase in the minority interest for the six months ended November 27, 2005 compared to the same period last year was due to higher volumes and profits during our first fiscal quarter.

*Other Expense*

Other consists of non-operating income and expenses.

**Liquidity and Capital Resources**

As of November 27, 2005, the Company had cash and cash equivalents of \$6.5 million, a net decrease of \$6.4 million from \$12.9 million at May 29, 2005.

*Cash Flow from Operating Activities*

Landec used \$10.0 million of cash flow in operating activities during the six months ended November 27, 2005 compared to using \$1.9 million from operating activities for the six months ended November 28, 2004. The primary source of cash during the six months ended November 27, 2005 was an increase in deferred revenue of \$2.5 million as a result of cash deposits for future seed corn shipments. The primary uses of cash in operating activities were from the purchase of seed corn inventory by Landec Ag of \$7.4 million, an increase in inventory at Apio of \$1.3 million primarily related to export inventory in transit and an increase in accounts receivable of \$2.6 million at Apio due to the increase in revenues.

*Cash Flow from Investing Activities*

Net cash used in investing activities for the six months ended November 27, 2005 was \$3.0 million compared to \$1.9 million for the same period last year. The primary source of cash from investing activities during the six months ended November 27, 2005 was from the net maturities of \$2.0 million of marketable securities. The

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primary uses of cash for investing activities during the first six months of fiscal year 2006 were for the purchase of the assets of Heartland Hybrids of \$3.6 million and the purchase of \$1.5 million of property and equipment primarily for the further automation of Apio's value-added facility.

### *Cash Flow from Financing Activities*

Net cash provided by financing activities for the six months ended November 27, 2005 was \$6.6 million compared to net cash provided by financing activities of \$3.6 million for the same period last year. The cash provided by financing activities during the first six months of fiscal year 2005 was primarily the net borrowings under Landec Ag's line of credit of \$7.3 million for the purchase of seed corn to be sold during the Company's third and fourth fiscal quarters.

### *Capital Expenditures*

During the six months ended November 27, 2005, Landec purchased vegetable processing equipment to support the expansion of Apio's value added business. These expenditures represented the majority of the \$1.5 million of equipment purchased.

### *Debt*

On November 1, 2005, Apio amended its revolving line of credit that was scheduled to expire on August 31, 2006, with Wells Fargo Bank N.A. The line was reduced from \$10.0 million to \$7.0 million and outstanding amounts under the line of credit now bear interest at either the prime rate less .25% or the LIBOR adjustable rate plus 1.75% (5.96% at November 27, 2005). The revolving line of credit, the equipment line of credit and the term note with Wells Fargo (collectively, the "Loan Agreement") contains certain restrictive covenants, which require Apio to meet certain financial tests, including minimum levels of net income, maximum leverage ratio, minimum net worth and maximum capital expenditures. Landec has pledged substantially all of the assets of Apio to secure the lines with Wells Fargo. At November 27, 2005, no amounts were outstanding under the revolving line of credit or the equipment line of credit. Apio has been in compliance with all loan covenants in the Loan Agreement since the inception of this loan.

Landec Ag has a revolving line of credit which allows for borrowings of up to \$7.5 million, based on Landec Ag's inventory levels. The interest rate on the revolving line of credit is the prime rate plus 0.375% (7.375% at November 27, 2005). The line of credit contains certain restrictive covenants, which, among other things, restrict the ability of Landec Ag to make payments on debt owed by Landec Ag to Landec. Landec Ag was in compliance with all of the loan covenants during the first six months of fiscal year 2006. Landec has pledged substantially all of the assets of Landec Ag to secure the line of credit. At November 27, 2005, \$7.3 million was outstanding under Landec Ag's revolving line of credit.

At November 27, 2005, Landec's total debt, including current maturities and capital lease obligations, was \$9.4 million and the total debt to equity ratio was 13% compared to 4% at May 29, 2005. This debt was comprised of borrowing under Landec Ag's line of credit of \$7.3 million and term debt and capital lease obligations of \$2.1 million, \$2.0 million of which is mortgage debt on Apio's manufacturing facilities. The amount of debt outstanding on the Company's revolving lines of credit fluctuates over time. Borrowings on Landec's lines of credit are expected to vary with seasonal requirements of the Company's businesses.

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*Contractual Obligation*

The Company's material contractual obligations for the next five years and thereafter as of November 27, 2005, are as follows (in thousands):

Obligation	Due in Fiscal Year Ended May						
	Total	Remainder of 2006	2007	2008	2009	2010	Thereafter
Lines of Credit	\$ 7,272	\$ 7,272	\$ —	\$ —	\$ —	\$ —	\$ —
Long-term Debt	2,082	116	114	122	130	138	1,462
Capital Leases	61	13	22	23	3	—	—
Interest Expense	1,195	197	133	124	114	105	522
Operating Leases	1,995	295	587	653	285	172	3
Licensing Obligation	650	50	100	100	100	100	200
Purchase Commitments	205	205	—	—	—	—	—
Total	<u>\$ 13,460</u>	<u>\$ 8,148</u>	<u>\$ 956</u>	<u>\$ 1,022</u>	<u>\$ 632</u>	<u>\$ 515</u>	<u>\$ 2,187</u>

Interest expense was determined based on the assumption that the Company's lines of credit will have an average daily outstanding balance of \$1.0 million at an annual interest rate of 6.0% for fiscal year 2006 and no borrowings thereafter. The interest expense on long term notes and lease obligations is based on the payment schedules and interest rates from the relevant agreements.

Landec is not a party to any agreements with, or commitments to, any special purpose entities that would constitute material off-balance sheet financing other than the operating lease commitments listed above.

Landec's future capital requirements will depend on numerous factors, including the progress of its research and development programs; the development of commercial scale manufacturing capabilities; the development of marketing, sales and distribution capabilities; the ability of Landec to establish and maintain new collaborative and licensing arrangements; any decision to pursue additional acquisition opportunities; weather conditions that can affect the supply and price of produce, the timing and amount, if any, of payments received under licensing and research and development agreements; the costs involved in preparing, filing, prosecuting, defending and enforcing intellectual property rights; the ability to comply with regulatory requirements; the emergence of competitive technology and market forces; the effectiveness of product commercialization activities and arrangements; and other factors. If Landec's currently available funds, together with the internally generated cash flow from operations are not sufficient to satisfy its capital needs, Landec would be required to seek additional funding through other arrangements with collaborative partners, additional bank borrowings and public or private sales of its securities. There can be no assurance that additional funds, if required, will be available to Landec on favorable terms if at all.

Landec believes that its debt facilities, cash from operations, along with existing cash, cash equivalents and existing borrowing capacities will be sufficient to finance its operational and capital requirements through at least the next twelve months.

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### **Additional Factors That May Affect Future Results**

Landec desires to take advantage of the “Safe Harbor” provisions of the Private Securities Litigation Reform Act of 1995 and of Section 21E and Rule 3b-6 under the Securities Exchange Act of 1934. Specifically, Landec wishes to alert readers that the following important factors, as well as other factors including, without limitation, those described elsewhere in this report, could in the future affect, and in the past have affected, Landec’s actual results and could cause Landec’s results for future periods to differ materially from those expressed in any forward-looking statements made by or on behalf of Landec. Landec assumes no obligation to update such forward-looking statements.

### ***Our Future Operating Results Are Likely to Fluctuate Which May Cause Our Stock Price to Decline***

In the past, our results of operations have fluctuated significantly from quarter to quarter and are expected to continue to fluctuate in the future. Historically, our direct marketer of hybrid corn seed, Landec Ag, has been the primary source of these fluctuations, as its revenues and profits are concentrated over a few months during the spring planting season (generally during our third and fourth fiscal quarters). In addition, Apio can be heavily affected by seasonal and weather factors which have impacted quarterly results, such as the high cost of sourcing product in December 2003, January 2004 and March/April 2005 due to a shortage of essential value-added produce items. Our earnings may also fluctuate based on our ability to collect accounts receivables from customers and note receivables from growers. Our earnings from our Food Products Technology business are sensitive to price fluctuations in the fresh vegetables and fruits markets. Excess supplies can cause intense price competition. Other factors that affect our food and/or agricultural operations include:

- the seasonality of our supplies;
- our ability to process produce during critical harvest periods;
- the timing and effects of ripening;
- the degree of perishability;
- the effectiveness of worldwide distribution systems;
- total worldwide industry volumes;
- the seasonality of consumer demand;
- foreign currency fluctuations; and
- foreign importation restrictions and foreign political risks.

As a result of these and other factors, we expect to continue to experience fluctuations in quarterly operating results.

### ***We May Not Be Able to Achieve Acceptance of Our New Products in the Marketplace***

Our success in generating significant sales of our products will depend in part on the ability of us and our partners and licensees to achieve market acceptance of our new products and technology. The extent to which, and rate at which, we achieve market acceptance and penetration of our current and future products is a function of many variables including, but not limited to:

- price;
- safety;
- efficacy;
- reliability;
- conversion costs;

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- marketing and sales efforts; and
- general economic conditions affecting purchasing patterns.

We may not be able to develop and introduce new products and technologies in a timely manner or new products and technologies may not gain market acceptance. We are in the early stage of product commercialization of certain Intelimer-based specialty packaging, Intellicoat seed coatings and other Intelimer polymer products and many of our potential products are in development. We believe that our future growth will depend in large part on our ability to develop and market new products in our target markets and in new markets. In particular, we expect that our ability to compete effectively with existing food products, agricultural, industrial and medical companies will depend substantially on successfully developing, commercializing, achieving market acceptance of and reducing the cost of producing our products. In addition, commercial applications of our temperature switch polymer technology are relatively new and evolving. Our failure to develop new products or the failure of our new products to achieve market acceptance would have a material adverse effect on our business, results of operations and financial condition.

### ***We Face Strong Competition in the Marketplace***

Competitors may succeed in developing alternative technologies and products that are more effective, easier to use or less expensive than those which have been or are being developed by us or that would render our technology and products obsolete and non-competitive. We operate in highly competitive and rapidly evolving fields, and new developments are expected to continue at a rapid pace. Competition from large food products, agricultural, industrial and medical companies is expected to be intense. In addition, the nature of our collaborative arrangements may result in our corporate partners and licensees becoming our competitors. Many of these competitors have substantially greater financial and technical resources and production and marketing capabilities than we do, and may have substantially greater experience in conducting clinical and field trials, obtaining regulatory approvals and manufacturing and marketing commercial products.

### ***We Have a Concentration of Manufacturing in One Location for Apio and May Have to Depend on Third Parties to Manufacture Our Products***

Any disruptions in our primary manufacturing operation would reduce our ability to sell our products and would have a material adverse effect on our financial results. Additionally, we may need to consider seeking collaborative arrangements with other companies to manufacture our products. If we become dependent upon third parties for the manufacture of our products, our profit margins and our ability to develop and deliver those products on a timely basis may be affected. Failures by third parties may impair our ability to deliver products on a timely basis and impair our competitive position. We may not be able to continue to successfully operate our manufacturing operations at acceptable costs, with acceptable yields, and retain adequately trained personnel.

### ***Our Dependence on Single-Source Suppliers and Service Providers May Cause Disruption in Our Operations Should Any Supplier Fail to Deliver Materials***

We may experience difficulty acquiring materials or services for the manufacture of our products or we may not be able to obtain substitute vendors. We may not be able to procure comparable materials or hybrid corn varieties at similar prices and terms within a reasonable time. Several services that are provided to Apio are obtained from a single provider. Several of the raw materials we use to manufacture our products are currently purchased from a single source, including some monomers used to synthesize Intelimer polymers and substrate materials for our breathable membrane products. In addition, a majority of the hybrid corn varieties sold by Landec Ag are grown under contract by a single seed producer. Any interruption of our relationship with single-source suppliers or service providers could delay product shipments and materially harm our business.

### ***We May Be Unable to Adequately Protect Our Intellectual Property Rights***

We may receive notices from third parties, including some of our competitors, claiming infringement by our products of patent and other proprietary rights. Regardless of their merit, responding to any such claim could be time-consuming, result in costly litigation and require us to enter royalty and licensing agreements which may not be offered



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or available on terms acceptable to us. If a successful claim is made against us and we fail to develop or license a substitute technology, we could be required to alter our products or processes and our business, results of operations or financial position could be materially adversely affected. Our success depends in large part on our ability to obtain patents, maintain trade secret protection and operate without infringing on the proprietary rights of third parties. Any pending patent applications we file may not be approved and we may not be able to develop additional proprietary products that are patentable. Any patents issued to us may not provide us with competitive advantages or may be challenged by third parties. Patents held by others may prevent the commercialization of products incorporating our technology. Furthermore, others may independently develop similar products, duplicate our products or design around our patents.

### ***Our Operations Are Subject to Regulations that Directly Impact Our Business***

Our food packaging products are subject to regulation under the Food, Drug and Cosmetic Act (the “FDC Act”). Under the FDC Act, any substance that when used as intended may reasonably be expected to become, directly or indirectly, a component or otherwise affect the characteristics of any food may be regulated as a food additive unless the substance is generally recognized as safe. We believe that food packaging materials are generally not considered food additives by the FDA because these products are not expected to become components of food under their expected conditions of use. We consider our breathable membrane product to be a food packaging material not subject to regulation or approval by the FDA. We have not received any communication from the FDA concerning our breathable membrane product. If the FDA were to determine that our breathable membrane products are food additives, we may be required to submit a food additive petition for approval by the FDA. The food additive petition process is lengthy, expensive and uncertain. A determination by the FDA that a food additive petition is necessary would have a material adverse effect on our business, operating results and financial condition.

Federal, state and local regulations impose various environmental controls on the use, storage, discharge or disposal of toxic, volatile or otherwise hazardous chemicals and gases used in some of the manufacturing processes. Our failure to control the use of, or to restrict adequately the discharge of, hazardous substances under present or future regulations could subject us to substantial liability or could cause our manufacturing operations to be suspended and changes in environmental regulations may impose the need for additional capital equipment or other requirements.

Our agricultural operations are subject to a variety of environmental laws including, the Food Quality Protection Act of 1966, the Clean Air Act, the Clean Water Act, the Resource Conservation and Recovery Act, the Federal Insecticide, Fungicide and Rodenticide Act, and the Comprehensive Environmental Response, Compensation and Liability Act. Compliance with these laws and related regulations is an ongoing process. Environmental concerns are, however, inherent in most agricultural operations, including those we conduct. Moreover, it is possible that future developments, such as increasingly strict environmental laws and enforcement policies could result in increased compliance costs.

The Company is subject to the Perishable Agricultural Commodities Act (“PACA”) law. PACA regulates fair trade standards in the fresh produce industry and governs all the products sold by Apio. Our failure to comply with the PACA requirements could among other things, result in civil penalties, suspension or revocation of a license to sell produce, and in the most egregious cases, criminal prosecution, which could have a material adverse affect on our business.

### ***Adverse Weather Conditions and Other Acts of God May Cause Substantial Decreases in Our Sales and/or Increases in Our Costs***

Our Food Products and Agricultural Seed Technology businesses are subject to weather conditions that affect commodity prices, crop yields, and decisions by growers regarding crops to be planted. Crop diseases and severe conditions, particularly weather conditions such as floods, droughts, frosts, windstorms, earthquakes and hurricanes, may adversely affect the supply of vegetables and fruits used in our business, which could reduce the sales volumes and/or increase the unit production costs. Because a significant portion of the costs are fixed and contracted in advance of each operating year, volume declines due to production interruptions or other factors could result in increases in unit production costs which could result in substantial losses and weaken our financial condition.

***We Depend on Strategic Partners and Licenses for Future Development***

Our strategy for development, clinical and field testing, manufacture, commercialization and marketing for some of our current and future products includes entering into various collaborations with corporate partners, licensees and others. We are dependent on our corporate partners to develop, test, manufacture and/or market some of our products. Although we believe that our partners in these collaborations have an economic motivation to succeed in performing their contractual responsibilities, the amount and timing of resources to be devoted to these activities are not within our control. Our partners may not perform their obligations as expected or we may not derive any additional revenue from the arrangements. Our partners may not pay any additional option or license fees to us or may not develop, market or pay any royalty fees related to products under the agreements. Moreover, some of the collaborative agreements provide that they may be terminated at the discretion of the corporate partner, and some of the collaborative agreements provide for termination under other circumstances. In addition, we may not receive any royalties on future sales of the PORT™ product because in the related agreement we have no control over commercializing the product or generating revenues from the sales of the product. Our partners may pursue existing or alternative technologies in preference to our technology. Furthermore, we may not be able to negotiate additional collaborative arrangements in the future on acceptable terms, if at all, and our collaborative arrangements may not be successful.

***Both Domestic and Foreign Government Regulations Can Have an Adverse Effect on Our Business Operations***

Our products and operations are subject to governmental regulation in the United States and foreign countries. The manufacture of our products is subject to periodic inspection by regulatory authorities. We may not be able to obtain necessary regulatory approvals on a timely basis or at all. Delays in receipt of or failure to receive approvals or loss of previously received approvals would have a material adverse effect on our business, financial condition and results of operations. Although we have no reason to believe that we will not be able to comply with all applicable regulations regarding the manufacture and sale of our products and polymer materials, regulations are always subject to change and depend heavily on administrative interpretations and the country in which the products are sold. Future changes in regulations or interpretations relating to matters such as safe working conditions, laboratory and manufacturing practices, environmental controls, and disposal of hazardous or potentially hazardous substances may adversely affect our business.

We are subject to USDA rules and regulations concerning the safety of the food products handled and sold by Apio, and the facilities in which they are packed and processed. Failure to comply with the applicable regulatory requirements can, among other things, result in:

- fines, injunctions, civil penalties, and suspensions,
- withdrawal of regulatory approvals,
- product recalls and product seizures, including cessation of manufacturing and sales,
- operating restrictions, and
- criminal prosecution.

We may be required to incur significant costs to comply with the laws and regulations in the future which may have a material adverse effect on our business, operating results and financial condition.

***Our International Operations and Sales May Expose Our Business to Additional Risks***

For the six months ended November 27, 2005, approximately 35% of our total revenues were derived from product sales to international customers. A number of risks are inherent in international transactions. International sales and operations may be limited or disrupted by any of the following:

- regulatory approval process,
- government controls,
- export license requirements,

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- political instability,
- price controls,
- trade restrictions,
- changes in tariffs, or
- difficulties in staffing and managing international operations.

Foreign regulatory agencies have or may establish product standards different from those in the United States, and any inability to obtain foreign regulatory approvals on a timely basis could have a material adverse effect on our international business, and our financial condition and results of operations. While our foreign sales are currently priced in dollars, fluctuations in currency exchange rates, may reduce the demand for our products by increasing the price of our products in the currency of the countries to which the products are sold. Regulatory, geopolitical and other factors may adversely impact our operations in the future or require us to modify our current business practices.

### ***Cancellations or Delays of Orders by Our Customers May Adversely Affect Our Business***

During the first six months of fiscal year 2006, sales to our top five customers accounted for approximately 47% of our revenues, with our largest customers, Costco Wholesale Corp. and Pomina Enterprise Co. LTD, accounting for approximately 15% and 11%, respectively of our revenues. We expect that, for the foreseeable future, a limited number of customers may continue to account for a substantial portion of our net revenues. We may experience changes in the composition of our customer base, as Apio and Landec Ag have experienced in the past. We do not have long-term purchase agreements with any of our customers. The reduction, delay or cancellation of orders from one or more major customers for any reason or the loss of one or more of our major customers could materially and adversely affect our business, operating results and financial condition. In addition, since some of the products processed by Apio at its Guadalupe, California facility are sole sourced to its customers, our operating results could be adversely affected if one or more of our major customers were to develop other sources of supply. Our current customers may not continue to place orders, orders by existing customers may be canceled or may not continue at the levels of previous periods or we may not be able to obtain orders from new customers.

### ***Our Sale of Some Products May Increase Our Exposure to Product Liability Claims***

The testing, manufacturing, marketing, and sale of the products we develop involves an inherent risk of allegations of product liability. If any of our products were determined or alleged to be contaminated or defective or to have caused a harmful accident to an end-customer, we could incur substantial costs in responding to complaints or litigation regarding our products and our product brand image could be materially damaged. Either event may have a material adverse effect on our business, operating results and financial condition. Although we have taken and intend to continue to take what we believe are appropriate precautions to minimize exposure to product liability claims, we may not be able to avoid significant liability. We currently maintain product liability insurance with limits in the amount of \$41.0 million per occurrence and \$42.0 million in the annual aggregate. Our coverage may not be adequate or may not continue to be available at an acceptable cost, if at all. A product liability claim, product recall or other claim with respect to uninsured liabilities or in excess of insured liabilities could have a material adverse effect on our business, operating results and financial condition.

### ***Our Stock Price May Fluctuate in Accordance with Market Conditions***

Over the past several years the stock market has experienced extreme price and volume fluctuations. The following events may cause the market price of our common stock to fluctuate significantly:

- technological innovations applicable to our products,
- our attainment of (or failure to attain) milestones in the commercialization of our technology,
- our development of new products or the development of new products by our competitors,
- new patents or changes in existing patents applicable to our products,
- our acquisition of new businesses or the sale or disposal of a part of our businesses,

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- development of new collaborative arrangements by us, our competitors or other parties,
- changes in government regulations applicable to our business,
- changes in investor perception of our business,
- fluctuations in our operating results and
- changes in the general market conditions in our industry.

These broad fluctuations may adversely affect the market price of our common stock.

### ***Since We Order Cartons and Film for Our Products from Suppliers in Advance of Receipt of Customer Orders for Such Products, We Could Face a Material Inventory Risk***

As part of our inventory planning, we enter into negotiated orders with vendors of cartons and film used for packing our products in advance of receiving customer orders for such products. Accordingly, we face the risk of ordering too many cartons and film since orders are generally based on forecasts of customer orders rather than actual orders. If we cannot change or be released from the orders, we may incur costs as a result of inadequately predicting cartons and film orders in advance of customer orders. Because of this, we may currently have an oversupply of cartons and film and face the risk of not being able to sell such inventory and our anticipated reserves for losses may be inadequate if we have misjudged the demand for our products. Our business and operating results could be adversely affected as a result of these increased costs.

### ***Our Seed Products May Fail to Germinate Properly and We May Be Subject to Claims for Reimbursement or Damages for Losses from Customers Who Use Such Products***

Farmers plant seed products sold by Landec Ag with the expectation that they will germinate under normal growing conditions. If our seed products do not germinate at the appropriate time or fail to germinate at all, our customers may incur significant crop losses and seek reimbursement or bring claims against us for such damages. Although insurance is generally available to cover such claims, the costs for premiums of such policies are prohibitively expensive and we currently do not maintain such insurance. Any claims brought for failure of our seed products to properly germinate could materially and adversely affect our operating and financial results.

### ***Recently Enacted Changes in Securities Laws and Regulations Are Likely to Increase Our Costs***

The Sarbanes-Oxley Act of 2002 (the "Act") that became law in July 2002 requires changes in some of our corporate governance, public disclosure and compliance practices. In addition, Nasdaq has made revisions to its requirements for companies, such as Landec, that are listed on the NASDAQ. We expect these developments to increase our legal and financial compliance costs. These changes could make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to accept reduced coverage or incur substantially higher costs to obtain coverage. These developments could make it more difficult for us to attract and retain qualified members for our board of directors, particularly to serve on our audit committee.

### ***Our Controlling Shareholders Exert Significant Influence over Corporate Events that May Conflict with the Interests of Other Shareholders***

Our executive officers and directors and their affiliates own or control approximately 25% of our common stock (including options exercisable within 60 days). Accordingly, these officers, directors and shareholders may have the ability to exert significant influence over the election of our Board of Directors, the approval of amendments to our articles and bylaws and the approval of mergers or other business combination transactions requiring shareholder approval. This concentration of ownership may have the effect of delaying or preventing a merger or other business combination transaction, even if the transaction or amendments would be beneficial to our other shareholders. In addition, our controlling shareholders may approve amendments to our articles or bylaws to implement anti-takeover or management friendly provisions that may not be beneficial to our other shareholders.

***Terrorist Attacks and Risk of Contamination May Negatively Impact All Aspects of Our Operations, Revenues, Costs and Stock Price***

The September 2001 terrorist attacks in the United States, as well as future events occurring in response or connection to them, including, future terrorist attacks against United States targets, rumors or threats of war, actual conflicts involving the United States or its allies, or trade disruptions impacting our domestic suppliers or our customers, may impact our operations and may, among other things, cause decreased sales of our products. More generally, these events have affected, and are expected to continue to affect, the general economy and customer demand for our products. While we do not believe that our employees, facilities, or products are a target for terrorists, there is a remote risk that terrorist activities could result in contamination or adulteration of our products. Although we have systems and procedures in place that are designed to prevent contamination and adulteration of our products, a disgruntled employee or third party could introduce an infectious substance into packages of our products, either at our manufacturing plants or during shipment of our products. Were our products to be tampered with, we could experience a material adverse effect in our business, operations and financial condition.

***We May Be Exposed to Employment Related Claims and Costs that Could Materially Adversely Affect Our Business***

We have been subject in the past, and may be in the future, to claims by employees based on allegations of discrimination, negligence, harassment and inadvertent employment of illegal aliens or unlicensed personnel, and we may be subject to payment of workers' compensation claims and other similar claims. We could incur substantial costs and our management could spend a significant amount of time responding to such complaints or litigation regarding employee claims, which may have a material adverse effect on our business, operating results and financial condition.

***We Are Dependent on Our Key Employees and if One or More of Them Were to Leave, We Could Experience Difficulties in Replacing Them and Our Operating Results Could Suffer***

The success of our business depends to a significant extent upon the continued service and performance of a relatively small number of key senior management, technical, sales, and marketing personnel. The loss of any of our key personnel would likely harm our business. In addition, competition for senior level personnel with knowledge and experience in our different lines of business is intense. If any of our key personnel were to leave, we would need to devote substantial resources and management attention to replace them. As a result, management attention may be diverted from managing our business, and we may need to pay higher compensation to replace these employees.

***We May Have to Pursue New Financings if We Are Unable to Comply with Provisions in Our Loan Agreements in the Future***

Apio is subject to various financial and operating covenants under the Wells Fargo Bank loan agreement, including minimum levels of net income, maximum leverage ratio, minimum net worth and maximum capital expenditures. The Wells Fargo Bank loan agreement limits the ability of Apio to make cash payments to Landec. If we violate any obligations under the loan agreement in the future, we could trigger an event of default, which, if not cured or waived, would permit acceleration of our obligation to repay the indebtedness due under the loan agreement. If the indebtedness due under the loan agreement were accelerated, we would be forced to pursue one or more alternative strategies such as selling assets, seeking new debt financing from another lender or seeking additional equity capital, which might not be achievable or available on attractive terms, if at all, and which could substantially dilute the ownership interest of existing shareholders.

***We May Issue Preferred Stock with Preferential Rights that Could Affect Your Rights***

Our Board of Directors has the authority, without further approval of our shareholders, to fix the rights and preferences, and to issue shares, of preferred stock. In November 1999, we issued and sold shares of Series A Convertible Preferred Stock and in October 2001 we issued and sold shares of Series B Convertible Preferred Stock. The Series A Convertible Preferred Stock was converted into 1,666,670 shares of Common Stock on November 19, 2002 and the Series B Convertible Preferred Stock was converted into 1,744,102 shares of Common Stock on May 7, 2004.

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The issuance of new shares of preferred stock could have the effect of making it more difficult for a third party to acquire a majority of our outstanding stock, and the holders of such preferred stock could have voting, dividend, liquidation and other rights superior to those of holders of our Common Stock.

***We Have Never Paid any Dividends on Our Common Stock***

We have not paid any cash dividends on our Common Stock since inception and do not expect to do so in the foreseeable future. Any dividends may be subject to preferential dividends payable on any preferred stock we may issue.

***Our Profitability Could Be Materially And Adversely Affected if it Is Determined that the Book Value of Goodwill is Higher than Fair Value***

Our balance sheet includes an amount designated as “goodwill” that represents a portion of our assets and our shareholders’ equity. Goodwill arises when an acquirer pays more for a business than the fair value of the tangible and separately measurable intangible net assets. Under Statement of Financial Accounting Standards No. 142 “Goodwill and Other Intangible Assets”, beginning in fiscal year 2002, the amortization of goodwill has been replaced with an “impairment test” which requires that we compare the fair value of goodwill to its book value at least annually and more frequently if circumstances indicate a possible impairment. If we determine at any time in the future that the book value of goodwill is higher than fair value then the difference must be written-off, which could materially and adversely affect our profitability.

**Item 3. Quantitative and Qualitative Disclosures about Market Risk**

The following table presents information about the Company's debt obligations and derivative financial instruments that are sensitive to changes in interest rates. The table presents principal amounts and related weighted average interest rates by year of expected maturity for the Company's debt obligations. The carrying value of the Company's debt obligations approximates the fair value of the debt obligations as of November 27, 2005.

	Remainder of 2006	2007	2008	2009	2010	There- after	Total
<b>Liabilities (in 000's)</b>							
Lines of Credit	\$7,272	\$ —	\$ —	\$ —	\$ —	\$ —	\$7,272
Avg. Int. Rate	4.88%						4.88%
Long term debt, including current portion							
Variable Rate	\$ 129	\$ 136	\$ 145	\$ 133	\$ 138	\$1,462	\$2,143
Avg. Int. Rate	6.58%	6.59%	6.59%	6.59%	6.59%	6.59%	6.59%

**Item 4. Controls and Procedures**

- (a) Based on their evaluation as of the end of the period covered by this Quarterly Report on Form 10-Q (the "Evaluation Date"), Landec's principal executive officer and principal financial officer concluded that, as of the Evaluation Date, Landec's 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"), were effective and designed to ensure that information required to be disclosed by Landec in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms.
- (b) There was no change in Landec's internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, such internal control over financial reporting.

**PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

None.

**Item 1A. Risk Factors**

Not applicable.

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

Pursuant to the Asset Purchase Agreement dated June 29, 2005, the Company on August 29, 2005 issued to the former owners of Heartland Hybrids, Inc. 152,186 shares of Common Stock valued at \$960,000.

The issuance of securities in this Item 2 was deemed to be exempt from registration under the Securities Act of 1933, as amended (the "Act"), in reliance on Section 4(2) of the Act as a transaction by an issuer not involving any public offering. The recipients of the securities in such transaction represented their intention to acquire the securities for investment only and not with a view to or for sale in connection with any distribution thereof and also represented that each is an "accredited investor" with the meaning of Rule 501(a) of Regulation D under the Act. Appropriate legends were affixed to the securities issued in such transaction. The recipients were given adequate access to information about the Company.

**Item 3. Defaults Upon Senior Securities**

None.

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

At the Company's Annual Meeting of Shareholders held on October 14, 2005 the following proposals were adopted by the margins indicated:

		Number of Shares	
		Voted For	Withheld
1.	Four Class II directors were elected by the margins indicated to serve for a term of office to expire at the second succeeding annual meeting of shareholders at which their successors will be elected and qualified:		
	Gary T. Steele	20,709,455	574,916
	Nicholas Tompkins	20,726,836	557,535
	Duke Bristow	20,769,836	514,535
	Robert Tobin	20,769,836	514,535
	The Class I directors were not up for election at the Annual Meeting. The four current Class I directors, Frederick Frank, Stephen E. Halprin, Richard S. Schneider, Ph.D., and Kenneth E. Jones will serve as Class I directors until the next Annual Meeting, when their successors will be elected and qualified.		



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		Voted For	Voted Against	Abstain
2.	To approve the Company's Stock Incentive Plan	12,584,534	1,017,790	146,647
3.	To ratify the appointment of Ernst & Young LLP as independent public accountants of the Company for the 2006 fiscal year.	21,201,823	26,512	56,035

**Item 5. Other Information**

None.

**Item 6. Exhibits**

Exhibit Number	Exhibit Title:
10.57+	Amended and Restated Credit Agreement by and among Apio, Inc. as Borrower, and Wells Fargo Bank, National Association, dated as of November 1, 2005.
10.58+	Fifth Amendment to Credit Agreement dated as of October 7, 2004.
10.59+	Sixth Amendment to Credit Agreement dated as of October 7, 2005.
31.1+	CEO Certification pursuant to section 302 of the Sarbanes-Oxley Act of 2002.
31.2+	CFO Certification pursuant to section 302 of the Sarbanes-Oxley Act of 2002.
32.1+	CEO Certification pursuant to section 906 of the Sarbanes-Oxley Act of 2002.
32.2+	CFO Certification pursuant to section 906 of the Sarbanes-Oxley Act of 2002.

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+ Filed herewith.

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

LANDEC CORPORATION

By: /s/ Gregory S. Skinner  
Gregory S. Skinner  
Vice President, Finance and Chief Financial Officer  
(Principal Financial and Accounting Officer)

Date: January 6, 2006

**Exhibit Index**

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+ Filed herewith.

Amended and Restated  
Credit Agreement

by and between

Apio, Inc.,

as Borrower,

and

Wells Fargo Bank, National Association,

as Bank

Dated as of November 1, 2005

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**Amended and Restated  
Credit Agreement**

This Amended and Restated Credit Agreement (this "*Agreement*") is dated and made as of November 1, 2005, by and between Apio, Inc., a Delaware corporation ("*Borrower*"), and Wells Fargo Bank, National Association ("*Bank*"), and amends and restates in its entirety the Credit Agreement, dated as of September 1, 2004 (the "*Original Agreement*"), by and among Borrower, Cal Ex Trading Company, a Delaware corporation, and Bank.

**Recitals**

Whereas, Borrower has requested that Bank extend or continue credit to Borrower as described below, and Bank has agreed to provide such credit to Borrower on the terms and conditions contained herein.

NOW, THEREFORE, for valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Bank and Borrower hereby agree as follows:

**Article I Definitions**

Section 1.1. *Definitions*. For all purposes of this Agreement, except as otherwise expressly provided, the following terms shall have the meanings assigned to them in this Section or in the Section referenced after such term:

"*Acceptable Grower Contract*" means a contract between Borrower and a grower of goods pursuant to which Borrower acquires goods in the ordinary course of business and for which each of the following requirements has been satisfied: (i) a copy of such contract, together with all amendments, modifications, supplements and replacements thereto, has been provided to and approved by Bank, in its reasonable discretion, and (ii) the contract, as amended, modified, supplemented, or replaced, provides that Borrower's obligations to make payment to the related grower shall not be due and payable before the Friday of the fifth (5th) week following the week of delivery of goods to Borrower from such grower.

"*Acceptable Wells Fargo Deposit Account*" has the meaning given in Section 6.10.

"*Account Debtor*" means any Person who is or who may become obligated under, with respect to, or on account of, an Account, chattel paper, or a General Intangible.

"*Accounts*" means all of Borrower's now owned or hereafter acquired right, title, and interest with respect to "accounts" (as that term is defined in the UCC), and any and all supporting obligations in respect thereof.

"*Advance*" means a Line of Credit Advance.



*"Affiliate"* means, as applied to any Person, any other Person who, directly or indirectly, controls, is controlled by, or is under common control with, such Person. For purposes of this definition, "control" means the possession, directly or indirectly, of the power to direct the management and policies of a Person, whether through the ownership of stock, by contract, or otherwise; *provided, however*, that, in any event: (a) any Person which owns directly or indirectly 10% or more of the securities having ordinary voting power for the election of directors or other members of the governing body of a Person or 10% or more of the partnership or other ownership interests of a Person (other than as a limited partner of such Person) shall be deemed to control such Person, (b) each director (or comparable manager) of a Person shall be deemed to be an Affiliate of such Person, and (c) each partnership or joint venture in which a Person is a partner or joint venturer shall be deemed to be an Affiliate of such Person.

*"Agreement"* means this Credit Agreement.

*"Aggregate Stated Amount"* has the meaning given in Section 2.6(c).

*"Apio Cooling"* means Apio Cooling, a California limited partnership.

*"Availability"* means, (i) for any date of determination prior to the Borrowing Base Trigger Date, the Line of Credit Commitment Availability, and (ii) for any date of determination on or after the Borrowing Base Trigger Date, the lesser of (A) the Borrowing Base Availability and (B) the Line of Credit Commitment Availability.

*"Bankruptcy Code"* means the Bankruptcy Reform Act, Title 11 of the United States Code.

*"Borrowing Base"* means, as of any date of determination, (i) 80% of Eligible Accounts, *less*, (ii) the Dilution Reserve, if any, *less*, (iii) the Grower Reserve, if any; *provided* that, Bank may create additional reserves against the Eligible Accounts if it reasonably determines that there has occurred a Material Adverse Effect.

*"Borrowing Base Availability"* means, as of any date of determination, and only if a positive number, the Borrowing Base minus the sum of: (i) the outstanding principal balance of the Line of Credit and (ii) the L/C Amount.

*"Borrowing Base Trigger Date"* means the first date on or after the Closing Date upon which Borrower requests either a Line of Credit Advance or the issuance of a Letter of Credit that would cause, after giving effect to such Line of Credit Advance or Letter of Credit, the sum of the outstanding principal balance of the Line of Credit Advances plus the L/C Amount to equal or exceed Two Million Five Hundred Thousand Dollars (\$2,500,000.00).

*"Business Day"* means any day except a Saturday, Sunday or any other day on which commercial banks in California are authorized or required by law to close.

*"Cal Ex"* means Cal Ex Trading Company, a Delaware corporation, and its permitted successors and assigns.

“*Capital Expenditures*” means for a period, any expenditure of money during such period for the purchase or construction of assets, or for improvements or additions thereto, which are capitalized on Borrower’s balance sheet.

“*Cash Equivalents*” has the meaning set forth in Section 6.7(a).

“*Change of Control*” means the occurrence of any of the following events:

(a) any Person or “group” (as such term is used in Sections 13(d) and 14(d) of the Securities Exchange Act of 1934), other than Parent, is or becomes the “beneficial owner” (as defined in Rules 13d-3 and 13d-5 under the Securities Exchange Act of 1934, except that a Person will be deemed to have “beneficial ownership” of all securities that such Person has the right to acquire, whether such right is exercisable immediately or only after the passage of time), directly or indirectly, of more than twenty-five percent of the voting power of all classes of voting stock of Borrower; or

(b) during any consecutive two-year period, individuals who at the beginning of such period constituted the board of Directors of Borrower (together with any new Directors whose election to such board of Directors, or whose nomination for election by the owners of Borrower, was approved by a vote of 66-2/3% of the Directors then still in office who were either Directors at the beginning of such period or whose election or nomination for election was previously so approved) cease for any reason to constitute a majority of the board of Directors of Borrower then in office.

“*Closing Date*” means November 30, 2005.

“*Collateral*” means (a) “Collateral” as such term is defined in the Security Agreement plus (b) all collateral subject to the Lien of any Security Document other than the Security Agreement.

“*Companies*” means Borrower, Cal Ex and Apio Cooling.

“*Constituent Documents*” means with respect to any Person, as applicable, such Person’s certificate of incorporation, articles of incorporation, by-laws, certificate of formation, articles of organization, limited liability company agreement, management agreement, operating agreement, shareholder agreement, partnership agreement or similar document or agreement governing such Person’s existence, organization or management or concerning disposition of ownership interests of such Person or voting rights among such Person’s owners.

“*Credit Facility*” means the credit facility being made available to Borrower by Bank under Article II hereof.

“*Daily Balance*” means, with respect to each day during the term of this Agreement, the amount of an Obligation owed at the end of such day.

*“Default”* means an event that, with giving of notice or passage of time or both, would constitute an Event of Default.

*“Default Period”* means any period of time beginning on the day a Default or Event of Default occurs and ending on the date that such Default or Event of Default has been cured or waived, as determined by Bank in its sole and absolute discretion.

*“Default Rate”* has the meaning assigned to such term in the Line of Credit Note.

*“Dilution”* means, as of any date of determination, a percentage, based upon the experience of the immediately preceding three months, that is the result of dividing the Dollar amount of bad debt write-downs, returns, rebates, discounts, advertising and other allowances, credits, or other dilutive items with respect to the Accounts during such period, by Borrower’s gross sales during such period (excluding extraordinary items).

*“Dilution Reserve”* means, as of any date of determination, an amount sufficient to reduce the advance rate against Eligible Accounts used in the definition of Borrowing Base by one percentage point for each full percentage point by which Dilution is in excess of 5%.

*“Director”* means a director of Borrower.

*“Dollars” or “\$”* means lawful currency of the United States of America.

*“EBITDA”* means, as of any date of determination for any period, the Companies’ consolidated net profit before tax plus interest expense (net of any capitalized interest), intercompany interest expense, depreciation expense, amortization expense, and management fees expense of the Companies accrued by and payable to Parent.

*“EBITDA Coverage Ratio”* means, as of any date of determination for any period, (a) EBITDA divided by (b) the sum of (i) the aggregate of the Companies’ total interest expense (excluding any interest expense attributable to intercompany debt subordinated pursuant to the Subordination Agreement) for such period plus (without duplication of amounts) and (ii) the current maturity of the Companies’ long-term senior debt paid in such period.

*“Eligible Accounts”* means those Accounts created by Borrower in the ordinary course of its business, that arise out of Borrower’s sale of goods or rendition of services, that comply with each of the representations and warranties respecting Eligible Accounts made by Borrower in the Loan Documents, upon which Borrower’s right to receive payment is absolute and not contingent upon the fulfillment of any condition whatsoever, in which Bank has a perfected security interest of first priority, and that are not excluded as ineligible by virtue of one or more of the criteria set forth below; *provided* that such criteria may be fixed and revised from time to time by Bank in Bank’s sole and absolute discretion to address the results of any audit performed by Bank from time to time after the Closing Date. In determining the amount to be included, Eligible Accounts shall be calculated net of customer deposits and unapplied cash remitted to Borrower. Eligible Accounts shall not include the following:

- (i) any Account which is more than ninety (90) days past due;
- (ii) any Account that is disputed or subject to a claim of offset or other potential credit or a contra account;
- (iii) any Account not yet earned by the final delivery of goods or rendition of services, as applicable, by Borrower to the customer;
- (iv) any Account for services not yet rendered or for goods not yet shipped, including, without limitation, that portion of any Account, which represents interim or progress billings or retention rights on the part of the Account Debtor;
- (v) Accounts constituting proceeds of copyrightable material unless such copyrightable material shall have been registered with the United States Copyright Office and shall be covered by a duly executed copyright security agreement, in form and substance satisfactory to Bank, and filed in the United States Copyright Office;
- (vi) Accounts owed by an Account Debtor that is not Solvent, the subject of an Insolvency Proceeding or has gone out of business;
- (vii) Accounts owed by an Owner, Subsidiary, Affiliate, Officer or employee of Borrower, or Accounts owed by Cal Ex or Apio Cooling;
- (viii) Accounts not subject to a duly perfected security interest in Bank's favor or which are subject to any Lien (including any Liens imposed under PACA and any Producer's Lien Law) other than a Permitted Lien;
- (ix) that portion of any Account for which there exists any right of setoff, defense or discount (except regular discounts allowed in the ordinary course of business to promote prompt payment) or for which any defense or counterclaim has been asserted;
- (x) that portion of Accounts that has been restructured, extended, amended or modified;
- (xi) that portion of Accounts that constitutes advertising, finance charges, service charges or sales or excise taxes;
- (xii) Accounts owed by an Account Debtor (or an Affiliate of such Account Debtor), regardless of whether otherwise eligible, to the extent that the balance of such Accounts exceeds 25% of the sum of the aggregate amount of all Accounts (except in the case of each of Wal-Mart and Sam's Club, in which case such percentage shall be 30% in the aggregate for both Account Debtors, and except in the case of Costco, in which case such percentage shall be 30%); exceptions to such limit may be granted by Bank on a case by case basis, in Bank's sole and absolute discretion;

(xiii) any Account which represents an obligation of any Account Debtor (or an Affiliate of such Account Debtor), regardless of whether otherwise eligible, when twenty percent (20%) or more of Borrower's Accounts from such Account Debtor are not eligible pursuant to (i) above;

(xiv) Accounts arising in a transaction wherein goods are placed on consignment or are sold pursuant to a guaranteed sale, a sale or return, a sale on approval, a bill and hold, or any other terms by reason of which the payment by the Account Debtor may be conditional;

(xv) Accounts that are not payable in Dollars;

(xvi) Accounts with respect to which the Account Debtor either (A) does not maintain its chief executive office in the United States or Canada (excluding the Canadian province of Quebec), or (B) is not organized under the laws of the United States or Canada, or any state or province thereof (excluding the Canadian province of Quebec), or (C) is the government for any foreign country or sovereign state, or of any state, province, municipality, or other political subdivision thereof, or of any department, agency, public corporation, or other instrumentality thereof, unless (I) the Account is supported by an irrevocable letter of credit satisfactory to Bank (as to form, substance, and issuer or domestic confirming bank) that has been delivered to Bank and is directly drawable by Bank, or (II) the Account is covered by credit insurance in form, substance, and amount, and by an insurer, satisfactory to Bank;

(xvii) any Account which represents an obligation of any state or municipal government or of the United States government or any political subdivision thereof (except Accounts which represent obligations of the United States government and for which the assignment provisions of the Federal Assignment of Claims Act, 31 USC § 3727, as amended or recodified from time to time, have been complied with to Bank's satisfaction);

(xviii) Accounts with respect to which the Account Debtor is located in the states of New Jersey, Minnesota, or West Virginia (or any other state that requires a creditor to file a business activity report or similar document in order to bring suit or otherwise enforce its remedies against such Account Debtor in the courts or through any judicial process of such state), unless Borrower has qualified to do business in New Jersey, Minnesota, West Virginia, or such other states, or has filed a business activities report with the applicable division of taxation, the department of revenue, or with such other state offices, as appropriate, for the then-current year, or is exempt from such filing requirement; or

(xix) Upon telephonic notice to Borrower (other than voicemail), any Account deemed ineligible by Bank when Bank, in its sole discretion, deems the creditworthiness or financial condition of the Account Debtor, or the industry in which the Account Debtor is engaged, to be unsatisfactory.

*“Environmental Law”* means any federal, state, local or other governmental statute, regulation, law or ordinance dealing with the protection of human health and the environment.

*“Equipment”* means all of Borrower’s equipment, as such term is defined in the UCC, whether now owned or hereafter acquired, including but not limited to all present and future machinery, vehicles, furniture, fixtures, manufacturing equipment, shop equipment, office and recordkeeping equipment, parts, tools, supplies, and including specifically the goods described in any equipment schedule or list herewith or hereafter furnished to Bank by Borrower.

*“ERISA”* means the Employee Retirement Income Security Act of 1974.

*“ERISA Affiliate”* means any trade or business (whether or not incorporated) that is a member of a group which includes Borrower and which is treated as a single employer under Section 414 of the IRC.

*“Event of Default”* has the meaning given in Section 7.1.

*“Financial Covenants”* means the covenants set forth in Section 6.3.

*“Funding Date”* has the meaning given in Section 2.1.

*“GAAP”* means generally accepted accounting principles in the United States of America, consistently applied, which are in effect as of the date of this Agreement. If any changes in accounting principles from those in effect on the date hereof are hereafter occasioned by promulgation of rules, regulations, pronouncements or opinions by or are otherwise required by the Financial Accounting Standards Board or the American Institute of Certified Public Accountants (or successors thereto or agencies with similar functions), and any of such changes results in a change in the method of calculation of, or affects the results of such calculation of, any of the financial covenants, standards or terms found herein, then the parties hereto agree to enter into and diligently pursue negotiations in order to amend such financial covenants, standards or terms so as to equitably reflect such changes, with the desired result that the criteria for evaluating financial condition and results of operations of Borrower and the Subsidiaries shall be the same after such changes as if such changes had not been made.

*“General Intangibles”* means all of Borrower’s general intangibles, as such term is defined in the UCC, whether now owned or hereafter acquired, including all present and future Intellectual Property Rights, customer or supplier lists and contracts, manuals, operating instructions, permits, franchises, the right to use Borrower’s name, and the goodwill of Borrower’s business.

*“Governmental Authority”* means any federal, state, local, or other governmental or administrative body, instrumentality, department, or agency or any court, tribunal, administrative hearing body, arbitration panel, commission, or other similar dispute-resolving panel or body.

*“Grower Reserve”* means, as of the date of determination, a reserve against the Borrowing Base in an amount equal to 100% of all accounts payable then owing to all growers

of any of the produce sold by Borrower that are not parties to Acceptable Grower Contracts. The amount of all such accounts payable shall be determined by Bank in cooperation with Borrower in a commercially reasonable manner, and shall be prima facie evidence of such amount.

*“Guarantor(s)”* means Parent and any other Person now or hereafter guarantying the Obligations.

*“Guaranty”* means each certain Continuing Guaranty now or hereafter executed by a Guarantor in favor of Bank.

*“Hazardous Substances”* means pollutants, contaminants, hazardous substances, hazardous wastes, petroleum and fractions thereof, and all other chemicals, wastes, substances and materials listed in, regulated by or identified in any Environmental Law.

*“Immaterial Intellectual Property Rights”* means Intellectual Property Rights that Borrower, in its commercially reasonable judgment, determines from time to time to be no longer material to the operation of its business.

*“Indebtedness”* means of a Person as of a given date, all items of indebtedness or liability which in accordance with GAAP would be included in determining total liabilities as shown on the liabilities side of a balance sheet for such Person and shall also include the aggregate payments required to be made by such Person at any time under any lease that is considered a capitalized lease under GAAP.

*“Infringe”* means, when used with respect to Intellectual Property Rights, any infringement or other violation of such Intellectual Property Rights.

*“Insolvency Proceeding”* means any proceeding commenced by or against any Person under any provision of the Bankruptcy Code or under any other state or federal bankruptcy or insolvency law, assignments for the benefit of creditors, formal or informal moratoria, compositions, extensions generally with creditors, or proceedings seeking reorganization, arrangement, or other similar relief.

*“Intellectual Property Rights”* means all actual or prospective rights arising in connection with any intellectual property or other proprietary rights, including all rights arising in connection with copyrights, patents, service marks, trade dress, trade secrets, trademarks, trade names or mask works.

*“Inventory”* means all of Borrower’s inventory, as such term is defined in the UCC, whether now owned or hereafter acquired, whether consisting of whole goods, spare parts or components, supplies or materials, whether acquired, held or furnished for sale, for lease or under service contracts or for manufacture or processing, and wherever located.

*“Investment Property”* means all of Borrower’s investment property, as such term is defined in the UCC, whether now owned or hereafter acquired, including but not limited to all

securities, security entitlements, securities accounts, commodity contracts, commodity accounts, stocks, bonds, mutual fund shares, money market shares and U.S. Government securities.

*"IRC"* means the Internal Revenue Code of 1986.

*"Issuer"* means the issuer of any Letter of Credit.

*"Landec Ag"* means Landec Ag, Inc., a Delaware corporation.

*"L/C Amount"* means the sum of (i) the aggregate stated amount of any issued and outstanding Letters of Credit and (ii) the unpaid amount of the Obligation of Reimbursement.

*"L/C Application"* has the meaning specified in Section 2.2(a).

*"Letter of Credit"* has the meaning specified in Section 2.2(a).

*"Licensed Intellectual Property"* has the meaning given in Section 5.11(c).

*"Licensor Agreement"* means that certain Licensor Agreement, dated as of September 1, 2004, executed by Parent in favor of Bank, with respect to all licensing agreements between Parent and Borrower.

*"Lien"* means any security interest, mortgage, deed of trust, pledge, lien, charge, encumbrance, title retention agreement or analogous instrument or device, including the interest of each lessor under any capitalized lease and the interest of any bondsman under any payment or performance bond, in, of or on any assets or properties of a Person, whether now owned or hereafter acquired and whether arising by agreement or operation of law.

*"Life Insurance Assignment"* means an Assignment of Life Insurance Policy as Collateral to be executed by the owner and the beneficiary thereof, in form and substance satisfactory to Bank, granting Bank a first priority Lien on a Life Insurance Policy to secure payment of the Obligations.

*"Life Insurance Policy"* has the meaning given in Section 6.10.

*"Line of Credit"* means a credit accommodation in the maximum principal amount of the Line of Credit Commitment Amount, as defined more fully in Section 2.1.

*"Line of Credit Advance"* has the meaning given in Section 2.1(a).

*"Line of Credit Commitment Amount"* means \$7,000,000.

*"Line of Credit Commitment Availability"* means, as of any date of determination, and only if a positive number, the Line of Credit Commitment Amount minus the sum of: (i) the outstanding principal balance of the Line of Credit and (ii) the L/C Amount.



*"Line of Credit Maturity Date"* means August 31, 2007.

*"Line of Credit Note"* means Borrower's revolving promissory note evidencing its obligation to repay Line of Credit Advances, payable to the order of Bank in substantially the form of Exhibit A attached hereto, all terms of which are incorporated herein by this reference.

*"Loan Account"* has the meaning given in Section 9.9.

*"Loan Documents"* means this Agreement, the Line of Credit Note, any Guaranty, the Security Documents, the Subordination Agreement, and any L/C Application.

*"Lockbox"* means the post office box described in the Lockbox Agreement, or any replacement thereto, through which checks are processed pursuant to the Lockbox Agreement.

*"Lockbox Account"* means the "Account" as defined in the Lockbox Agreement.

*"Lockbox Agreement"* means the Deposit Account Control Agreement, dated as of August 20, 2003, by and among Borrower, Wells Fargo Business Credit, Inc. and Bank of America, National Association, or any subsequent lockbox agreement entered into by Bank and Borrower.

*"Material Adverse Effect"* means any of the following:

(i) a material adverse effect on the business, operations, results of operations, assets, liabilities or financial condition of the Companies, taken as a whole, or any Guarantor;

(ii) a material adverse effect on the ability of Borrower or any Guarantor to perform its obligations under the Loan Documents;

(iii) a material adverse effect on the ability of Bank to enforce the Obligations or to realize the intended benefits of the Security Documents, including a material adverse effect on the validity or enforceability of any Loan Document or of any rights against any Guarantor, or on the status, existence, perfection, priority (subject to Permitted Liens) or enforceability of any Lien securing payment or performance of the Obligations; or

(iv) any claim against Borrower or any Guarantor or threat of litigation which is reasonably likely to be determined adversely to Borrower or any Guarantor and, if so determined, would cause Borrower or such Guarantor to be liable to pay an amount exceeding \$1,000,000 over applicable insurance coverage, or would be an event described in clauses (i), (ii) and (iii) above.

*"Multiemployer Plan"* means a multiemployer plan (as defined in Section 4001(a)(3) of ERISA) to which Borrower or any ERISA Affiliate contributes or is obligated to contribute.

*"Net Income"* means fiscal year-to-date after-tax net income from continuing operations, as determined in accordance with GAAP.

*"Obligation of Reimbursement"* has the meaning given in Section 2.2(e)(i).

*"Obligations"* means the Line of Credit Note, the Obligation of Reimbursement and each and every other debt, liability and obligation of Borrower arising under this Agreement or any other Loan Document, whether such debt, liability or obligation now exists or is hereafter created or incurred, whether it is direct or indirect, due or to become due, absolute or contingent, primary or secondary, liquidated or unliquidated, or sole, joint, several or joint and several, and whether now in effect or hereafter entered into.

*"Officer"* means a duly appointed and presently sitting officer of Borrower.

*"Original Closing Date"* means September 1, 2004.

*"Owned Intellectual Property"* has the meaning given in Section 5.11(a).

*"Owner"* means with respect to Borrower, each Person having legal or beneficial title to an ownership interest in Borrower or a right to acquire such an interest.

*"PACA"* means the Perishable Agricultural Commodities Act, 7 U.S.C. § 499e, et seq., as amended.

*"Parent"* means Landec Corporation, a California corporation.

*"Pension Plan"* means a pension plan (as defined in Section 3(2) of ERISA) maintained for employees of Borrower or any ERISA Affiliate and covered by Title IV of ERISA.

*"Permitted Lien"* has the meaning given in Section 6.4(a).

*"Person"* means any individual, corporation, partnership, joint venture, limited liability company, association, joint-stock company, trust, unincorporated organization or government or any agency or political subdivision thereof.

*"Plan"* means an employee benefit plan (as defined in Section 3(3) of ERISA) maintained for employees of Borrower or any ERISA Affiliate.

*"Premises"* means all premises where Borrower conducts its business and has any rights of possession, including the premises described in Exhibit D attached hereto.

*"Producer's Lien Law"* means §55631, et seq. of the California Food and Agriculture Code, and any similar state or federal statutes creating Liens on agricultural products in favor of unpaid growers, producers, or processors.

*"Related Documents"* has the meaning given in Section 2.2(f)(i).

“*Reportable Event*” means a reportable event (as defined in Section 4043 of ERISA), other than an event for which the 30-day notice requirement under ERISA has been waived in regulations issued by the Pension Benefit Guaranty Corporation.

“*Security Agreement*” means that certain Security Agreement, dated as of even date herewith, executed by Borrower in favor of Bank.

“*Security Agreement Re: Patents and Trademarks*” means that certain Security Agreement Re: Patents and Trademarks, dated as of even date herewith, executed by Borrower in favor of Bank.

“*Security Agreement and Collateral Assignment of Partnership Interest*” means that certain Security Agreement and Collateral Assignment of Partnership Interest, dated as of even date herewith, executed by Borrower in favor of Bank, with respect to Borrower’s interest in Apio Cooling.

“*Security Documents*” means this Agreement, the Lockbox Agreement, the Security Agreement, the Security Agreement Re: Patents and Trademarks, the Licensor Agreement, the Security Agreement and Collateral Assignment of Partnership Interest, and any other agreement, instrument or document delivered to Bank from time to time to secure the Obligations.

“*Security Interest*” has the meaning given in Section 3.1.

“*Solvent*” means, with respect to any Person on a particular date, that such Person is not insolvent (as such term is defined in the Uniform Fraudulent Transfer Act).

“*Special Account*” means a specified cash collateral account maintained with Bank in connection with Letters of Credit, as contemplated by Section 2.2.

“*Subordination Agreement*” means the Subordination Agreement of even date herewith, among Parent, Bank and Borrower, and any other subordination agreement accepted by Bank from time to time.

“*Subsidiary*” means, as to any Person, any Person of which a majority of the shares of securities or other interests having ordinary voting power for the election of directors or other governing body (other than securities or interests having such power only by reason of the happening of a contingency) are at the time beneficially owned, or the management of which is otherwise controlled, directly, or indirectly through one or more intermediaries, or both, by such Person. Unless otherwise specified, all references herein to a “Subsidiary” or to “Subsidiaries” shall refer to a Subsidiary or Subsidiaries of a Borrower.

“*Tangible Net Worth*” means the aggregate of the common and preferred stockholders’ equity in the Companies plus subordinated debt less any intangible assets, determined in accordance with GAAP.

"*Termination Date*" means the earliest of (i) August 31, 2007, (ii) the date Borrower terminates the Credit Facility, or (iii) the date Bank demands payment of the Obligations after an Event of Default pursuant to Section 7.2 hereof.

"*Total Liabilities*" means, as of the date of determination, the aggregate of the Companies' consolidated Indebtedness and capitalized leases less subordinated debt.

"*UCC*" means the Uniform Commercial Code as in effect in the state designated in Section 8.15 as the state whose laws shall govern this Agreement, or in any other state whose laws are held to govern this Agreement or any portion hereof.

Section 1.2. *Other Definitional Terms; Rules of Interpretation.* The words "hereof", "herein" and "hereunder" and words of similar import when used in this Agreement shall refer to this Agreement as a whole and not to any particular provision of this Agreement. All accounting terms not otherwise defined herein have the meanings assigned to them in accordance with GAAP. All terms defined in the UCC and not otherwise defined herein have the meanings assigned to them in the UCC. References to Articles, Sections, subsections, Exhibits, Schedules and the like, are to Articles, Sections and subsections of, or Exhibits or Schedules attached to, this Agreement unless otherwise expressly provided. The words "include", "includes" and "including" shall be deemed to be followed by the phrase "without limitation". Unless the context in which used herein otherwise clearly requires, "or" has the inclusive meaning represented by the phrase "and/or". Defined terms include in the singular number the plural and in the plural number the singular. Reference to any agreement (including the Loan Documents), document or instrument means such agreement, document or instrument as amended or modified and in effect from time to time in accordance with the terms thereof (and, if applicable, in accordance with the terms hereof and the other Loan Documents), except where otherwise explicitly provided, and reference to any promissory note includes any promissory note which is an extension or renewal thereof or a substitute or replacement therefor. Reference to any law, rule, regulation, order, decree, requirement, policy, guideline, directive or interpretation means as amended, modified, codified, replaced or reenacted, in whole or in part, and in effect on the determination date, including rules and regulations promulgated thereunder.

## **Article II**

### **Amount and Terms of the Credit Facility**

#### Section 2.1. *Line of Credit.*

(a) *Advances.* Bank agrees, on the terms and subject to the conditions herein set forth, to make advances to Borrower from time to time under the Line of Credit (each such advance, a "*Line of Credit Advance*"), for working capital and general corporate purposes, from the date all of the conditions set forth in Section 4.1 are satisfied (the "*Funding Date*") to the Line of Credit Maturity Date. Bank shall have no obligation to make a Line of Credit Advance to the extent the amount of the requested Line of Credit Advance exceeds Availability. Borrower's obligation to repay the Line of Credit Advances shall be evidenced by the Line of Credit Note and shall be secured by the Collateral. Within the limits set forth in this Section 2.1 and in the Line of Credit Note, Borrower may from time to time prior to the Line of Credit

Maturity Date borrow, partially or wholly repay its outstanding borrowings, and reborrow under the Line of Credit, subject to all of the limitations, terms and conditions contained herein or in the Line of Credit Note.

(b) *[Reserved.]*

(c) *[Reserved.]*

(d) *Procedures for Requesting Advances.*

(i) *Time for Requests.* Borrower shall request each Line of Credit Advance not later than 10:00 a.m., San Francisco time (or 9:00 a.m., San Francisco time, on the last Business Day of each month, on Christmas eve, and on New Years eve) on the Business Day which is the date the Line of Credit Advance is to be made. Each such request shall be effective upon receipt by Bank, shall be in writing or by telephone, telecopy transmission or email, to be confirmed in writing by Borrower if so requested by Bank, shall be by (i) an Officer of Borrower; or (ii) a person designated as Borrower's agent by an Officer of Borrower in a writing delivered to Bank; or (iii) a person whom Bank reasonably believes to be an Officer of Borrower or such a designated agent. Borrower shall repay all Line of Credit Advances even if Bank does not receive such confirmation and even if the person requesting a Line of Credit Advance was not in fact authorized to do so. Any request for a Line of Credit Advance, whether written or telephonic, shall be deemed to be a representation by Borrower that the conditions set forth in Section 4.2 have been satisfied as of the time of the request.

(ii) *Disbursement.* Upon fulfillment of the applicable conditions set forth in Article IV, Bank shall disburse the proceeds of the requested Line of Credit Advance by crediting the same to the Loan Account, on that same Business Day, unless Bank and Borrower shall agree in writing to another manner of disbursement.

Section 2.2. *Letter of Credit Subfeature.*

(a) *Letters of Credit.* As a subfeature under the Line of Credit, Bank agrees from time to time during the term thereof to issue or cause an Affiliate to issue irrevocable standby or documentary letters of credit for the account of Borrower (each, a "*Letter of Credit*" and collectively, "*Letters of Credit*"); *provided* that the aggregate undrawn amount of all outstanding Letters of Credit shall not at any time exceed the lesser of:

(i) \$500,000 less the L/C Amount, or

(ii) Availability.

The form and substance of each Letter of Credit shall be subject to approval by Bank, in its sole but reasonable discretion. Each Letter of Credit shall be subject to the additional terms and conditions of the Letter of Credit agreements, applications and any related documents required by the Issuer in connection with the issuance thereof (collectively, an "*L/C Application*"), the

terms and conditions of which shall supplement the terms and conditions hereof, but if the terms of any such L/C Application and the terms of this Agreement are inconsistent, the terms hereof shall control.

(b) *Term.* No Letter of Credit shall be issued with an expiry date later than the Line of Credit Maturity Date.

(c) *Deemed Representation.* Any request to issue a Letter of Credit shall be deemed to be a representation by Borrower that the conditions set forth in Section 4.2 have been satisfied as of the date of the request.

(d) *Special Account.* If the Credit Facility is terminated for any reason while any Letter of Credit is outstanding, Borrower shall thereupon pay Bank in immediately available funds for deposit in the Special Account an amount equal to the L/C Amount. The Special Account shall be an interest bearing account with Bank. Bank may apply amounts on deposit in the Special Account at any time or from time to time to the Obligations in Bank's sole discretion. Borrower may not withdraw any amounts on deposit in the Special Account as long as Bank maintains a security interest therein. Bank agrees to transfer any balance in the Special Account to Borrower when Bank is required to release its security interest in the Special Account under applicable law.

(e) *Payment of Amounts Drawn Under Letters of Credit; Obligation of Reimbursement.* Borrower shall pay to Bank any and all amounts required to be paid under the applicable L/C Application, when and as required to be paid thereby, and the amounts designated below, when and as designated:

(i) Borrower shall pay to Bank on the day a draft is honored under any Letter of Credit a sum equal to all amounts drawn under such Letter of Credit plus any and all reasonable charges and expenses that the Issuer or Bank may pay or incur relative to such draw and the applicable L/C Application, plus interest on all such amounts, charges and expenses as set forth below (Borrower's obligation to pay all such amounts is herein referred to as the "*Obligation of Reimbursement*").

(ii) Whenever a draft is submitted under a Letter of Credit, Borrower authorizes Bank to make a Line of Credit Advance in the amount of the Obligation of Reimbursement and to apply the proceeds of such Line of Credit Advance thereto. Such Line of Credit Advance shall be repayable in accordance with and be treated in all other respects as a Line of Credit Advance hereunder.

(iii) If a draft is submitted under a Letter of Credit when Borrower is unable, because a Default Period exists or for any other reason, to obtain a Line of Credit Advance to pay the Obligation of Reimbursement, Borrower shall pay to Bank on demand and in immediately available funds, the amount of the Obligation of Reimbursement together with interest, accrued from the date of the draft until payment in full at the Default Rate. Notwithstanding Borrower's inability to obtain a Line of Credit Advance for any reason, Bank is irrevocably authorized, in its sole discretion, to make a

Line of Credit Advance in an amount sufficient to discharge the Obligation of Reimbursement and all accrued but unpaid interest thereon.

(iv) Borrower's obligation to pay any Line of Credit Advance made under this Section 2.2, shall be evidenced by the Line of Credit Note and shall bear interest as provided therein.

(f) *Obligations Absolute.* Borrower's obligations arising under this Section 2.2 shall be absolute, unconditional and irrevocable, and shall be paid strictly in accordance with the terms of this Section 2.2, under all circumstances whatsoever, including (without limitation) the following circumstances:

(i) any lack of validity or enforceability of any Letter of Credit or any other agreement or instrument relating to any Letter of Credit (collectively the "Related Documents");

(ii) any amendment or waiver of or any consent to departure from all or any of the Related Documents;

(iii) the existence of any claim, setoff, defense or other right which Borrower may have at any time, against any beneficiary or any transferee of any Letter of Credit (or any persons or entities for whom any such beneficiary or any such transferee may be acting), or other person or entity, whether in connection with this Agreement, the transactions contemplated herein or in the Related Documents or any unrelated transactions;

(iv) any statement or any other document presented under any Letter of Credit proving to be forged, fraudulent, invalid or insufficient in any respect or any statement therein being untrue or inaccurate in any respect whatsoever;

(v) payment by or on behalf of the Issuer under any Letter of Credit against presentation of a draft or certificate which does not strictly comply with the terms of such Letter of Credit; or

(vi) any other circumstance or happening whatsoever, whether or not similar to any of the foregoing.

Section 2.3. *[Reserved]*.

Section 2.4. *[Reserved]*.

Section 2.5. *Interest; Default Interest; Participations; Usury; Collection of Payments.*

(a) *Notes.* Except as set forth in Subsections (b) and (c), the outstanding principal balance of the Line of Credit Note shall bear interest at the rate of interest, and in the manner, set forth therein, and shall be due as set forth therein.

(b) *Default Interest Rate.* The principal of the Line of Credit outstanding from time to time shall bear interest at the applicable Default Rates, as more fully described in the Line of Credit Note. Bank's election to charge such Default Rates shall be in its sole discretion and shall not be a waiver of any of its other rights and remedies. Bank's election to charge interest at the Default Rate for less than the entire period during which the Default Rate may be charged shall not be a waiver of its right to subsequently charge the Default Rate for the entirety of another Default Period.

(c) *[Reserved.]*

(d) *Participations.* If any Person shall acquire a participation in the Line of Credit or the Obligation of Reimbursement, Borrower shall be obligated to Bank to pay the full amount of all interest calculated under this Section 2.5, along with all other fees, charges and other amounts due under this Agreement, regardless if such Person elects to accept interest with respect to its participation at a lower rate than that calculated under this Section 2.5, or otherwise elects to accept less than its pro rata share of such fees, charges and other amounts due under this Agreement.

(e) *Usury.* In any event, no rate change shall be put into effect which would result in a rate greater than the highest rate permitted by law. Notwithstanding anything to the contrary contained in any Loan Document, all agreements which either now are or which shall become agreements between Borrower and Bank are hereby limited so that in no contingency or event whatsoever shall the total liability for payments in the nature of interest, additional interest and other charges exceed the applicable limits imposed by any applicable usury laws. If any payments in the nature of interest, additional interest and other charges made under any Loan Document are held to be in excess of the limits imposed by any applicable usury laws, it is agreed that any such amount held to be in excess shall be considered payment of principal hereunder, and the indebtedness evidenced by the Line of Credit Note shall be reduced by such amount so that the total liability for payments in the nature of interest, additional interest and other charges shall not exceed the applicable limits imposed by any applicable usury laws, in compliance with the desires of Borrower and Bank. This provision shall never be superseded or waived and shall control every other provision of the Loan Documents and all agreements between Borrower and Bank, or their successors and assigns.

(f) *Collection of Payments.* All payments to Bank shall be made in immediately available funds and shall be applied to the Obligations upon receipt by Bank. Bank may hold all payments not constituting immediately available funds for three (3) additional days before applying them to the Obligations then due and payable. Subject to Section 7.7 of this Agreement, all payments with respect to the Obligations may be applied, and in Bank's sole discretion reversed and re-applied, to the Obligations, in such order and manner as Bank shall determine in its sole discretion.



Section 2.6. *Fees.*

(a) *Commitment Fee.* Borrower shall pay to Bank a non-refundable commitment fee for the Line of Credit equal to \$5,000.00, which fee shall be due and payable in full on the Closing Date.

(b) *Collateral Monitoring Fees.* Borrower shall pay to Bank, within 15 days after written demand, collateral monitoring fees, at the rates established from time to time by Bank as its audit fees, in connection with any audits or inspections conducted at any time after the Borrowing Base Trigger Date by or on behalf of Bank of any Collateral or Borrower's operations or business, including, without limitation, audits and inspections conducted by or on behalf of Bank as part of its normal monthly collateral monitoring process as have been conducted by Bank with respect to the Collateral since the Original Closing Date, together with all actual out-of-pocket costs and expenses incurred in conducting any such audit or inspection. Such collateral monitoring fees shall not exceed \$1,200 per month unless a Default Period is continuing.

(c) *Letter of Credit Fees.* Borrower shall pay to Bank a fee with respect to each Letter of Credit, if any, accruing on a daily basis and computed at the per annum rate of one percent (1.00%), of the aggregate amount that may then be drawn under it assuming compliance with all conditions for drawing (the "Aggregate Stated Amount"), from and including the date of issuance of such Letter of Credit until such date as such Letter of Credit shall terminate by its terms or be returned to the Issuer, due and payable monthly in arrears on the first day of each month and on the expiration date thereof; *provided* that during Default Periods, in Bank's sole discretion and without waiving any of its other rights and remedies, such fee shall increase to three percent (3.00%) of the Aggregate Stated Amount. The foregoing fee shall be in addition to any and all fees, commissions and charges of the Issuer with respect to or in connection with such Letter of Credit.

(d) *Letter of Credit Administrative Fees.* Borrower shall pay to Bank, within fifteen (15) days after written demand, the administrative fees charged by the Issuer in connection with the honoring of drafts under any Letter of Credit, amendments thereto, transfers thereof and all other activity with respect to any Letters of Credit at the then-current rates published by the Issuer for such services rendered on behalf of customers of the Issuer generally.

(e) *Prepayment Fees.* Borrower shall pay prepayment fees, if any, in the amount and manner described in the Line of Credit Note.

(f) *Unused Line Fee.* On the first day of each calendar quarter during the term of this Agreement, Borrower shall pay to Bank, in arrears for the immediately preceding calendar quarter, an unused line fee in an amount equal to 0.100% per annum times the result of (a) the Line of Credit Commitment Amount less (b) the sum of (i) the average Daily Balance of indebtedness under the Line of Credit outstanding during the immediately preceding calendar quarter and (ii) the average Daily Balance of the L/C Amount during the immediately preceding calendar quarter. The unused line fee due under this paragraph (f) shall not be payable following the termination and payment in full of the Line of Credit.

(g) *Audit Fees.* In addition to the fees described in paragraph (b) of this Section 2.6, Borrower shall pay Bank, within 15 days after written demand, fees in connection with any audits or inspections conducted by or on behalf of Bank of Borrower's operations or business at the rates established from time to time by Bank as its audit fees, together with all actual out-of-pocket costs and expenses incurred in conducting any such audit or inspection. There shall be no more than one such audit of Borrower per year unless a Default Period is continuing, in which case Bank may conduct as many audits as it may require.

(h) *Other Fees.* Bank may from time to time, upon five (5) days prior written notice to Borrower during a Default Period, charge additional fees for Line of Credit Advances made and Letters of Credit issued in excess of Availability, for late delivery of reports and in lieu of imposing interest at the Default Rate. Borrower's request for a Line of Credit Advance or the issuance of a Letter of Credit at any time after such notice is given and such five (5) day period has elapsed shall constitute Borrower's agreement to pay the fees described in such notice.

Section 2.7. *Increased Costs; Capital Adequacy; Funding Exceptions.*

(a) *Increased Costs; Capital Adequacy.* If Bank determines at any time that its Return (as defined below) has been reduced as a result of any Rule Change (as defined below), Bank may so notify Borrower and require Borrower, beginning thirty (30) days after such notice is received by Borrower, to pay it the amount necessary to restore its Return to what it would have been had there been no Rule Change. For purposes of this Section 2.7:

(i) "*Capital Adequacy Rule*" means any law, rule, regulation, guideline, directive, requirement or request regarding capital adequacy, or the interpretation or administration thereof by any Governmental Authority, whether or not having the force of law, that applies to any Related Bank (as defined below), including rules requiring financial institutions to maintain total capital in amounts based upon percentages of outstanding loans, binding loan commitments and letters of credit.

(ii) "*L/C Rule*" means any law, rule, regulation, guideline, directive, requirement or request regarding letters of credit, or the interpretation or administration thereof by any Governmental Authority, whether or not having the force of law, that applies to any Related Bank, including those that impose taxes, duties or other similar charges, or mandate reserves, special deposits or similar requirements against assets of, deposits with or for the account of, or credit extended by any Related Bank, on letters of credit.

(iii) "*Related Bank*" includes (but is not limited to) Bank, any parent of Bank and any assignee of any interest of Bank hereunder.

(iv) "*Return*", for any period, means the percentage determined by dividing (i) the sum of interest and ongoing fees earned by Bank under this Agreement during such period, by (ii) the average capital such Bank is required to maintain during such period as a result of its being a party to this Agreement, as determined by Bank based upon its total capital requirements and a reasonable attribution formula that takes account

of the Capital Adequacy Rules and L/C Rules, (if applicable) then in effect, costs of issuing or maintaining any Advance or Letter of Credit and amounts received or receivable under this Agreement or the Line of Credit Note with respect to any Advance or Letter of Credit. Return may be calculated for each calendar quarter and for the shorter period between the end of a calendar quarter and the date of termination in whole of this Agreement.

(v) “*Rule Change*” means any change in any Capital Adequacy Rule, or L/C Rule, (if applicable) occurring after the date of this Agreement, but the term does not include any changes that at the Funding Date are scheduled to take place under the existing Capital Adequacy Rules, or L/C Rules or any increases in the capital that Bank is required to maintain to the extent that the increases are required due to a regulatory authority’s assessment of that Bank’s financial condition.

(b) The initial notice sent by Bank shall be sent as promptly as practicable after Bank learns that its Return has been reduced, shall include a demand for payment of the amount necessary to restore Bank’s Return for the subsequent quarter in which the notice is sent, and shall state in reasonable detail the cause for the reduction in its Return and its calculation of the amount of such reduction. Thereafter, Bank may send a new notice during each calendar quarter setting forth the calculation of the reduced Return for that quarter and including a demand for payment of the amount necessary to restore its Return for that quarter. Bank’s calculation in any such notice shall be prima facie evidence of such amount.

(c) Borrower shall not be required to compensate Bank pursuant to the provisions of this Section 2.7 for any reduction of its Return suffered more than 90 days prior to the date that Bank notifies Borrower of the Rule Change giving rise to such reduction and of Bank’s intention to claim compensation therefor.

Section 2.8. *Lockbox*. Borrower shall instruct all Account Debtors to pay all Accounts directly to the Lockbox. If, notwithstanding such instructions, Borrower receives any payments on Accounts, Borrower shall deposit such payments into the Lockbox Account.

Section 2.9. *Mandatory Prepayment*. Without notice or demand, if the sum of the outstanding principal balance of the Line of Credit Advances plus the L/C Amount shall at any time exceed the Borrowing Base, Borrower shall (i) first, immediately prepay the Line of Credit Advances to the extent necessary to eliminate such excess; and (ii) if prepayment in full of the Line of Credit Advances is insufficient to eliminate such excess, pay to Bank in immediately available funds for deposit in the Special Account an amount equal to the remaining excess. Any payment received by Bank under this Section 2.9 may be applied to the Obligations, in such order and in such amounts as Bank, in its reasonable discretion, may from time to time determine.

Section 2.10. *Line of Credit Advances to Pay Obligations*. Notwithstanding anything in Section 2.1, Bank may, in its discretion at any time or from time to time, without Borrower’s request and even if the conditions set forth in Section 4.2 would not be satisfied, make a Line of Credit Advance in an amount equal to the portion of the Obligations from time to time due and

payable. Bank will use its commercially reasonable best efforts to provide Borrower with prompt notice after any such Advance pursuant to this Section 2.10 has been made; *provided* that any failure by Bank to provide such notice shall not be deemed to be a breach or default by Bank of its obligations hereunder.

Section 2.11. *Liability Records*. Bank may maintain from time to time, at its discretion, records as to the Obligations. All entries made on any such record shall be presumed correct until Borrower establishes the contrary. Upon Bank's demand, Borrower will admit and certify in writing the exact principal balance of the Obligations that Borrower then asserts to be outstanding. Any billing statement or accounting rendered by Bank shall be conclusive and fully binding on Borrower unless Borrower gives Bank specific written notice of exception within 30 days after receipt.

### **Article III Security Interest**

Section 3.1. *Grant of Security Interest*. Borrower hereby pledges, assigns and grants to Bank, and reaffirms its prior pledge, assignment and grant to Bank of, a lien and security interest (collectively referred to as the "*Security Interest*") in the Collateral, as security for the payment and performance of the Obligations. Upon request by Bank, Borrower will grant Bank a security interest in all commercial tort claims it may have against any Person.

All of the foregoing shall be evidenced by and subject to the terms of such security agreements, financing statements and other documents as Bank shall reasonably require, all in form and substance satisfactory to Bank (including, without limitation, the Security Documents). Borrower shall reimburse Bank within fifteen (15) days after written demand for all reasonable costs and expenses incurred by Bank in connection with any of the foregoing security, including without limitation, filing and recording fees and costs of appraisals and audits.

Section 3.2. *Financing Statements*. Borrower authorizes Bank to file from time to time where permitted by law, such financing statements against collateral described as "all personal property" or describing specific items of collateral including commercial tort claims as Bank deems necessary or useful to perfect the Security Interest, including, without limitation, amendments to any financing statements that were filed prior to the Closing Date. A carbon, photographic or other reproduction of this Agreement or of any financing statements authorized by Borrower is sufficient as a financing statement and may be filed as a financing statement in any state to perfect the security interests granted hereby. For this purpose, the following information is set forth:

Name and address of Debtor:

Apio, Inc.  
4575 West Main Street  
Guadalupe, CA 93434  
Federal Employer Identification No. 77-0528042  
Organizational Identification No. 2863977

Name and address of Secured Party:

Wells Fargo Bank, National Association  
400 Hamilton Avenue, P.O. Box 150  
Palo Alto, CA 94302

**Article IV**  
**Conditions of Lending**

Section 4.1. *Conditions Precedent to the Initial Advances and Letter of Credit.* The obligation of Bank to extend any credit contemplated by this Agreement is subject to the fulfillment to Bank's satisfaction of all of the following conditions:

- (a) This Agreement, duly executed by Borrower.
- (b) The Line of Credit Note, duly executed by Borrower.
- (c) To the extent not previously delivered in connection with the closing of the Original Agreement, a true and correct copy of any and all leases pursuant to which Borrower is leasing the Premises, together with a landlord's disclaimer and consent with respect to each such lease.
- (d) To the extent not previously delivered in connection with the closing of the Original Agreement, a true and correct copy of any and all mortgages pursuant to which Borrower has mortgaged the Premises, together with a mortgagee's disclaimer and consent with respect to each such mortgage.
- (e) To the extent not previously delivered in connection with the closing of the Original Agreement, the Life Insurance Assignment (if any), properly executed by the beneficiary and owner thereof, and the Life Insurance Policy (if any), together with evidence that such Life Insurance Policy is subject to no assignments or encumbrances other than the Life Insurance Assignment.
- (f) [Reserved].
- (g) To the extent not previously delivered in connection with the closing of the Original Agreement, control agreements, duly executed by Borrower and each bank at which Borrower maintains deposit accounts.
- (h) Each of the Security Agreement, the Security Agreement Re: Patents and Trademarks, the Licensor Agreement, and the Security Agreement and Collateral Assignment of Partnership Interest, duly executed by Borrower.
- (i) A Guaranty, duly executed by Parent.

(j) The Subordination Agreement, duly executed by Parent and acknowledged by Borrower.

(k) [Reserved].

(l) [Reserved].

(m) One or more certificates of Borrower's Secretary or Assistant Secretary certifying that attached to such certificate, or incorporated therein, are (i) the resolutions of Borrower's Directors and, if required, Owners, authorizing the execution, delivery and performance of the Loan Documents to which Borrower is a party, (ii) true, correct and complete copies of Borrower's Constituent Documents, and (iii) examples of the signatures of Borrower's Officers or agents authorized to execute and deliver the Loan Documents to which Borrower is a party and other instruments, agreements and certificates, including requests for Advances, on Borrower's behalf.

(n) A current certificate issued by the Secretary of State of Delaware, certifying that Borrower is in good standing and is in compliance with all applicable formation requirements of the State of Delaware.

(o) One or more certificates of Parent's Secretary or Assistant Secretary certifying that attached to such certificate, or incorporated therein, are (i) the resolutions of Parent's board of directors and, if required, owners, authorizing the execution, delivery and performance of the Loan Documents to which Parent is a party, (ii) true, correct and complete copies of Parent's Constituent Documents, and (iii) examples of the signatures of Parent's corporate officers or agents authorized to execute and deliver the Loan Documents to which Parent is a party and other instruments, agreements and certificates on Parent's behalf.

(p) A current certificate issued by the Secretary of State of California, certifying that Parent is in good standing and is in compliance with all applicable formation requirements of the State of California.

(q) Evidence that Borrower is duly licensed or qualified to transact business in all jurisdictions where the character of the property owned or leased or the nature of the business transacted by it makes such licensing or qualification necessary.

(r) A certificate of an Officer of Borrower confirming the representations and warranties set forth in Article V.

(s) A favorable opinion of counsel to Borrower and Parent, addressed to Bank.

(t) Certificates of the insurance required hereunder, with all hazard insurance containing a lender's loss payable endorsement in Bank's favor and with all liability insurance naming Bank as an additional insured.

(u) Payment of the fees and commissions due under Section 2.6 through the date of the initial Advances or Letter of Credit and reasonable expenses incurred by Bank through such date and required to be paid by Borrower under Section 8.5, including all reasonable legal expenses incurred through the date of this Agreement.

(v) [Reserved].

(w) Review and approval by Bank of the Companies' internally prepared financial statements for the period ended May 31, 2005.

(x) Review and approval by Bank of Parent's consolidating internally prepared financial statements for the period ended May 31, 2005.

(y) Review and approval of the Companies' consolidated financial projections.

(z) Satisfactory results of invoice verifications and vendor references.

(aa) Review and approval by Bank of all material agreements, including licensing agreements, royalty agreements, shareholder debt agreements, the management fee agreement, earn-out agreements, seller notes, mortgage agreements, grower contracts, material leases, and the agreements relating to the sale of Borrower's domestic commodity vegetable business.

(bb) No material adverse change in the financial condition of the Companies or Parent shall have occurred since the date of the most recent financial statement of Borrower received by Bank.

(cc) To the extent not previously delivered in connection with the closing of the Original Agreement, true and complete copies of all license agreements pursuant to which Borrower licenses any Intellectual Property Rights, together with a consent to assignment to Bank or its nominee from each licensor thereof.

(dd) Such other documents as Bank may reasonably require.

Section 4.2. *Conditions Precedent to All Advances and Letters of Credit.* The obligation of Bank to make each extension of credit requested by Borrower hereunder shall be subject to the fulfillment to Bank's satisfaction of each of the following conditions:

(a) the representations and warranties contained in Article V are correct on and as of the date of such extension of credit as though made on and as of such date, except to the extent that such representations and warranties relate solely to an earlier date;

(b) no event has occurred and is continuing, or would result from such extension of credit which constitutes a Default or an Event of Default; and

(c) no injunction, writ, restraining order, or other order of any nature prohibiting, directly or indirectly, the extending of such credit shall have been issued and remain in force by any Governmental Authority against Borrower, Bank, or any of their Affiliates.

## **Article V Representations and Warranties**

Borrower represents and warrants to Bank as follows:

Section 5.1. *Existence and Power; Name; Chief Executive Office; Inventory and Equipment Locations; Federal Employer Identification Number.* Borrower is a corporation, duly organized, validly existing and in good standing under the laws of the State of Delaware, and is duly licensed or qualified to transact business in all jurisdictions where the character of the property owned or leased or the nature of the business transacted by it makes such licensing or qualification necessary. Borrower has all requisite power and authority to conduct its business, to own its properties and to execute and deliver, and to perform all of its obligations under, the Loan Documents to which it is a party. During its existence, Borrower has done business solely under the names set forth in Schedule 5.1 and all of Borrower's records relating to its business or the Collateral are kept at the location set forth on Schedule 5.1. Borrower's chief executive office and principal place of business is located at the address set forth in Schedule 5.1. All Inventory and Equipment is located at that location or at one of the other locations listed in Schedule 5.1. Borrower's federal employer identification number and organizational identification number are each correctly set forth in Section 3.2.

Section 5.2. *Capitalization.* Schedule 5.2 constitutes a correct and complete list of all ownership interests of Borrower and rights to acquire ownership interests including the record holder, number of interests and percentage interests on a fully diluted basis, and an organizational chart showing the ownership structure of all Subsidiaries of Borrower.

Section 5.3. *Authorization of Borrowing; No Conflict as to Law or Agreements.* The execution, delivery and performance by Borrower of the Loan Documents to which it is a party and the borrowings from time to time hereunder have been duly authorized by all necessary corporate action and do not and will not (i) require any consent or approval of Borrower's Owners; (ii) require any authorization, consent or approval by, or registration, declaration or filing with, or notice to, any Governmental Authority, or any third Person, except such authorization, consent, approval, registration, declaration, filing or notice as has been obtained, accomplished or given prior to the date hereof; (iii) violate any provision of any law, rule or regulation (including Regulation X of the Board of Governors of the Federal Reserve System) or of any order, writ, injunction or decree presently in effect having applicability to Borrower or of Borrower's Constituent Documents; (iv) result in a breach of or constitute a default under any indenture or loan or credit agreement or any other material agreement, lease or instrument to which Borrower is a party or by which it or its properties may be bound or affected, in each case, the failure of which to comply with would result in a Material Adverse Effect; or (v) result in, or require, the creation or imposition of any Lien (other than the Security Interest) upon or with respect to any of the properties now owned or hereafter acquired by Borrower.



Section 5.4. *Legal Agreements.* This Agreement and the other Loan Documents to which Borrower is a party, upon their execution and delivery in accordance with the provisions hereof, will constitute the legal, valid and binding obligations of Borrower, enforceable against Borrower in accordance with their respective terms, except as enforcement may be limited by equitable principles or by bankruptcy, insolvency, reorganization, moratorium, or similar laws relating to or limiting creditors' rights generally.

Section 5.5. *Subsidiaries.* Borrower has no Subsidiaries other than as set forth in Schedule 5.5 hereto.

Section 5.6. *Financial Condition; No Adverse Change.* Borrower has furnished to Bank the Companies' audited financial statements for the fiscal year ended May 31, 2005, and those statements fairly present in all material respects the Companies' financial condition on the dates thereof and the results of their operations and cash flows for the periods then ended and were prepared in accordance GAAP. Since the date of the most recent financial statements, there has been no change in the Companies' business, properties or condition (financial or otherwise) which has had a Material Adverse Effect.

Section 5.7. *Litigation.* There are no actions, suits or proceedings pending or, to Borrower's knowledge, threatened against or affecting Borrower or any of its Affiliates or the properties of Borrower or any of its Affiliates before any court or governmental department, commission, board, bureau, agency or instrumentality, domestic or foreign, which, is reasonably likely to be adversely determined and, if determined adversely to Borrower or any of its Affiliates, would have a Material Adverse Effect.

Section 5.8. *Regulation U.* Borrower is not engaged in the business of extending credit for the purpose of purchasing or carrying margin stock (within the meaning of Regulation U of the Board of Governors of the Federal Reserve System), and no part of the proceeds of any Advance will be used to purchase or carry any margin stock or to extend credit to others for the purpose of purchasing or carrying any margin stock.

Section 5.9. *Taxes.* Borrower and its Affiliates have paid or caused to be paid to the proper authorities when due all federal, state and local taxes required to be paid by each of them (other than taxes that are being contested in good faith through appropriate processes and for which adequate reserves have been established) and Borrower has no knowledge of any pending assessments or adjustments of its income tax payable with respect to any year or the income tax payable by any Affiliate with respect to any year. Borrower and its Affiliates have filed all federal, state and local tax returns which to the knowledge of the Officers of Borrower or the officers of any Affiliate, as the case may be, are required to be filed, and Borrower and its Affiliates have paid or caused to be paid to the respective taxing authorities all taxes as shown on said returns or on any assessment received by any of them to the extent such taxes have become due.

Section 5.10. *Titles and Liens.* Borrower has good and absolute title to all Collateral free and clear of all Liens other than Permitted Liens. No financing statement naming Borrower as debtor is on file in any office except to perfect only Permitted Liens.

Section 5.11. *Intellectual Property Rights*

(a) *Owned Intellectual Property*. Schedule 5.11 (as updated by written notice to Bank from time to time) contains a complete list of all patents, applications for patents, trademarks, applications for trademarks, service marks, applications for service marks, mask works, trade dress and copyrights for which Borrower is the registered owner (the "*Owned Intellectual Property*"). Except for Immaterial Intellectual Property Rights or as disclosed on Schedule 5.11, (i) Borrower owns the Owned Intellectual Property free and clear of all restrictions (including covenants not to sue a third party), court orders, injunctions, decrees, writs or Liens, whether by written agreement or otherwise, (ii) no Person other than Borrower owns or has been granted any right in the Owned Intellectual Property, (iii) all Owned Intellectual Property is valid, subsisting and enforceable and (iv) Borrower has taken all commercially reasonable action necessary to maintain and protect the Owned Intellectual Property.

(b) *Agreements with Employees and Contractors*. Borrower has entered into a legally enforceable agreement with each of its employees and subcontractors obligating each such Person to assign to Borrower, without any additional compensation, any Intellectual Property Rights created, discovered or invented by such Person in the course of such Person's employment or engagement with Borrower (except to the extent prohibited by law), and further requiring such Person to cooperate with Borrower, without any additional compensation, in connection with securing and enforcing any Intellectual Property Rights therein; *provided* that the foregoing shall not apply with respect to employees and subcontractors whose job descriptions are of the type such that no such assignments are reasonably foreseeable.

(c) *Intellectual Property Rights Licensed from Others*. Schedule 5.11 (as updated by written notice to Bank from time to time) contains a complete list of all agreements under which Borrower has licensed Intellectual Property Rights from another Person ("*Licensed Intellectual Property*") other than readily available, non-negotiated licenses of computer software and other intellectual property used solely for performing accounting, word processing and similar administrative tasks ("*Off-the-shelf Software*") and a summary of any ongoing payments Borrower is obligated to make with respect thereto. Except as disclosed on Schedule 5.11 and in written agreements copies of which have been given to Bank, Borrower's licenses to use the Licensed Intellectual Property are free and clear of all restrictions, Liens, court orders, injunctions, decrees, or writs, whether by written agreement or otherwise. Except as disclosed on Schedule 5.11 (as updated by written notice to Bank from time to time), Borrower is not obligated or under any liability whatsoever to make any payments of a material nature by way of royalties, fees or otherwise to any owner of, licensor of, or other claimant to, any Intellectual Property Rights.

(d) *Other Intellectual Property Needed for Business*. Except for Off-the-shelf Software and as disclosed on Schedule 5.11 (as updated by written notice to Bank from time to time), the Owned Intellectual Property and the Licensed Intellectual Property constitute all Intellectual Property Rights used or necessary to conduct Borrower's business as it is presently conducted or as Borrower reasonably foresees conducting it.

(e) *Infringement.* Except as disclosed on Schedule 5.11 (as updated by written notice to Bank from time to time), Borrower has no knowledge of, and has not received any written claim or notice alleging, any Infringement of another Person's Intellectual Property Rights (including any written claim that Borrower must license or refrain from using the Intellectual Property Rights of any third party) nor, to Borrower's knowledge, is there any threatened claim or any reasonable basis for any such claim.

Section 5.12. *Plans.* Except as disclosed to Bank in writing prior to the date hereof, neither Borrower nor any ERISA Affiliate (i) maintains or has maintained any Pension Plan, (ii) contributes or has contributed to any Multiemployer Plan or (iii) provides or has provided post-retirement medical or insurance benefits with respect to employees or former employees (other than benefits required under Section 601 of ERISA, Section 4980B of the IRC or applicable state law). Neither Borrower nor any ERISA Affiliate has received any notice or has any knowledge to the effect that it is not in full compliance with any of the requirements of ERISA, the IRC or applicable state law with respect to any Plan. No Reportable Event exists in connection with any Pension Plan. Each Plan which is intended to qualify under the IRC is so qualified, and no fact or circumstance exists which may have an adverse effect on the Plan's tax-qualified status. Neither Borrower nor any ERISA Affiliate has (i) any accumulated funding deficiency (as defined in Section 302 of ERISA and Section 412 of the IRC) under any Plan, whether or not waived, (ii) any liability under Section 4201 or 4243 of ERISA for any withdrawal, partial withdrawal, reorganization or other event under any Multiemployer Plan or (iii) any liability or knowledge of any facts or circumstances which could result in any liability to the Pension Benefit Guaranty Corporation, the Internal Revenue Service, the Department of Labor or any participant in connection with any Plan (other than routine claims for benefits under the Plan).

Section 5.13. *Default.* Borrower is in compliance with all provisions of all agreements, instruments, decrees and orders to which it is a party or by which it or its property is bound or affected, the breach or default of which could have a Material Adverse Effect.

Section 5.14. *Environmental Matters.*

(a) To Borrower's best knowledge, there are not present in, on or under the Premises any Hazardous Substances in such form or quantity as to create any material liability or obligation for either Borrower or Bank under common law of any jurisdiction or under any Environmental Law, and no Hazardous Substances have ever been stored, buried, spilled, leaked, discharged, emitted or released in, on or under the Premises in such a way as to create any such material liability.

(b) To Borrower's best knowledge, Borrower has not disposed of Hazardous Substances in such a manner as to create any material liability under any Environmental Law.

(c) To Borrower's best knowledge, there are not any requests, claims, notices, investigations, demands, administrative proceedings, hearings or litigation, relating in any way to the Premises or Borrower, alleging material liability under, violation of, or noncompliance with

any Environmental Law or any license, permit or other authorization issued pursuant thereto. To Borrower's best knowledge, no such matter is threatened or impending.

(d) To Borrower's best knowledge, Borrower's businesses are and have in the past always been conducted in accordance with all Environmental Laws and all licenses, permits and other authorizations required pursuant to any Environmental Law and necessary for the lawful and efficient operation of such businesses are in Borrower's possession and are in full force and effect. No permit required under any Environmental Law is scheduled to expire within 12 months and there is no threat that any such permit will be withdrawn, terminated, limited or materially changed.

(e) To Borrower's best knowledge, the Premises are not and never have been listed on the National Priorities List, the Comprehensive Environmental Response, Compensation and Liability Information System or any similar federal, state or local list, schedule, log, inventory or database.

(f) Borrower has delivered to Bank all environmental assessments, audits, reports, permits, licenses and other documents describing or relating in any way to the Premises or Borrower's businesses.

Section 5.15. *Submissions to Bank.* All financial and other information provided to Bank by or on behalf of Borrower in connection with Borrower's request for the credit facilities contemplated hereby is (i) true and correct in all material respects, (ii) does not omit any material fact necessary to make such information not misleading and (iii) as to projections, valuations or proforma financial statements, present a good faith opinion as to such projections, valuations and proforma condition and results.

Section 5.16. *Financing Statements.* Borrower has authorized the filing of financing statements sufficient when filed to perfect the Security Interest and the other security interests created by the Security Documents. When such financing statements are filed in the offices noted therein, Bank will have a valid and perfected security interest in all Collateral which is capable of being perfected by filing financing statements. None of the Collateral is or will become a fixture on real estate, unless a sufficient fixture filing is in effect with respect thereto.

Section 5.17. *Rights to Payment.* To Borrower's best knowledge, each right to payment and each instrument, document, chattel paper and other agreement constituting or evidencing Collateral is (or, in the case of all future Collateral, will be when arising or issued) the valid, genuine and legally enforceable obligation, subject to no defense, setoff or counterclaim, of the Account Debtor or other obligor named therein or in Borrower's records pertaining thereto as being obligated to pay such obligation.

Section 5.18. *Eligible Accounts.* All Accounts that are included in the Borrowing Base are Eligible Accounts, and meet the definition thereof.

Section 5.19. *[Reserved].*

Section 5.20. *Fraudulent Transfer*. Borrower is Solvent. No transfer of property is being made by Borrower and no obligation is being incurred by Borrower in connection with the transactions contemplated by this Agreement or the other Loan Documents with the intent to hinder, delay, or defraud either present or future creditors of Borrower.

Section 5.21. *Permits, Franchises*. Borrower possesses, and will hereafter possess, all permits, consents, approvals, franchises and licenses required and rights to all trademarks, trade names, patents, and fictitious names, if any, necessary to enable it to conduct the business in which it is now engaged in compliance with applicable law and the failure of which to obtain would result in a Material Adverse Effect.

Section 5.22. *No Subordination*. There is no agreement, indenture, contract or instrument to which Borrower is a party or by which Borrower may be bound that requires the subordination in right of payment of any of Borrower's obligations subject to this Agreement to any other obligation of Borrower.

## **Article VI Covenants**

So long as the Obligations shall remain unpaid, or the Credit Facility shall remain outstanding, Borrower will comply with the following requirements, unless Bank shall otherwise consent in writing:

Section 6.1. *Punctual Payments*. Borrower shall punctually pay all principal, interest, fees or other liabilities due under any of the Loan Documents at the times and place and in the manner specified therein.

Section 6.2. *Reporting Requirements*. Borrower will deliver, or cause to be delivered, to Bank each of the following, which shall be in form and detail acceptable to Bank:

(a) *Financial Statements*.

(i) As soon as available, and in any event within 120 days after the end of each fiscal year of Parent, Borrower will deliver, or cause to be delivered, to Bank, Parent's audited financial statements with the unqualified opinion of independent certified public accountants selected by Parent and acceptable to Bank, which annual financial statements shall include Parent's balance sheet as at the end of such fiscal year and the related statements of Parent's income, reconciliation of retained earnings and cash flows for the fiscal year then ended, prepared on a consolidated basis to include any Affiliates, all in reasonable detail and prepared in accordance with GAAP, together with (A) copies of all management letters prepared by such accountants; and (B) a certificate of the chief financial officer of Borrower stating that such financial statements have been prepared in accordance with GAAP, fairly represent Parent's financial position and the results of its operations, and whether or not such officer has knowledge of the occurrence of any Default or Event of Default and, if so, stating in reasonable detail the facts with respect thereto.

(ii) As soon as available, and in any event within 45 days after the end of each fiscal quarter of Parent, Borrower will deliver, or cause to be delivered, to Bank, Parent's internally-prepared consolidating financial statements, which financial statements shall include Parent's balance sheet as at the end of such fiscal quarter and the related statements of Parent's income, reconciliation of retained earnings and cash flows for the fiscal quarter then ended, prepared on a consolidated basis to include any Affiliates, all in reasonable detail and prepared in accordance with GAAP.

(iii) As soon as available, and in any event within 45 days after the end of each fiscal quarter of Borrower, Borrower will deliver to Bank an unaudited/internal balance sheet and statements of income and reconciliation of retained earnings of Borrower as at the end of and for such fiscal quarter and for the year to date period then ended, prepared, if Bank so requests, on a consolidating and consolidated basis to include any Subsidiaries, in reasonable detail and stating in comparative form the figures for the corresponding date and periods in the previous year, all prepared in accordance with GAAP, subject to year-end audit adjustments and fairly representing in all material respects Companies' financial position and the results of its operations.

(b) *Other Information.* Borrower will deliver to Bank the following documents at the following times in form satisfactory to Bank:

- |                      |       |   |
|----------------------|-------|---|
| Quarterly            | (i)   | a certificate of the chief financial Officer of Borrower, substantially in the form of Exhibit C hereto stating (i) whether or not such officer has knowledge of the occurrence of any Default or Event of Default not theretofore reported and remedied and, if so, stating in reasonable detail the facts with respect thereto, and (ii) all relevant facts in reasonable detail to evidence, and the computations as to, whether or not Borrower is compliance with the Financial Covenants and other covenants contained in this Agreement, |
| Semi-Annually        | (ii)  | a detailed list of Borrower's customers with contact names and addresses,   |
| Upon request by Bank | (iii) | copies of invoices in connection with the Accounts, credit memos, remittance advices, deposit slips, shipping and delivery documents in connection with the Accounts and, for Inventory and Equipment acquired by Borrower, purchase orders and invoices, and   |
|                      | (iv)  | such other reports or information as to the Collateral, or the financial condition of Borrower, or otherwise, as Bank may reasonably request.   |

(c) *Collateral Reports.* On and after the occurrence of a Borrowing Base Trigger Date, Borrower will deliver to Bank the following documents at the following times in form reasonably satisfactory to Bank:

- |        |     |   |
|--------|-----|---|
| On the | (i) | a Borrowing Base certificate in the form of Exhibit B attached hereto |
|--------|-----|---|

Borrowing  
Base Trigger  
Date

(dated as of such Borrowing Base Trigger Date), executed by a financial representative of Borrower,

Monthly (not  
later  
than the 25th  
day  
after each fiscal  
month)

- (ii) a report of cash collections, sales assignments, credit memos/adjustments and deposits (*provided* that the frequency of such reports may be increased to weekly or daily, at Bank's option, during any Default Period),
- (iii) a report of outstanding payable balances owing to all growers,
- (iv) a detailed calculation of the Borrowing Base (including detail regarding those Accounts that are not Eligible Accounts),
- (v) a detailed listing and aging, by total, of the Accounts, together with a reconciliation to the detailed calculation of the Borrowing Base previously provided to Bank,
- (vi) monthly Borrowing Base certificate in the form of Exhibit B attached hereto, executed by a financial representative of Borrower, and
- (vii) a detailed aging, by vendor, of Borrower's accounts payable and any book overdraft, together with a reconciliation to Borrower's general ledger and monthly financial statements delivered pursuant to Section 6.2(b).

(d) *Projections.* Within 30 days after the beginning of each fiscal year of Borrower, Borrower will deliver to Bank the projected balance sheets and income statements for each month of such year for the Companies, Parent and Landec Ag, each in reasonable detail, representing Borrower's good faith projections and certified by the chief financial officer of Borrower and Parent as being the most accurate projections available and identical to the projections used by Borrower and Parent for internal planning purposes, together with a statement of underlying assumptions and such supporting schedules and information as Bank may in its discretion require.

(e) *Litigation.* Immediately after the commencement thereof, Borrower will deliver to Bank notice in writing of all litigation and of all proceedings before any governmental or regulatory agency affecting Borrower (i) of the type described in Section 5.14(c) or (ii) which seek a monetary recovery against Borrower in excess of \$500,000.

(f) *Defaults.* As promptly as practicable (but in any event not later than five business days) after an Officer of Borrower obtains knowledge of the occurrence of any Default or Event of Default, Borrower will deliver to Bank notice of such occurrence, together with a detailed statement by a responsible Officer of Borrower of the steps being taken by Borrower to cure the effect thereof.

(g) *Plans*. As soon as possible, and in any event within 30 days after Borrower knows or has reason to know that any Reportable Event with respect to any Pension Plan has occurred, Borrower will deliver to Bank a statement of the chief financial officer of Borrower setting forth details as to such Reportable Event and the action which Borrower proposes to take with respect thereto, together with a copy of the notice of such Reportable Event to the Pension Benefit Guaranty Corporation. As soon as possible, and in any event within 10 days after Borrower fails to make any quarterly contribution required with respect to any Pension Plan under Section 412(m) of the IRC, Borrower will deliver to Bank a statement of the chief financial officer of Borrower setting forth details as to such failure and the action which Borrower proposes to take with respect thereto, together with a copy of any notice of such failure required to be provided to the Pension Benefit Guaranty Corporation. As soon as possible, and in any event within 10 days after Borrower knows or has reason to know that it has or is reasonably expected to have any liability under Section 4201 or 4243 of ERISA for any withdrawal, partial withdrawal, reorganization or other event under any Multiemployer Plan, Borrower will deliver to Bank a statement of the chief financial officer of Borrower setting forth details as to such liability and the action which Borrower proposes to take with respect thereto.

(h) *Disputes*. Promptly upon knowledge thereof, Borrower will deliver to Bank notice of (i) any disputes or claims by Borrower's customers exceeding \$250,000 individually or \$1,000,000 in the aggregate during any fiscal year; (ii) credit memos exceeding \$250,000 for any individual Account Debtor or \$1,000,000 in the aggregate for all Account Debtors; or (iii) any goods returned to or recovered by Borrower with a value exceeding \$250,000 from any individual Account Debtor or \$1,000,000 in the aggregate from all Account Debtors.

(i) *Officers and Directors*. Promptly upon knowledge thereof, Borrower will deliver to Bank notice any change in the persons constituting Borrower's Officers and Directors.

(j) *Collateral*. Promptly upon knowledge thereof, Borrower will deliver to Bank notice of any loss of or material damage to any material portion of the Collateral or of any substantial adverse change in any material portion of the Collateral or the prospect of payment thereof.

(k) *Commercial Tort Claims*. Promptly upon knowledge thereof, Borrower will deliver to Bank notice of any commercial tort claims it may bring against any person, including the name and address of each defendant, a summary of the facts, an estimate of Borrower's damages, copies of any complaint or demand letter submitted by Borrower, and such other information as Bank may request.

(l) *Intellectual Property*.

(i) Borrower will give Bank 30 days prior written notice of its intent to acquire material Intellectual Property Rights; except for transfers permitted under Section 6.19, Borrower will give Bank 30 days prior written notice of its intent to dispose of material Intellectual Property Rights; and upon request, shall provide Bank with copies of all applicable documents and agreements.



(ii) Promptly upon knowledge thereof, Borrower will deliver to Bank notice of (A) any Infringement of its Intellectual Property Rights by others, (B) claims that Borrower is Infringing another Person's Intellectual Property Rights and (C) any threatened cancellation, termination or material limitation of its Intellectual Property Rights.

(iii) Promptly upon receipt, Borrower will give Bank copies of all registrations and filings with respect to its Intellectual Property Rights.

(m) *Reports to Owners*. Promptly upon their distribution, Borrower will deliver to Bank copies of all financial statements, reports and proxy statements which Parent shall have sent to its owners.

(n) *SEC Filings*. Promptly after the sending or filing thereof, Borrower will deliver to Bank copies of all regular and periodic reports which Parent shall file with the Securities and Exchange Commission or any national securities exchange.

(o) *Violations of Law*. Promptly upon knowledge thereof, Borrower will deliver to Bank notice of Borrower's violation of any law, rule or regulation, the non-compliance with which could materially and adversely affect Borrower's business or its financial condition.

(p) *Other Reports*. From time to time, with reasonable promptness, Borrower will deliver to Bank any and all receivables schedules, collection reports, deposit records, Equipment schedules, copies of invoices to Account Debtors, shipment documents and delivery receipts for goods sold, and such other material, reports, records or information as Bank may reasonably request.

#### Section 6.3. *Financial Covenants*.

(a) *Minimum EBITDA Coverage Ratio*. Borrower, together with the other Companies, will maintain the EBITDA Coverage Ratio, measured on a trailing 12 month basis as of the end of each fiscal quarter, at not less than 1.50:1.00.

(b) *Minimum Tangible Net Worth*. Borrower, together with the other Companies, will maintain, at all times, Tangible Net Worth, determined as of the end of each fiscal quarter, at an amount not less than \$19,500,000 plus 75% of cumulative Net Income realized since May 2005 up to such fiscal quarter end.

(c) *Minimum Net Income*. Borrower, together with the other Companies, will achieve (together with the other Companies) during each period described below, consolidated Net Income, of not less than the amount set forth in the table below opposite such period:

Fiscal Year to Date Period Ending	Minimum Net Income
August 31, 2005	\$ 400,000
November 30, 2005	\$ 1,500,000
Commencing with August 31, 2006, August 31 of each year	\$ 750,000
Commencing with the November 30, 2006, November 30 of each year	\$ 1,750,000
February 28 or 29, as applicable, of each year	\$ 2,150,000
May 31 of each year	\$ 2,900,000

(d) *Capital Expenditures*. Borrower together with the other Companies will not incur financed or unfinanced Capital Expenditures of more than \$6,000,000 in the aggregate during any fiscal year.

(e) *Maximum Leverage*. Borrower, together with the other Companies, will maintain Total Liabilities divided by Tangible Net Worth, as of the end of each fiscal quarter, at not greater than 1.50:1.00.

Section 6.4. *Permitted Liens; Financing Statements*.

(a) Borrower will not create, incur or suffer to exist any Lien upon or of any of its assets, now owned or hereafter acquired, to secure any Indebtedness; excluding, however, from the operation of the foregoing, the following (collectively, "*Permitted Liens*"):

- (i) in the case of any of Borrower's property which is not Collateral, covenants, restrictions, rights, easements and minor irregularities in title which do not materially interfere with Borrower's business or operations as presently conducted;
- (ii) Liens in existence on the date hereof and listed in Schedule 6.4 hereto, securing Indebtedness for borrowed money permitted under Section 6.5;
- (iii) the Security Interest and Liens created by the Security Documents;
- (iv) liens of carriers, warehousemen, mechanics, materialmen, vendors, and landlords and other similar liens imposed by law incurred in the ordinary course of business for sums not overdue or being contested in good faith, provided that adequate reserves for the payment thereof have been established in accordance with GAAP;

(v) deposits under workers' compensation, unemployment insurance and social security laws or to secure the performance of bids, tenders, contracts (other than for the repayment of borrowed money) or leases, or to secure statutory obligations of surety or appeal bonds or to secure indemnity, performance or other similar bonds in the ordinary course business;

(vi) banker's liens and similar liens (including set-off rights) in respect of bank deposits;

(vii) purchase money Liens incurred in connection with Capital Expenditures otherwise permitted pursuant to this Agreement; *provided* that such Liens attach only to the Equipment acquired thereby;

(viii) Liens incurred in connection with extensions, renewals or refinancings of the indebtedness secured by Liens of the type described above;

(ix) Liens incurred in connection with leases, subleases, licenses and sublicenses granted, in the ordinary course of Borrower's business, to Persons not interfering in any material respect with the business of Borrower and its Subsidiaries and any interest or title of a lessee or licensee under any such lease, sublease, license or sublicense; and

(x) Liens incurred in connection with the financing of the approximately 48,000 square foot expansion of Borrower's facility located at 4575 W. Main Street, Guadalupe, California; provided that (A) the aggregate principal amount of such financing does not exceed \$5,000,000, and (B) such Liens are limited to the real property on which such Borrower's facility is located and any improvements and fixtures affixed thereto.

(b) Borrower will not amend any financing statements in favor of Bank except as permitted by law. Any authorization by Bank to any Person to amend financing statements in favor of Bank shall be in writing.

Section 6.5. *Indebtedness*. Borrower will not incur, create, assume or permit to exist any Indebtedness or liability on account of deposits or advances or any Indebtedness for borrowed money or letters of credit issued on Borrower's behalf, or any other Indebtedness or liability evidenced by notes, bonds, debentures or similar obligations, except:

(a) Indebtedness arising hereunder;

(b) Indebtedness of Borrower in existence on the date hereof and listed in Schedule 6.5 hereto;

(c) Indebtedness relating to Permitted Liens;

(d) Indebtedness of Borrower arising from the endorsement of instruments for collection in the ordinary course of business;

(e) Indebtedness of Borrower under initial or successive refinancings of any Indebtedness permitted by clause (b) or (c) above, *provided* that (i) the principal amount of any such refinancing does not exceed the principal amount of the Indebtedness being refinanced and (ii) the material terms and provisions of any such refinancing (including maturity, redemption, prepayment, default and subordination provisions) are no less favorable to Bank than the Indebtedness being refinanced; and

(f) Other unsecured indebtedness of Borrower provided the aggregate principal amount of all such indebtedness does not exceed \$1,000,000.

Section 6.6. *Guaranties*. Borrower will not assume, guarantee, endorse or otherwise become directly or contingently liable in connection with any obligations of any other Person, except the endorsement of negotiable instruments by Borrower for deposit or collection or similar transactions in the ordinary course of business.

Section 6.7. *Investments and Subsidiaries*. Borrower will not purchase or hold beneficially any stock or other securities or evidences of indebtedness of, make or permit to exist any loans or advances to, or make any investment or acquire any interest whatsoever in, any other Person, including any partnership or joint venture, except:

(a) investments in direct obligations of the United States of America or any agency or instrumentality thereof whose obligations constitute full faith and credit obligations of the United States of America having a maturity of one year or less, commercial paper issued by U.S. corporations rated "A-1" or "A-2" by Standard & Poor's Corporation or "P-1" or "P-2" by Moody's Investors Service or certificates of deposit or bankers' acceptances having a maturity of one year or less issued by members of the Federal Reserve System having deposits in excess of \$100,000,000 (which certificates of deposit or bankers' acceptances are fully insured by the Federal Deposit Insurance Corporation) (each of the foregoing, collectively, "*Cash Equivalents*");

(b) travel advances or loans to Borrower's Officers and employees not exceeding at any one time an aggregate of \$50,000;

(c) security deposits, ground leases, and advances in the form of progress payments;

(d) current investments in the Subsidiaries in existence on the date hereof and listed in Schedule 5.5 hereto;

(e) value added joint venture investments; and

(f) crop advances.

Section 6.8. *Dividends and Distributions*. Borrower will not declare or pay any dividends (other than dividends payable solely in stock of Borrower) on any class of its stock or make any payment on account of the purchase, redemption or other retirement of any shares of such stock or make any distribution in respect thereof, either directly or indirectly.

Section 6.9. *Salaries*. Borrower will not pay excessive or unreasonable salaries, bonuses, commissions, consultant fees or other compensation to the extent that such payment would cause an Event of Default.

Section 6.10. *Key Person Life Insurance*. If Borrower shall at any time maintain insurance upon the life of any key Officer ("*Life Insurance Policy*"), then Borrower shall promptly notify Bank of each such Life Insurance Policy and assign to Bank the right to receive the proceeds of such Life Insurance Policy by a Life Insurance Assignment. The proceeds of any such Life Insurance Policy ("*Life Insurance Proceeds*"), whenever and however arising, shall be deposited in an Acceptable Wells Fargo Deposit Account and shall constitute Collateral for purposes of this Agreement and the other Loan Documents. For purposes of this Agreement, the term "Acceptable Wells Fargo Deposit Account" shall mean an interest bearing deposit account held at Bank over which Borrower shall have no control and in which Bank has a perfected security interest in such deposit account subject only to such other Liens as Bank may approve and subject to such additional security agreements and other documentation reasonably requested by Bank. Borrower hereby agrees that any Life Insurance Proceeds may be held by Bank as additional collateral for the Obligations until the repayment in full of all of the Obligations and the termination of this Agreement.

Section 6.11. *Books and Records; Inspection and Examination*. Borrower will keep accurate books of record and account for itself pertaining to the Collateral and pertaining to Borrower's business and financial condition and such other matters as Bank may from time to time reasonably request in which true and complete entries will be made in accordance with GAAP and, upon Bank's request, will permit any officer, employee, attorney or accountant for Bank to audit, review, make extracts from or copy any and all company and financial books and records of Borrower during ordinary business hours and upon one Business Day's advance notice (unless a Default Period exists in which case no notice shall be required), and to discuss Borrower's affairs with any of its Directors, Officers, and/or accounting personnel. Borrower hereby irrevocably authorizes all accountants and third parties to disclose and deliver to Bank, at Borrower's expense, all financial information, books and records, work papers, management reports and other information in its possession regarding Borrower. Borrower will permit Bank, or its employees, accountants, attorneys or agents, to examine and inspect any Collateral or any other property of Borrower during ordinary business hours and upon one Business Day's advance notice (unless a Default Period exists in which case no notice shall be required).

Section 6.12. *Account Verification*. Bank may at any time and from time to time send or require Borrower to send requests for verification of accounts and amounts owed to Account Debtors and other obligors. Bank may also at any time an Event of Default has occurred and is continuing and from time to time telephone Account Debtors and other obligors to verify accounts and send such Account Debtors and other obligors notification of the assignment of Accounts to Bank.

Section 6.13. *Compliance with Laws.*

(a) Borrower will (i) comply with the requirements of applicable laws and regulations, the non-compliance with which would materially and adversely affect its business or its financial condition and (ii) use and keep the Collateral, and require that others use and keep the Collateral, only for lawful purposes, without violation of any federal, state or local law, statute or ordinance.

(b) Without limiting the foregoing undertakings, Borrower specifically agrees that it will comply with all applicable Environmental Laws and obtain and comply with all permits, licenses and similar approvals required by any Environmental Laws, and will not generate, use, transport, treat, store or dispose of any Hazardous Substances in such a manner as to create any material liability or obligation under the common law of any jurisdiction or any Environmental Law.

Section 6.14. *Payment of Taxes and Other Claims.* Borrower will pay or discharge, when due, (a) all taxes, assessments and governmental charges levied or imposed upon it or upon its income or profits, upon any properties belonging to it (including the Collateral) or upon or against the creation, perfection or continuance of the Security Interest, prior to the date on which penalties attach thereto, (b) all federal, state and local taxes required to be withheld by it, and (c) all lawful claims for labor, materials and supplies which, if unpaid, might by law become a Lien upon any properties of Borrower; *provided* that Borrower shall not be required to pay any such tax, assessment, charge or claim whose amount, applicability or validity is being contested in good faith by appropriate proceedings and for which proper reserves have been made.

Section 6.15. *Maintenance of Properties.*

(a) Borrower will keep and maintain the Collateral and all of its other properties necessary or useful in its business in good condition, repair and working order (normal wear and tear excepted) and will from time to time replace or repair any worn, defective or broken parts; *provided* that nothing in this Section 6.15 shall prevent Borrower from discontinuing the operation and maintenance of any of its properties if such discontinuance is, in Borrower's commercially reasonable judgment, desirable in the conduct of Borrower's business and not disadvantageous in any material respect to Bank. Borrower will take all commercially reasonable steps necessary to protect and maintain its Intellectual Property Rights, other than Immaterial Intellectual Property Rights.

(b) Borrower will defend the Collateral against all Liens, claims or demands of all Persons (other than Bank) claiming the Collateral or any interest therein. Borrower will keep all Collateral free and clear of all Liens except Permitted Liens. Borrower will take all commercially reasonable steps necessary to prosecute any Person Infringing its Intellectual Property Rights and to defend itself against any Person accusing it of Infringing any Person's Intellectual Property Rights.

Section 6.16. *Insurance.* Borrower will obtain and at all times maintain insurance with insurers believed by Borrower to be responsible and reputable, in such amounts and against such

risks as may from time to time be required by Bank, but in all events in such amounts and against such risks as is usually carried by companies engaged in similar business and owning similar properties in the same general areas in which Borrower operates. Without limiting the generality of the foregoing, Borrower will at all times keep all tangible Collateral insured against risks of fire (including so-called extended coverage), theft, collision (for Collateral consisting of motor vehicles) and such other risks and in such amounts as Bank may reasonably request, with any loss payable to Bank to the extent of its interest, and all policies of such insurance shall contain a lender's loss payable endorsement for Bank's benefit. All policies of liability insurance required hereunder shall name Bank as an additional insured.

Section 6.17. *Preservation of Existence.* Borrower will preserve and maintain its existence and all of its rights, privileges and franchises necessary or desirable in the normal conduct of its business and shall conduct its business in an orderly, efficient and regular manner.

Section 6.18. *Delivery of Instruments, etc.* Upon request by Bank, Borrower will promptly deliver to Bank in pledge all instruments, documents and chattel paper constituting Collateral, duly endorsed or assigned by Borrower.

Section 6.19. *Sale or Transfer of Assets; Suspension of Business Operations.* Borrower will not sell, lease, assign, transfer or otherwise dispose of (i) the stock of any Subsidiary, (ii) all or a substantial part of its assets, or (iii) any Collateral or any interest therein (whether in one transaction or in a series of transactions) to any other Person other than (v) the sale of Inventory in the ordinary course of business, (w) dispositions of obsolete, surplus, worn or nonfunctional Equipment, (x) dispositions of cash or Cash Equivalents not otherwise prohibited under this Agreement, (y) transfers of Intellectual Property Rights as permitted under this Section 6.19 and (z) dispositions of other assets in any given fiscal year in an aggregate amount not to exceed \$750,000 or \$250,000 for any individual asset. Borrower will not liquidate, dissolve or suspend business operations. Borrower will not transfer any part of its ownership interest in any Intellectual Property Rights except for transfers of Immaterial Intellectual Property Rights and licensing or sublicensing of Intellectual Property Rights in the ordinary course of Borrower's business. Borrower will not permit any agreement under which it has licensed Licensed Intellectual Property, other than Immaterial Intellectual Property Rights, to lapse. If Borrower transfers any Intellectual Property Rights for value, other than transfers of Immaterial Intellectual Property Rights and licensing or sublicensing of Intellectual Property Rights in the ordinary course of Borrower's business, Borrower will pay over the proceeds to Bank for application to the Obligations. Bank hereby agrees that in the event Borrower licenses or sublicenses any Intellectual Property Rights pursuant to the terms of this Section 6.19, following written demand of Borrower, Bank shall execute a form of estoppel reasonably acceptable in form and substance to Borrower and Bank pursuant to which Bank shall represent that upon its exercise of any of its rights or remedies hereunder or under any other Loan Document with respect to the licensed or sublicensed Intellectual Property Rights, including a foreclosure under any Security Document, so long as there shall then exist no breach, default, or event of default on the part of the related licensee or sublicensee, as applicable, which breach, default or event of default has continued beyond any cure periods provided in the license or sublicense, Bank shall not extinguish or terminate the interest of the licensee or sublicensee, as applicable, by reason of such foreclosure.

Section 6.20. Consolidation and Merger; Asset Acquisitions. Borrower will not consolidate with or merge into any Person, or permit any other Person to merge into Borrower, or acquire (in a transaction analogous in purpose or effect to a consolidation or merger) all or substantially all the assets of any other Person.

Section 6.21. Sale and Leaseback. Borrower will not enter into any arrangement, directly or indirectly, with any other Person whereby Borrower shall sell or transfer any real or personal property, whether now owned or hereafter acquired, and then or thereafter rent or lease as lessee such property or any part thereof or any other property which Borrower intends to use for substantially the same purpose or purposes as the property being sold or transferred.

Section 6.22. Restrictions on Nature of Business. Borrower will not engage in any line of business materially different from that presently engaged in by Borrower and will not purchase, lease or otherwise acquire assets not related to its business.

Section 6.23. Accounting. Borrower will not adopt any material change in accounting principles other than as required by GAAP. Borrower will not adopt, permit or consent to any change in its fiscal year.

Section 6.24. Discounts, etc. Borrower will not grant any discount, credit or allowance to any customer of Borrower or accept any return of goods sold except in accordance with its historical practice or in the ordinary course of business. After notice from Bank, Borrower will not at any time modify, amend, subordinate, cancel or terminate the obligation of any Account Debtor or other obligor of Borrower.

Section 6.25. Plans. Unless disclosed to Bank pursuant to Section 5.12, neither Borrower nor any ERISA Affiliate will (i) adopt, create, assume or become a party to any Pension Plan, (ii) incur any obligation to contribute to any Multiemployer Plan, (iii) incur any obligation to provide post-retirement medical or insurance benefits with respect to employees or former employees (other than benefits required by law) or (iv) amend any Plan in a manner that would materially increase its funding obligations.

Section 6.26. Place of Business; Name. Borrower will not transfer its chief executive office or principal place of business, or move, relocate, close or sell any business location. Borrower will not permit any tangible Collateral or any records pertaining to the Collateral to be located in any state or area in which, in the event of such location, a financing statement covering such Collateral would be required to be, but has not in fact been, filed in order to perfect the Security Interest. Borrower will not change its name or jurisdiction of organization.

Section 6.27. Constituent Documents. Borrower will not amend its Constituent Documents in any respect that will result in a Material Adverse Effect.

Section 6.28. Transactions With Affiliates. Borrower will not directly or indirectly enter into or permit to exist any transaction with any Affiliate of Borrower except for transactions that are in the ordinary course of Borrower's business, upon fair and reasonable terms, that are fully



disclosed to Bank, and that are no less favorable to Borrower than would be obtained in an arm's length transaction with a non-Affiliate.

Section 6.29. *Use of Funds.* Borrower will not use any of the proceeds of any credit extended hereunder except for the purposes stated in Article II hereof.

Section 6.30. *Subordination of Debt.* All obligations of Borrower to any Guarantor or any Affiliate of Borrower (other than amounts arising pursuant to the tax sharing agreement among the Companies and Parent) shall be subordinated in right of repayment to all obligations of Borrower to Bank, as evidenced by and subject to the terms of subordination agreements in form and substance satisfactory to Bank.

Section 6.31. *Management Fees.* The Companies, collectively, will not pay management fees to Parent (including any fees or other amounts due Parent pursuant to the Corporate Services Agreement, dated November 15, 1999, between Parent and Borrower) in an amount greater than \$2,500,000 during any one fiscal year and, with respect solely to operating expenses paid by Parent on behalf of the Companies in the ordinary course of business of such parties and in line with historical practices, will reimburse Parent only for the reasonable portion of any such expenses; *provided* during any Default Period, Borrower shall not make any payments of management fees or expense reimbursements and any such items that would otherwise be paid notwithstanding such Default Period shall be accrued until such time, if any, following the expiration of such Default Period. Any management fees paid by Borrower to Parent shall be paid no more frequently than once per month.

Section 6.32. *Maintenance of Accounts with Bank.* Borrower shall, and shall cause each of the other Companies to, at all times during the period commencing on the Closing Date and ending on the Termination Date, maintain its primary depository accounts with Bank, including, without limitation, the Loan Account and the Lockbox Account, pursuant to account agreements and terms mutually acceptable to Borrower and Bank.

Section 6.33. *Grower Contracts.* With respect to all contracts with growers entered into by Borrower after the Closing Date, (i) Borrower shall use its commercially reasonable efforts to ensure that all such contracts shall be Acceptable Grower Contracts and (ii) upon Bank's request, Borrower shall permit any officer, employee, attorney or accountant for Bank to audit, review, make extracts from or copy any and all such grower contracts.

Section 6.34. *Performance by Bank.* If Borrower at any time fails to perform or observe any of the foregoing covenants contained in this Article VI or elsewhere herein, and if such failure shall continue for a period of ten calendar days after Bank gives Borrower written notice thereof (or in the case of the agreements contained in Sections 6.14 and 6.16, immediately upon the occurrence of such failure, without notice or lapse of time), Bank may, but need not, perform or observe such covenant or covenants on behalf and in the name, place and stead of Borrower (or, at Bank's option, in Bank's name) and may, but need not, take any and all other actions which Bank may reasonably deem necessary to cure or correct such failure (including the payment of taxes, the satisfaction of Liens, the performance of obligations owed to Account Debtors or other obligors, the procurement and maintenance of insurance, the execution of

assignments, security agreements and financing statements, and the endorsement of instruments); and Borrower shall thereupon pay to Bank on demand the amount of all monies expended and all costs and expenses (including reasonable attorneys' fees and legal expenses) incurred by Bank in connection with or as a result of the performance or observance of such agreements or the taking of such action by Bank, together with interest thereon from the date expended or incurred at the Default Rate applicable to Line of Credit Advances. To facilitate Bank's performance or observance of such covenants of Borrower, Borrower hereby irrevocably appoints Bank, or Bank's delegate, acting alone, as Borrower's attorney in fact (which appointment is coupled with an interest) with the right (but not the duty) from time to time to create, prepare, complete, execute, deliver, endorse or file in the name and on behalf of Borrower any and all instruments, documents, assignments, security agreements, financing statements, applications for insurance and other agreements and writings required to be obtained, executed, delivered or endorsed by Borrower under this Section 6.34.

**Article VII**  
**Events of Default, Rights and Remedies**

Section 7.1. *Events of Default*. "Event of Default", wherever used herein, means any one of the following events:

- (a) Default in the payment of any Obligations when they become due and payable;
- (b) Default in the performance, or breach, of any covenant or agreement of Borrower contained in this Agreement or in any other Loan Document, and (i) with respect to any such default under Section 6.2, such default shall continue unremedied for a period of five (5) days, and (ii) and with respect to any such default under Sections 6.13, 6.14, 6.15 and 6.18, such default shall continue unremedied for twenty (20) days after the earlier of (A) the date upon which an Officer or Director of Borrower obtained actual knowledge of such failure or (B) the date upon which written notice thereof is given to Borrower by Bank.
- (c) A Change of Control shall occur;
- (d) An Insolvency Proceeding is commenced by Borrower or any Guarantor;
- (e) An Insolvency Proceeding is commenced against Borrower, or any Guarantor, and any of the following events occur: (a) Borrower or such Guarantor consents to the institution of such Insolvency Proceeding against it, (b) the petition commencing the Insolvency Proceeding is not timely controverted, (c) the petition commencing the Insolvency Proceeding is not dismissed within sixty (60) calendar days of the date of the filing thereof; *provided* that, during the pendency of such period, Bank shall be relieved of its obligations to extend credit hereunder, (d) an interim trustee is appointed to take possession of all or any substantial portion of the properties or assets of, or to operate all or any substantial portion of the business of, Borrower or any such Guarantor, or (e) an order for relief shall have been entered therein;

(f) Any material portion of Borrower's or any Guarantor's assets is attached, seized, subjected to a writ or distress warrant, levied upon, or comes into the possession of any third Person;

(g) Borrower or any Guarantor is enjoined, restrained, or in any way prevented by court order from continuing to conduct all or any material part of its business affairs;

(h) A notice of Lien, levy, or assessment is filed of record with respect to any of Borrower's or any Guarantor's assets by the United States, or any department, agency, or instrumentality thereof, or by any state, county, municipal, or governmental agency, or if any taxes or debts owing at any time hereafter to any one or more of such entities becomes a Lien, whether choate or otherwise, upon any of Borrower's or any Guarantor's assets valued in excess of \$500,000 and the same is not paid before such payment is delinquent; *provided* that Bank may at any time that any such Lien exists reserve against the Borrowing Base in the amount of such Lien;

(i) This Agreement or any other Loan Document that purports to create a Lien, shall, for any reason, fail or cease to create a valid and perfected and, except to the extent permitted by the terms hereof or thereof, first priority Lien on or security interest in the Collateral covered hereby or thereby; *provided* that any such event described in this clause (i) shall not be an Event of Default for so long as Borrower is diligently assisting Bank, as determined by Bank in its sole and absolute discretion, in correcting the applicable problem;

(j) Any provision of any Loan Document shall at any time for any reason be declared to be null and void, or the validity or enforceability thereof shall be contested by Borrower, or a proceeding shall be commenced by Borrower, or by any Governmental Authority having jurisdiction over Borrower, seeking to establish the invalidity or unenforceability thereof, or Borrower shall deny that Borrower has any liability or obligation purported to be created under any Loan Document;

(k) Any representation or warranty made by Borrower in this Agreement or in any other Loan Document, by any Guarantor in any guaranty delivered to Bank, or by Borrower (or any of its Officers) or any Guarantor in any agreement, certificate, instrument or financial statement or other statement contemplated by or made or delivered pursuant to or in connection with this Agreement or any such guaranty shall prove to have been incorrect in any material respect when deemed to be effective;

(l) The rendering against Borrower of an arbitration award, final judgment, decree or order for the payment of money in excess of \$1,000,000 over applicable insurance coverage and the continuance of such arbitration award, judgment, decree or order unsatisfied and in effect for any period of 60 consecutive days without a stay of execution;

(m) A default under any bond, debenture, note or other evidence of material Indebtedness of Borrower owed to any Person other than Bank, or under any indenture or other instrument under which any such evidence of Indebtedness has been issued or by which it is governed, or under any material lease or other contract, and the expiration of the applicable

period of grace, if any, specified in such evidence of Indebtedness, indenture, other instrument, lease or contract, and the effect of such failure, event or condition is to cause, or permit the holder or holders thereof to cause, Indebtedness of Borrower (other than the Obligations) (in an aggregate amount exceeding \$500,000 in the event that such Indebtedness is unsecured) to become redeemable, due or otherwise payable (whether at scheduled maturity, by required prepayment, upon acceleration or otherwise);

(n) Any Reportable Event, which Bank determines in good faith might constitute grounds for the termination of any Pension Plan or for the appointment by the appropriate United States District Court of a trustee to administer any Pension Plan, shall have occurred and be continuing 30 days after written notice to such effect shall have been given to Borrower by Bank; or a trustee shall have been appointed by an appropriate United States District Court to administer any Pension Plan; or the Pension Benefit Guaranty Corporation shall have instituted proceedings to terminate any Pension Plan or to appoint a trustee to administer any Pension Plan; or Borrower or any ERISA Affiliate shall have filed for a distress termination of any Pension Plan under Title IV of ERISA; or Borrower or any ERISA Affiliate shall have failed to make any quarterly contribution required with respect to any Pension Plan under Section 412(m) of the IRC, which Bank determines in good faith may by itself, or in combination with any such failures that Bank may determine are likely to occur in the future, result in the imposition of a Lien on Borrower's assets in favor of the Pension Plan; or any withdrawal, partial withdrawal, reorganization or other event occurs with respect to a Multiemployer Plan which results or could reasonably be expected to result in a material liability of Borrower to the Multiemployer Plan under Title IV of ERISA.

(o) An event of default shall occur under any Security Document;

(p) Borrower shall liquidate, dissolve, terminate or suspend its business operations or otherwise fail to operate its business in the ordinary course, or sell or attempt to sell all or substantially all of its assets;

(q) Default in the payment of any amount owed by Borrower to Bank other than any Indebtedness arising hereunder after the expiration of any applicable express grace period related to such amount;

(r) Any Guarantor shall repudiate, purport to revoke or fail to perform his obligations under his guaranty in favor of Bank, any individual Guarantor shall die or any other Guarantor shall cease to exist;

(s) Borrower shall take or participate in any action which would be prohibited under the provisions of any Subordination Agreement or make any payment on any indebtedness subordinated thereby that any Person was not entitled to receive under the provisions of the Subordination Agreement;

(t) The occurrence of any "Default" or "Event of Default" under, and as defined in, any agreement between any Affiliate of Borrower and Bank (but giving effect to any applicable grace or cure periods with respect thereto); or

(u) Any other event having a Material Adverse Effect shall occur, and if such Material Adverse Effect is capable of cure, such Material Adverse Effect shall continue uncured for twenty (20) days after the earlier of (A) the date upon which an Officer or Director of Borrower obtained actual knowledge of such Material Adverse Effect or (B) the date upon which written notice thereof is given to Borrower by Bank.

Section 7.2. *Rights and Remedies.* Upon the occurrence and during the continuation of an Event of Default, Bank may exercise any or all of the following rights and remedies, all of which Borrower acknowledges and agrees are commercially reasonable:

- (a) Bank may, by notice to Borrower, declare the Credit Facility to be terminated, whereupon the same shall forthwith terminate;
- (b) Bank may, by notice to Borrower, declare the Obligations to be forthwith due and payable, whereupon all Obligations shall become and be forthwith due and payable, without presentment, notice of dishonor, protest or further notice of any kind, all of which Borrower hereby expressly waives;
- (c) Bank may, without notice to Borrower and without further action, apply any and all money owing by Bank to Borrower to the payment of the Obligations;
- (d) Bank may settle or adjust disputes and claims directly with Account Debtors for amounts and upon terms which Bank considers advisable, and in such cases, Bank will credit the Obligations with only the net amounts received by Bank in payment of such disputed Accounts after deducting all expenses incurred or expended by Bank in connection therewith;
- (e) Bank may cause Borrower to hold all returned Inventory in trust for Bank, segregate all returned Inventory from all other assets of Borrower or in Borrower's possession and conspicuously label said returned Inventory as the property of Bank;
- (f) without notice to or demand upon Borrower or any Guarantor, Bank may make such payments and do such acts as Bank considers necessary or reasonable to protect its security interests in the Collateral. Borrower agrees to assemble the Collateral if Bank so requires, and to make the Collateral available to Bank at a place that Bank may designate which is reasonably convenient to both parties. Borrower authorizes Bank to enter the premises where the Collateral is located, to take and maintain possession of the Collateral, or any part of it, and to pay, purchase, contest, or compromise any Lien that in Bank's determination appears to conflict with Bank's Liens and to pay all expenses incurred in connection therewith and to charge the Obligations therefor. With respect to any of Borrower's owned or leased premises, Borrower hereby grants Bank a license to enter into possession of such premises and to occupy the same, without charge, in order to exercise any of Bank's rights or remedies provided herein, at law, in equity, or otherwise;
- (g) without notice to Borrower (such notice being expressly waived), and without constituting a retention of any collateral in satisfaction of an obligation (within the meaning of the UCC), Bank may set off and apply to the Obligations any and all (i) balances and deposits of

Borrower held by Bank (including any amounts received in the Lockbox), or (ii) Indebtedness at any time owing to or for the credit or the account of Borrower held by Bank;

(h) Bank may hold, as cash collateral, any and all balances and deposits of Borrower held by Bank, and any amounts received in the Lockbox, to secure the full and final repayment of all of the Obligations;

(i) Bank may ship, reclaim, recover, store, finish, maintain, repair, prepare for sale, advertise for sale, and sell (in the manner provided for herein) the Collateral;

(j) Bank may sell the Collateral at either a public or private sale, or both, by way of one or more contracts or transactions, for cash or on terms, in such manner and at such places (including Borrower's premises) as Bank determines is commercially reasonable. It is not necessary that the Collateral be present at any such sale;

(k) Bank shall give notice of the disposition of the Collateral as follows:

(i) Bank shall give Borrower a notice in writing of the time and place of public sale, or, if the sale is a private sale or some other disposition other than a public sale is to be made of the Collateral, the time on or after which the private sale or other disposition is to be made; and

(ii) The notice shall be personally delivered or mailed, postage prepaid, to Borrower as provided in Section 8.3, at least 10 days before the earliest time of disposition set forth in the notice; no notice needs to be given prior to the disposition of any portion of the Collateral that is perishable or threatens to decline speedily in value or that is of a type customarily sold on a recognized market;

(l) Bank may credit bid and purchase at any public sale;

(m) Bank may seek the appointment of a receiver or keeper to take possession of all or any portion of the Collateral or to operate the same and, to the maximum extent permitted by law, may seek the appointment of such a receiver without the requirement of prior notice or a hearing;

(n) If Bank sells any of the Collateral on credit, the Obligations will be reduced only to the extent of payments actually received. If the purchaser fails to pay for the Collateral, Bank may resell the Collateral and shall apply any proceeds actually received to the Obligations;

(o) Bank shall have no obligation to attempt to satisfy the Obligations by collecting them from any third Person which may be liable for them or any portion thereof, and Bank may release, modify or waive any collateral provided by any other Person as security for the Obligations or any portion thereof, all without affecting Bank's rights against Borrower. Borrower waives any right it may have to require Bank to pursue any third Person for any of the Obligations;

(p) Bank may make demand upon Borrower and, forthwith upon such demand, Borrower will pay to Bank in immediately available funds for deposit in the Special Account an amount equal to the aggregate maximum amount available to be drawn under all Letters of Credit then outstanding, assuming compliance with all conditions for drawing thereunder;

(q) Bank may exercise and enforce its rights and remedies under the Loan Documents; and

(r) Bank may exercise any other rights and remedies available to it by law or agreement.

Notwithstanding the foregoing, upon the occurrence of an Event of Default described in subsections (d) or (e) of Section 7.1, the Obligations shall be immediately due and payable automatically without presentment, demand, protest or notice of any kind.

Section 7.3. *Disclaimer of Warranties.* Bank may sell the Collateral without giving any warranties as to the Collateral. Bank may specifically disclaim any warranties of title or the like. This procedure will not be considered to adversely affect the commercial reasonableness of any sale of the Collateral.

Section 7.4. *Compliance With Laws.* Bank may comply with any applicable state or federal law requirements in connection with a disposition of the Collateral, and Bank's compliance therewith will not be considered to adversely affect the commercial reasonableness of any sale of the Collateral.

Section 7.5. *No Marshalling.* Bank shall be under no obligation to marshal any assets in favor of Borrower, or against or in payment of the Obligations or any other obligation owned to Bank by Borrower or any other Person.

Section 7.6. *Borrower to Cooperate.* Upon the exercise by Bank of any power, right, privilege, or remedy pursuant to this Agreement which requires any consent, approval, registration, qualification, or authorization of any Governmental Authority, Borrower agrees to execute and deliver, or will cause the execution and delivery of, all applications, certificates, instruments, assignments, and other documents and papers that Bank or any purchaser of the Collateral may be required to obtain for such governmental consent, approval, registration, qualification, or authorization.

Section 7.7. *Application of Proceeds.* All proceeds realized as the result of any sale of the Collateral shall be applied by Bank:

FIRST to the costs, expenses, liabilities, obligations and attorneys' fees incurred by Bank in the exercise of its rights under this Agreement;

SECOND to the interest and fees due upon any of the Obligations; and

THIRD to the principal of the Obligations, in such order as Bank shall determine in its sole discretion. Any surplus shall be paid to Borrower or other Persons legally entitled thereto; Borrower shall remain liable to Bank for any deficiency.

Section 7.8. *Remedies Cumulative.* The rights and remedies of Bank under this Agreement, the other Loan Documents, and all other agreements contemplated hereby and thereby shall be cumulative. Bank shall have all other rights and remedies not inconsistent herewith as provided under the UCC, by law, or in equity. No exercise by Bank of any one right or remedy shall be deemed an election of remedies, and no waiver by Bank of any default on Borrower's part shall be deemed a continuing waiver of any further defaults.

Section 7.9. *Bank Not Liable For The Collateral.* So long as Bank complies with the obligations, if any, imposed by the UCC, Bank shall not otherwise be liable or responsible in any way or manner for: (a) the safekeeping of the Collateral; (b) any loss or damage thereto occurring or arising in any manner or fashion or from any cause; (c) any diminution in the value thereof; or (d) any act or default of any carrier, warehouseman, bailee, forwarding agency, or other person whomsoever, in each case, other than arising as a result of the gross negligence or willful misconduct of Bank. Borrower bears the risk of loss or damage of the Collateral.

#### **Article VIII Miscellaneous**

Section 8.1. *No Waiver.* No failure or delay by Bank in exercising any right, power or remedy under the Loan Documents shall operate as a waiver thereof, nor shall any single or partial exercise of any such right, power or remedy preclude any other or further exercise thereof or the exercise of any other right, power or remedy under the Loan Documents.

Section 8.2. *Amendments, Etc.* No amendment, modification, termination or waiver of any provision of any Loan Document or consent to any departure by Borrower therefrom or any release of a Security Interest shall be effective unless the same shall be in writing and signed by Bank, and then such waiver or consent shall be effective only in the specific instance and for the specific purpose for which given. No notice to or demand on Borrower in any case shall entitle Borrower to any other or further notice or demand in similar or other circumstances.

Section 8.3. *Addresses for Notices; Requests for Accounting.* Except as otherwise expressly provided herein, all notices, requests, demands and other communications provided for under the Loan Documents shall be in writing and shall be (a) personally delivered, (b) sent by first class United States mail, (c) sent by overnight courier of national reputation, or (d) transmitted by telecopy, in each case addressed or telecopied to the party to whom notice is being given at its address or telecopier number as set forth below next to its signature or, as to each party, at such other address or telecopier number as may hereafter be designated by such party in a written notice to the other party complying as to delivery with the terms of this Section. All such notices, requests, demands and other communications shall be deemed to have been given on (a) the date received if personally delivered, (b) when deposited in the mail if delivered by mail, (c) the date sent if sent by overnight courier, or (d) the date of transmission if delivered by telecopy, except that notices or requests to Bank pursuant to any of the provisions



of Article II shall not be effective until received by Bank. All requests under Section 9210 of the UCC (i) shall be made in a writing signed by a person authorized under Section 2.1(d), (ii) shall be personally delivered, sent by registered or certified mail, return receipt requested, or by overnight courier of national reputation (iii) shall be deemed to be sent when received by Bank and (iv) shall otherwise comply with the requirements of Section 9210. Borrower requests that Bank respond to each such request which on its face appears to come from an authorized individual and releases Bank from any liability for so responding. Borrower shall pay Bank the maximum amount allowed by law for responding to such requests.

Section 8.4. *Further Documents.* Borrower will from time to time execute and deliver or endorse any and all instruments, documents, conveyances, assignments, security agreements, financing statements, control agreements and other agreements and writings that Bank may reasonably request in order to secure, protect, perfect or enforce the Security Interest or Bank's rights under the Loan Documents (but any failure to request or assure that Borrower executes, delivers or endorses any such item shall not affect or impair the validity, sufficiency or enforceability of the Loan Documents and the Security Interest, regardless of whether any such item was or was not executed, delivered or endorsed in a similar context or on a prior occasion).

Section 8.5. *Costs and Expenses.* Borrower shall pay within fifteen (15) days after written demand all costs and expenses, including reasonable attorneys' fees, incurred by Bank in connection with the Obligations, this Agreement, the Loan Documents, any Letter of Credit and any other document or agreement related hereto or thereto, and the transactions contemplated hereby, including all such costs, expenses and fees incurred in connection with the negotiation, preparation, execution, amendment, administration, performance, collection and enforcement of the Obligations and all such documents and agreements and the creation, perfection, protection, satisfaction, foreclosure or enforcement of the Security Interest.

Section 8.6. *Indemnity.* In addition to the payment of expenses pursuant to Section 8.5, Borrower shall indemnify, defend and hold harmless Bank, and any of its participants, parent corporations, subsidiary corporations, affiliated corporations, successor corporations, and all present and future officers, directors, employees, attorneys and agents of the foregoing (the "*Indemnitees*") from and against any of the following (collectively, "*Indemnified Liabilities*"), in each, other than arising as a result of the gross negligence or willful misconduct of any Indemnitee:

(i) any and all transfer taxes, documentary taxes, assessments or charges made by any Governmental Authority by reason of the execution and delivery of the Loan Documents or the making of the Advances;

(ii) any claims, loss or damage to which any Indemnitee may be subjected if any representation or warranty contained in Section 5.14 proves to be incorrect in any respect or as a result of any violation of the covenant contained in Section 6.13(b); and

(iii) any and all other liabilities, losses, damages, penalties, judgments, suits, claims, costs and expenses of any kind or nature whatsoever (including the reasonable fees and disbursements of counsel) in connection with the foregoing and any other

investigative, administrative or judicial proceedings, whether or not such Indemnitee shall be designated a party thereto, which may be imposed on, incurred by or asserted against any such Indemnitee, in any manner related to or arising out of or in connection with the Credit Facility and the Loan Documents or the use or intended use of the proceeds of the Line of Credit.

If any investigative, judicial or administrative proceeding arising from any of the foregoing is brought against any Indemnitee, upon such Indemnitee's request, Borrower, or counsel designated by Borrower and satisfactory to the Indemnitee, will resist and defend such action, suit or proceeding to the extent and in the manner directed by the Indemnitee, at Borrower's sole costs and expense. Each Indemnitee will use its best efforts to cooperate in the defense of any such action, suit or proceeding. If the foregoing undertaking to indemnify, defend and hold harmless may be held to be unenforceable because it violates any law or public policy, Borrower shall nevertheless make the maximum contribution to the payment and satisfaction of each of the Indemnified Liabilities which is permissible under applicable law. Borrower's obligation under this Section 8.6 shall survive the termination of this Agreement and the discharge of Borrower's other obligations hereunder.

Section 8.7. *Participants.* Borrower hereby authorizes Bank to disclose to any assignee or any participant (either, a "Transferee") and any prospective Transferee any and all financial information in Bank's possession concerning Borrower which has been delivered to Bank by Borrower pursuant to this Agreement or which has been delivered to Bank by Borrower in connection with Bank's credit evaluation prior to entering into this Agreement. Bank and its participants, if any, are not partners or joint venturers, and Bank shall not have any liability or responsibility for any obligation, act or omission of any of its participants. All rights and powers specifically conferred upon Bank may be transferred or delegated to any of Bank's participants, successors or assigns.

Section 8.8. *Advertising and Promotion.* Borrower agrees that Bank may use Borrower's name in advertising and promotional materials, and in conjunction therewith, Bank may disclose the amount of the Credit Facility and the purpose thereof.

Section 8.9. *Execution in Counterparts; Telefacsimile Execution.* This Agreement and the other Loan Documents may be executed in any number of counterparts, each of which when so executed and delivered shall be deemed to be an original and all of which counterparts, taken together, shall constitute but one and the same instrument. Delivery of an executed counterpart of this Agreement by telefacsimile shall be equally as effective as delivery of an original executed counterpart of this Agreement. Any party delivering an executed counterpart of this Agreement by telefacsimile also shall deliver an original executed counterpart of this Agreement but the failure to deliver an original executed counterpart shall not affect the validity, enforceability, and binding effect of this Agreement.

Section 8.10. *Retention of Borrower's Records.* Bank shall have no obligation to maintain any electronic records or any documents, schedules, invoices, agings, or other papers delivered to Bank by Borrower or in connection with the Loan Documents for more than twelve

months after receipt by Bank; *provided* that Borrower shall not have any obligation to provide Bank with duplicate records and documents after the same have been destroyed by Bank.

Section 8.11. *Binding Effect; Assignment; Complete Agreement; Exchanging Information.* The Loan Documents shall be binding upon and inure to the benefit of Borrower and Bank and their respective successors and assigns, except that Borrower shall not have the right to assign its rights thereunder or any interest therein without Bank's prior written consent. Bank shall not assign any of its rights and obligations arising under this Agreement or the Line of Credit Note without the prior written consent of Borrower, which consent shall not be unreasonably withheld or delayed; *provided* notwithstanding the foregoing, Borrower's consent to any such assignment shall not be required (i) if a Default Period has occurred and is continuing, (ii) if Bank assigns this Agreement in connection with any sale or all or any portion of its loan portfolio, or (iii) if Bank assigns this Agreement to any Affiliate of Bank. To the extent permitted by law, Borrower waives and will not assert against any assignee any claims, defenses or set-offs which Borrower could assert against Bank. This Agreement shall also bind all Persons who become a party to this Agreement as Borrower. This Agreement, together with the Loan Documents, comprises the complete and integrated agreement of the parties on the subject matter hereof and supersedes all prior agreements, written or oral, on the subject matter hereof. Without limiting Bank's right to share information regarding Borrower and its Affiliates with Bank's participants, accountants, lawyers and other advisors, Bank, Wells Fargo & Company, and all direct and indirect subsidiaries of Wells Fargo & Company, may exchange any and all information they may have in their possession regarding Borrower and its Affiliates, and Borrower waives any right of confidentiality it may have with respect to such exchange of such information.

Section 8.12. *Severability of Provisions.* Any provision of this Agreement which is prohibited or unenforceable shall be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof.

Section 8.13. *Revival and Reinstatement of Obligations.* If the incurrence or payment of the Obligations by Borrower or any Guarantor or the transfer to Bank of any property should for any reason subsequently be declared to be void or voidable under any state or federal law relating to creditors' rights, including provisions of the Bankruptcy Code relating to fraudulent conveyances, preferences, or other voidable or recoverable payments of money or transfers of property (collectively, a "*Voidable Transfer*"), and if Bank is required to repay or restore, in whole or in part, any such Voidable Transfer, or elects to do so upon the reasonable advice of its counsel, then, as to any such Voidable Transfer, or the amount thereof that Bank is required or elects to repay or restore, and as to all reasonable costs, expenses, and attorneys fees of Bank related thereto, the liability of Borrower or any Guarantor automatically shall be revived, reinstated, and restored and shall exist as though such Voidable Transfer had never been made.

Section 8.14. *Headings.* Article, Section and subsection headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

Section 8.15. *GOVERNING LAW.* This agreement and the other loan documents (except as otherwise specified therein), and the rights and duties of the parties hereto, shall be construed and determined in accordance with the internal laws of the state of California.

Section 8.16. *SUBMISSION TO JURISDICTION.* Subject to section 8.17: (i) any legal action or proceeding with respect to this Agreement or any other Loan Document may be brought solely in the courts of the state of California or of the United States for the Northern District of California, and, by execution and delivery hereof, each of Borrower and Bank consents, for itself and in respect of its property, to the jurisdiction of those courts; (ii) each of Borrower and Bank irrevocably waives any objection, including any objection to the laying of venue or based on the grounds of forum non conveniens, which it may now or hereafter have to the bringing of any action or proceeding in such jurisdiction in respect of this agreement or any document related hereto. Each of Borrower and Bank waives personal service of any summons, complaint or other process, which may be made by any other means permitted by California law.

Section 8.17. *WAIVER OF JURY TRIAL.* Each of Borrower and Bank, to the fullest extent permitted by applicable law, hereby irrevocably waives all right to a trial by jury in any action, proceeding, counterclaim or other litigation in any way arising out of or relating to this Agreement, any other of the Loan Documents or any of the transactions or events referenced herein or therein or contemplated hereby or thereby, whether with respect to contract claims, tort claims or otherwise. This waiver shall apply to any subsequent amendments, renewals, supplements or modifications to this Agreement or any other of the Loan Documents. A copy of this section 8.17 may be filed with any court as written evidence of the waiver of the right to trial by jury and the consent to trial by court.

Section 8.18. *Arbitration.*

(a) *Arbitration.* The parties hereto agree, upon demand by any party, to submit to binding arbitration all claims, disputes and controversies between or among them (and their respective employees, officers, directors, attorneys, and other agents), whether in tort, contract or otherwise arising out of or relating to in any way (i) the loan and related Loan Documents which are the subject of this Agreement and its negotiation, execution, collateralization, administration, repayment, modification, extension, substitution, formation, inducement, enforcement, default or termination; or (ii) requests for additional credit.

(b) *Governing Rules.* Any arbitration proceeding will (i) proceed in a location in California selected by the American Arbitration Association (“AAA”); (ii) be governed by the Federal Arbitration Act (Title 9 of the United States Code), notwithstanding any conflicting choice of law provision in any of the documents between the parties; and (iii) be conducted by the AAA, or such other administrator as the parties shall mutually agree upon, in accordance with the AAA’s commercial dispute resolution procedures, unless the claim or counterclaim is at

least \$1,000,000.00 exclusive of claimed interest, arbitration fees and costs in which case the arbitration shall be conducted in accordance with the AAA's optional procedures for large, complex commercial disputes (the commercial dispute resolution procedures or the optional procedures for large, complex commercial disputes to be referred to, as applicable, as the "Rules"). If there is any inconsistency between the terms hereof and the Rules, the terms and procedures set forth herein shall control. Any party who fails or refuses to submit to arbitration following a demand by any other party shall bear all costs and expenses incurred by such other party in compelling arbitration of any dispute. Nothing contained herein shall be deemed to be a waiver by any party that is a bank of the protections afforded to it under 12 U.S.C. §91 or any similar applicable state law.

(c) *No Waiver of Provisional Remedies, Self-Help and Foreclosure.* The arbitration requirement does not limit the right of any party to (i) foreclose against real or personal property collateral; (ii) exercise self-help remedies relating to collateral or proceeds of collateral such as setoff or repossession; or (iii) obtain provisional or ancillary remedies such as replevin, injunctive relief, attachment or the appointment of a receiver, before during or after the pendency of any arbitration proceeding. This exclusion does not constitute a waiver of the right or obligation of any party to submit any dispute to arbitration or reference hereunder, including those arising from the exercise of the actions detailed in sections (i), (ii) and (iii) of this paragraph.

(d) *Arbitrator Qualifications and Powers.* Any arbitration proceeding in which the amount in controversy is \$5,000,000.00 or less will be decided by a single arbitrator selected according to the Rules, and who shall not render an award of greater than \$5,000,000.00. Any dispute in which the amount in controversy exceeds \$5,000,000.00 shall be decided by majority vote of a panel of three arbitrators; *provided however*, that all three arbitrators must actively participate in all hearings and deliberations. The arbitrator will be a neutral attorney licensed in the State of California or a neutral retired judge of the state or federal judiciary of California, in either case with a minimum of ten years experience in the substantive law applicable to the subject matter of the dispute to be arbitrated. The arbitrator will determine whether or not an issue is arbitratable and will give effect to the statutes of limitation in determining any claim. In any arbitration proceeding the arbitrator will decide (by documents only or with a hearing at the arbitrator's discretion) any pre-hearing motions which are similar to motions to dismiss for failure to state a claim or motions for summary adjudication. The arbitrator shall resolve all disputes in accordance with the substantive law of California and may grant any remedy or relief that a court of such state could order or grant within the scope hereof and such ancillary relief as is necessary to make effective any award. The arbitrator shall also have the power to award recovery of all costs and fees, to impose sanctions and to take such other action as the arbitrator deems necessary to the same extent a judge could pursuant to the Federal Rules of Civil Procedure, the California Rules of Civil Procedure or other applicable law. Judgment upon the award rendered by the arbitrator may be entered in any court having jurisdiction. The institution and maintenance of an action for judicial relief or pursuit of a provisional or ancillary remedy shall not constitute a waiver of the right of any party, including the plaintiff, to submit the controversy or claim to arbitration if any other party contests such action for judicial relief.

(e) *Discovery.* In any arbitration proceeding discovery will be permitted in accordance with the Rules. All discovery shall be expressly limited to matters directly relevant to the dispute being arbitrated and must be completed no later than 20 days before the hearing date and within 180 days of the filing of the dispute with the AAA. Any requests for an extension of the discovery periods, or any discovery disputes, will be subject to final determination by the arbitrator upon a showing that the request for discovery is essential for the party's presentation and that no alternative means for obtaining information is available.

(f) *Class Proceedings and Consolidations.* The resolution of any dispute arising pursuant to the terms of this Agreement shall be determined by a separate arbitration proceeding and such dispute shall not be consolidated with other disputes or included in any class proceeding.

(g) *Payment Of Arbitration Costs And Fees.* The arbitrator shall award all costs and expenses of the arbitration proceeding.

(h) *Real Property Collateral; Judicial Reference.* Notwithstanding anything herein to the contrary, no dispute shall be submitted to arbitration if the dispute concerns indebtedness secured directly or indirectly, in whole or in part, by any real property unless (i) the holder of the mortgage, lien or security interest specifically elects in writing to proceed with the arbitration, or (ii) all parties to the arbitration waive any rights or benefits that might accrue to them by virtue of the single action rule statute of California, thereby agreeing that all indebtedness and obligations of the parties, and all mortgages, liens and security interests securing such indebtedness and obligations, shall remain fully valid and enforceable. If any such dispute is not submitted to arbitration, the dispute shall be referred to a referee in accordance with California Code of Civil Procedure Section 638 et seq., and this general reference agreement is intended to be specifically enforceable in accordance with said Section 638. A referee with the qualifications required herein for arbitrators shall be selected pursuant to the AAA's selection procedures. Judgment upon the decision rendered by a referee shall be entered in the court in which such proceeding was commenced in accordance with California Code of Civil Procedure Sections 644 and 645.

(i) *Miscellaneous.* To the maximum extent practicable, the AAA, the arbitrators and the parties shall take all action required to conclude any arbitration proceeding within 180 days of the filing of the dispute with the AAA. No arbitrator or other party to an arbitration proceeding may disclose the existence, content or results thereof, except for disclosures of information by a party required in the ordinary course of its business or by applicable law or regulation. If more than one agreement for arbitration by or between the parties potentially applies to a dispute, the arbitration provision most directly related to the Loan Documents or the subject matter of the dispute shall control. This arbitration provision shall survive termination, amendment or expiration of any of the Loan Documents or any relationship between the parties.

Section 8.19. *Confidentiality.* Bank shall hold all confidential non-public information obtained by Bank in accordance with Bank's customary procedures for handling confidential information of this nature; *provided* that Bank may disclose such confidential information (i) to its examiners, Affiliates, outside auditors, counsel and other professional advisors on a need to

know basis, (ii) to any prospective participant or transferee of Bank's rights or obligations hereunder, provided such participant or transferee agrees, prior to the disclosure of such information by Bank, to be bound by the terms of this Section 8.19 with respect to such information and (iii) as required or requested by any Governmental Authority or representative thereof or pursuant to legal process; *provided further* that this duty shall expire if such information becomes publicly available through no breach of this Section 8.19 by Bank; *provided further* that unless specifically prohibited by applicable law or court order, Bank shall use commercially reasonable efforts, prior to disclosure thereof, to notify Borrower of the request for disclosure of such non-public information (A) by a Governmental Authority or representative thereof or (B) pursuant to legal process. Notwithstanding anything herein to the contrary, Bank may disclose to any and all Persons, without limitation of any kind, any information with respect to the "tax treatment" and "tax structure" (in each case, within the meaning of Treasury Regulation Section 1.6011-4) of the transactions contemplated hereby and all materials of any kind (including opinions or other tax analyses) that are provided Bank relating to such tax treatment and tax structure; *provided* that with respect to any document or similar item that in either case contains information concerning the tax treatment or tax structure of the transaction as well as other information, this sentence shall only apply to such portions of the document or similar item that relate to the tax treatment or tax structure of the transactions contemplated hereby.

Section 8.20. *Effect on Prior Agreement.* This Agreement amends and restates the Original Agreement in its entirety, effective as of the Closing Date, and is not intended to constitute a novation of the obligations thereunder. Nothing contained herein shall terminate any security interests, guaranties or subordinations in favor of Bank and all such security interests, guaranties and subordinations shall continue in full force and effect.

*[Signatures on Next Page]*

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

Apio, Inc.  
4575 West Main Street  
Guadalupe, CA 93434  
Telecopier: (805) 249-6257  
Attention: Kathleen Morgan  
e-mail: kmorgan@apioinc.com

Wells Fargo Bank, N.A.  
Peninsula RCBO  
400 Hamilton Avenue, P.O. Box 150  
Palo Alto, CA 94302  
Telecopier: (650) 328-0814  
Attention: Tim Palmer  
e-mail: palmert@wellsfargo.com

Apio, Inc.

By: /s/ Kathleen Morgan  
Kathleen Morgan  
Chief Financial Officer

Wells Fargo Bank, National Association

By: /s/ Tim Palmer  
Tim Palmer  
Vice President

Amended and Restated  
Credit Agreement

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**Table of Exhibits and Schedules**

Exhibit A	Form of Line of Credit Note
Exhibit B	Form of Borrowing Base Certificate
Exhibit C	Form of Compliance Certificate
Exhibit D	Premises
Schedule 5.1	Trade Names, Chief Executive Office, Principal Place of Business, and Locations of Collateral
Schedule 5.2	Capitalization and Organizational Chart
Schedule 5.5	Subsidiaries
Schedule 5.11	Intellectual Property Disclosures
Schedule 6.4	Permitted Liens
Schedule 6.5	Permitted Indebtedness and Guaranties

**FIFTH AMENDMENT TO CREDIT AGREEMENT**

LANDEC AG, INC., formerly know as Intellicoat Corporation, a Delaware corporation (the "Company") and OLD NATIONAL BANK, formerly known as American National Bank, a national banking association (the "Bank"), being parties to that certain Credit Agreement dated as of June 5, 2000, as previously amended (collectively, the "Agreement") hereby agree to further amend the Agreement by this Fifth Amendment to Credit Agreement (this "Amendment"), on the terms and subject to the conditions set forth as follows.

1. **DEFINITIONS.** Terms used in this Amendment with their initial letters capitalized are used as defined in the Agreement, unless otherwise defined herein.

a. **Amended Definitions.** The following definitions are hereby amended and restated in their respective entireties as follows:

\*\* "**Revolving Loan Maturity Date**" means October 31, 2005, and thereafter any subsequent date to which the Commitment may be extended by the Bank pursuant to the terms of Section 2(a)(iv).

b. **New Definition.** The following definition is hereby added to Section 1 of the Agreement as follows:

\*\* "**Fifth Amendment**" means that certain agreement entitled "Fifth Amendment to Credit Agreement" between the Company and the Bank dated as of October 7<sup>th</sup>, 2004.

2. **THE REVOLVING LOAN.** Section 2(a)(i), the first sentence of Section 2(a)(ii), and Section 2(a)(iii) of the Agreement are hereby amended and restated in their respective entireties as follows:

(i) **The Commitment — Use of Proceeds.** From the date of the Fifth Amendment and until the Revolving Loan Maturity Date, the Bank agrees to make Advances (collectively, the "Revolving Loan") under a revolving line of credit from time to time to the Company of amounts not exceeding in the aggregate at any time outstanding the lesser of Seven Million Five Hundred Thousand and 00/100 Dollars (\$7,500,000.00) (the "Commitment") or the Borrowing Base, provided that all of the conditions of lending stated in Section 7 of this Agreement as being applicable to the Revolving Loan have been fulfilled at the time of each Advance. Proceeds of the Revolving Loan may be used by the Company only for working capital purposes.

(ii) **Method of Borrowing.** The obligation of the Company to repay the Revolving Loan shall be evidenced by the Promissory Note of the

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Company in the form of Exhibit "A" attached to the Fifth Amendment (the "Revolving Note").

- (iii) Interest on the Revolving Loan. The principal amount of the Revolving Loan outstanding from time to time shall bear interest until maturity of the Revolving Note at a rate per annum equal to the Prime Rate plus three eighths of one percent (.375%). After maturity, whether on the Revolving Loan Maturity Date or on account of acceleration upon the occurrence of an Event of Default, and until paid in full, the Revolving Loan shall bear interest at a per annum rate equal to the Prime Rate plus four and one-half percent (4-1/2%). Accrued interest shall be due and payable monthly on the last Banking Day of each month prior to maturity. After maturity, interest shall be payable as accrued and without demand.

3. **REPRESENTATIONS AND WARRANTIES.** To induce the Bank to enter into this Amendment, the Company affirms that the representations and warranties continued in the Agreement are correct and accurate as of the date of this Amendment, except that (i) they shall be deemed also to refer this Amendment, as well as all documents named herein, and (ii) Section 3(d) shall be deemed also to refer to the most recent audited and unaudited financial statements of the Company furnished to the Bank.

4. **EVENTS OF DEFAULT.** The Company certifies to the Bank that no Event of Default or Unmatured Event of Default under the Agreement has occurred and is continuing as of the date of this Amendment.

5. **CONDITIONS PRECEDENT.** This Amendment shall become effective upon receipt of the following by the Bank, duly executed and in form and substance satisfactory to the Bank:

- a. This Amendment.
- b. The Revolving Loan Note in the form attached hereto as Exhibit "A".
- c. The Reaffirmation of Guaranty Agreement in the form attached hereto as Exhibit "B." duly executed by Landec Corporation.
- e. The Acknowledgment and Consent of Subordinated Creditor in the form attached hereto as Exhibit "C." duly executed by Landec Corporation.
- f. A Resolution of the Board of Directors of the Company authorizing the execution, delivery and performance of this Amendment and the other Loan Documents named herein to which the Company is a party certified as of the closing date by the Secretary of the Board of Directors.

- g. A certificate of the Secretary of the Board of Directors of the Company certifying the names of the officer or officers authorized to sign this Amendment and other Loan Documents named herein to which the Company is a party.
- h. A Resolution of the Board of Directors of Landec authorizing the execution, delivery and performance of the Reaffirmation of Guaranty Agreement, the Acknowledgment and Consent of Subordinated Creditor, and the other Loan Documents named herein to which Landec is a party certified as of the closing date by the Secretary of the Board of Directors.
- i. A certificate of the Secretary of the Board of Directors of the Landec certifying the names of the officer or officers authorized to execute the Reaffirmation of Guaranty Agreement, the Acknowledgment and Consent of Subordinated Creditor, and other Loan Documents named herein to which Landec is a party.
- j. Payment of the reasonable attorneys' fees of counsel for the Bank incurred in connection with the drafting and negotiation of this Amendment; and
- k. Such other instruments, agreements, and documents as may be required by the Bank pursuant hereto.

9. **EFFECT OF FIFTH AMENDMENT.** Except as amended by this Amendment, all of the terms and conditions of the Agreement shall continue unchanged and in full force and effect together with this Amendment.

**IN WITNESS WHEREOF**, the Company and the Bank, by their respective duly authorized officers, have executed and delivered in Indiana this Fifth Amendment to Credit Agreement as of October 7, 2004.

**LANDEC AG, INC.**, formerly known as  
Intellicoat Corporation, a Delaware corporation

By: /s/ Michael E. Godlove  
Michael E. Godlove, Chief Financial Officer

**OLD NATIONAL BANK**, formerly known as  
American National Bank, a national banking association

By: /s/ John T. Travis, SVP  
John T. Travis, Senior Vice President and Senior Lender

**SCHEDULE OF EXHIBITS**

- Exhibit "A" — Promissory Note (Revolving Loan) (\$7,500,000.00)
- Exhibit "B" — Reaffirmation of Guaranty Agreement (Landec Corporation)
- Exhibit "C" — Acknowledgment and Consent of Subordinated Creditor (Landec Corporation)

**SIXTH AMENDMENT TO CREDIT AGREEMENT**

LANDEC AG, INC., formerly know as Intellicoat Corporation, a Delaware corporation (the "Company") and OLD NATIONAL BANK, formerly known as American National Bank, a national banking association (the "Bank"), being parties to that certain Credit Agreement dated as of June 5, 2000, as previously amended (collectively, the "Agreement") hereby agree to further amend the Agreement by this Sixth Amendment to Credit Agreement (the "Amendment"), on the terms and subject to the conditions set forth as follows.

1. **DEFINITIONS.** Terms used in this Amendment with their initial letters capitalized are used as defined in the Agreement, unless otherwise defined herein.

a. **Amended Definitions.** The following definitions are hereby amended and restated in their respective entireties as follows:

\*\* "**Revolving Loan Maturity Date**" means October 7, 2006, and thereafter any subsequent date to which the Commitment may be extended by the Bank pursuant to the terms of Section 2(a)(iv).

b. **New Definition.** The following definition is hereby added to Section 1 of the Agreement as follows:

\*\* "**Sixth Amendment**" means that certain agreement entitled "Sixth Amendment to Credit Agreement" between the Company and the Bank dated as of October 7, 2005.

2. **THE REVOLVING LOAN.** Section 2(a)(iii) of the Agreement is hereby amended and restated in its entirety as follows:

(iii) **Interest on the Revolving Loan.** The principal amount of the Revolving Loan outstanding from time to time shall bear interest until maturity of the Revolving Note at a rate per annum equal to the Prime Rate. After maturity, whether on the Revolving Loan Maturity Date or on account of acceleration upon the occurrence of an Event of Default, and until paid in full, the Revolving Loan shall bear interest at a per annum rate equal to the Prime Rate plus four and one-half percent (4-1/2%). Accrued interest shall be due and payable monthly on the last Banking Day of each month prior to maturity. After maturity, interest shall be payable as accrued and without demand.

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3. **AFFIRMATIVE COVENANTS OF THE COMPANY.** Section 5(b)(iv) of the Agreement is hereby amended and restated in its entirety as follows:

(iv) **Borrowing Base Certificates.** As of such dates as the Bank may reasonably require.

4. **NEGATIVE COVENANTS OF THE COMPANY.** Sections 6a(i) and (ii) of the Agreement are hereby amended and restated in their entirety as follows:

(i) **Ratio of Liabilities to Tangible Capital Base.** The Company shall maintain at all times the ratio of its total liabilities less Subordinated Debt to its Tangible Capital Base at a level not greater than 2.00 to 1.00, tested as of the end of each calendar quarter. For purposes of testing compliance with this covenant, the term “liabilities” shall include the present value of all capital lease obligations of the Company, determined as of any date the ratio is to be tested.

(ii) **Cash Flow Coverage Ratio.** The Company shall maintain a cash flow coverage ratio of not less than 1.25 to 1.00, tested annually as of the Fiscal Year End of the Company. For purposes of this covenant, the phrase “cash flow coverage ratio” means the ratio of: (A) the Company’s EBITDA over (B) the sum of the principal paid plus interest expense.

5. **RENEWAL FEE.** In consideration of the renewal of the Revolving Loan and the decrease in the interest rate applicable to the Revolving Loan, the Company agrees to pay the Bank, a fee of Ten Thousand and 00/100 Dollars (\$10,000.00) simultaneously with execution of this Amendment.

6. **REPRESENTATIONS AND WARRANTIES.** To induce the Bank to enter into this Amendment, the Company affirms that the representations and warranties continued in the Agreement are correct and accurate as of the date of this Amendment, except that (i) they shall be deemed also to refer this Amendment, as well as all documents named herein, and (ii) Section 3(d) shall be deemed also to refer to the most recent audited and unaudited financial statements of the Company furnished to the Bank.

7. **EVENTS OF DEFAULT.** The Company certifies to the Bank that no Event of Default or Unmatured Event of Default under the Agreement has occurred and is continuing as of the date of this Amendment.

8. **CONDITIONS PRECEDENT.** This Amendment shall become effective upon receipt of the following by the Bank, duly executed and in form and substance satisfactory to the Bank:

a. This Amendment.



- b. The Revolving Loan Note in the form attached hereto as Exhibit "A".
- c. The Reaffirmation of Guaranty Agreement in the form attached hereto as Exhibit "B," duly executed by Landec Corporation.
- e. The Acknowledgment and Consent of Subordinated Creditor in the form attached hereto as Exhibit "C," duly executed by Landec Corporation.
- f. A Resolution of the Board of Directors of the Company authorizing the execution, delivery and performance of this Amendment and the other Loan Documents named herein to which the Company is a party certified as of the closing date by the Secretary of the Board of Directors.
- g. A certificate of the Secretary of the Board of Directors of the Company certifying the names of the officer or officers authorized to sign this Amendment and other Loan Documents named herein to which the Company is a party.
- h. A Resolution of the Board of Directors of Landec authorizing the execution, delivery and performance of the Reaffirmation of Guaranty Agreement, the Acknowledgment and Consent of Subordinated Creditor, and the other Loan Documents named herein to which Landec is a party certified as of the closing date by the Secretary of the Board of Directors.
- i. A certificate of the Secretary of the Board of Directors of the Landec certifying the names of the officer or officers authorized to execute the Reaffirmation of Guaranty Agreement, the Acknowledgment and Consent of Subordinated Creditor, and other Loan Documents named herein to which Landec is a party.
- j. Payment of the reasonable attorneys' fees of counsel for the Bank incurred in connection with the drafting and negotiation of this Amendment; and
- k. Such other instruments, agreements, and documents as may be required by the Bank pursuant hereto.

9. **EFFECT OF SIXTH AMENDMENT.** Except as amended by this Amendment, all of the terms and conditions of the Agreement shall continue unchanged and in full force and effect together with this Amendment.

**IN WITNESS WHEREOF**, the Company and the Bank, by their respective duly authorized officers, have executed and delivered in Indiana this Sixth Amendment to Credit Agreement as of October 7, 2005.

**LANDEC AG, INC.**, formerly known as Intellicoat Corporation, a Delaware corporation

By: /s/ Michael E. Godlove  
Michael E. Godlove, Chief Financial Officer

**OLD NATIONAL BANK**, formerly known as American National Bank, a national banking association

By: /s/ John T. Travis  
John T. Travis, Senior Vice President



**SCHEDULE OF EXHIBITS**

- Exhibit "A" — Promissory Note (Revolving Loan) (\$7,500,000.00)
- Exhibit "B" — Reaffirmation of Guaranty Agreement (Landec Corporation)
- Exhibit "C" — Acknowledgment and Consent of Subordinated Creditor (Landec Corporation)

CERTIFICATION

I, Gary T. Steele, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Landec Corporation;
2. Based on my knowledge, this quarterly 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 quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly 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 quarterly report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this quarterly report based on such evaluation, and
  - (d) disclosed in this quarterly 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 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: January 6, 2006

/s/ Gary T. Steele

Gary T. Steele  
Chief Executive Officer

## CERTIFICATION

I, Gregory S. Skinner, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Landec Corporation;
2. Based on my knowledge, this quarterly 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 quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly 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 quarterly report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles ;
  - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this quarterly report based on such evaluation; and
  - (d) disclosed in this quarterly 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 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: January 6, 2006

/s/ Gregory S. Skinner

Gregory S. Skinner  
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 Quarterly Report of Landec Corporation (the "Company") on Form 10-Q for the period ending November 27, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Gary T. Steele, Chief Executive Officer and President of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Date: January 6, 2006

/s/ Gary T. Steele  
Gary T. Steele  
*Chief Executive Officer and President*  
*(Principal Executive Officer)*

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\* The foregoing certification is being furnished solely pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and is not being filed as part of the Form 10-Q or as a separate disclosure document.

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 Quarterly Report of Landec Corporation (the "Company") on Form 10-Q for the period ending November 27, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Gregory S. Skinner, Vice President of Finance and Administration and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Date: January 6, 2006

/s/ Gregory S. Skinner  
Gregory S. Skinner  
*Vice President and Chief Financial Officer*  
*(Principal Accounting Officer)*

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\* The foregoing certification is being furnished solely pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and is not being filed as part of the Form 10-Q or as a separate disclosure document.