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COMPANY DATA:
COMPANY CONFORMED NAME: DIGITAL ISLAND INC
CENTRAL INDEX KEY: 0001084329
STANDARD INDUSTRIAL CLASSIFICATION: []
IRS NUMBER: 680322824
STATE OF INCORPORATION: CA
FISCAL YEAR END: 0930

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BUSINESS ADDRESS:
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STATE: HI
ZIP: 96813
BUSINESS PHONE: 8085404000

MAIL ADDRESS:
STREET 1: 1132 BISHOP ST
STREET 2: STE 1001
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STATE: HI
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As filed with the Securities and Exchange Commission on April 26, 1999
Registration No. 333-

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM S-1
REGISTRATION STATEMENT
Under
The Securities Act of 1933

DIGITAL ISLAND, INC.
(Exact Name of Registrant as Specified in its Certificate of Incorporation)

<TABLE>
<S> <C> <C>
Delaware 4813 68-0322824
(State or Other Jurisdiction of Incorporation or Organization) (Primary Standard Industrial Classification Code Number) (I.R.S. Employer Identification Number)
</TABLE>

353 Sacramento Street, Suite 1520
San Francisco, CA 94111
(415) 228-4100
(Address, Including Zip Code, and Telephone Number, Including Area Code, of the Registrant's Principal Executive Offices)

T.L. Thompson
Chief Financial Officer
DIGITAL ISLAND, INC.
353 Sacramento Street, Suite 1520
San Francisco, CA 94111
(415) 228-4100

(Name and Address, Including Zip Code, and Telephone Number, Including Area Code, of Agent for Service)

Copies to:

<TABLE>
<CAPTION>

<S> <C>

Therese A. Mrozek, Esq.
Curtis L. Mo, Esq.
Rodrigo M. Guidero, Esq.
Andrew R. Hull, Esq.
Brobeck, Phleger & Harrison llp
Two Embarcadero Place
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(650) 424-0160

Gregory C. Smith, Esq.
Michael J. Cordero, Esq.
Christopher A. Rose, Esq.
Skadden, Arps, Slate, Meagher & Flom llp
525 University Avenue, Suite 220
Palo Alto, California 94301
(650) 470-4500

</TABLE>

Approximate date of commencement of proposed sale to the public:
As soon as practicable after this Registration Statement becomes effective.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box. [_]

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [_]

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [_]

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [_]

If delivery of the prospectus is expected to be made pursuant to Rule 434, check the following box. [_]

CALCULATION OF REGISTRATION FEE

- ---
- ---

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Title of Each Class of Securities to be Registered	Proposed Maximum Aggregate Offering Price(1)	Amount of Registration Fee

- ----------
<S> <C> <C>
Common Stock, $0.001 par value.. $75,000,000 $20,850
- ----------
- ----------
</TABLE>
(1) Estimated solely for the purpose of computing the registration fee pursuant to Rule 457(o) under the Securities Act of 1933, as amended.

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment that specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, or until the Registration Statement shall become effective on such date as the Commission, acting pursuant to such Section 8(a), may determine.

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+The information in this prospectus is not complete and may be changed. We may +
+not sell these securities until the registration statement filed with the +
+Securities and Exchange Commission is effective. This prospectus is not an +
+offer to sell these securities, and we are not soliciting offers to buy these +
+securities, in any state where the offer or sale is not permitted. +
++
++
++

SUBJECT TO COMPLETION, DATED APRIL , 1999

PRELIMINARY PROSPECTUS

Shares

[LOGO]

Digital Island, Inc.

Common Stock

This is an initial public offering of shares of our common stock. We are selling all of the shares of common stock offered under this prospectus.

There is currently no public market for our shares. We intend to apply to have

our common stock approved for listing on the Nasdaq National Market under the symbol "ISLD."

See "Risk Factors" beginning on page 8 to read about certain risks that you should consider before buying shares of our common stock.

Neither the Securities and Exchange Commission nor any other regulatory body has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

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	Per Share	Total
<S>	<C>	<C>
Public offering price.....	$	$
Underwriting discounts and commissions.....	$	$
Proceeds, before expenses, to us.....	$	$

</TABLE>

The underwriters under certain circumstances may purchase up to an additional shares of common stock from us at the initial public offering price less the underwriting discount, solely to cover over-allotments.

The underwriters are severally underwriting the shares being offered. The underwriters expect to deliver the shares against payment in New York, New York on or about , 1999.

Bear, Stearns & Co. Inc.

Lehman Brothers

Thomas Weisel Partners LLC

The date of this prospectus is , 1999

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[Graphic depiction of company products and services]

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PROSPECTUS SUMMARY

This summary contains basic information about us and this offering. Because it is a summary, it does not contain all of the information that you should consider before investing. You should read the entire prospectus carefully, including the section entitled "Risk Factors" and our Consolidated Financial Statements and the Notes thereto before making an investment decision. Our fiscal year ends on September 30. Unless otherwise indicated or required by the context, references to years in this prospectus refer to our fiscal years. In this prospectus, Digital Island, "we," "us," and "our" refers to Digital Island, Inc. but not to the underwriters listed in this prospectus.

DIGITAL ISLAND, INC.

We offer a leading global e-business network for companies that are using the Internet for worldwide deployment of business-critical applications. We have developed a private global Internet protocol applications network to avoid congestion points common on the public Internet and to intelligently allocate bandwidth and storage to maximize the performance and functionality of our customers' applications. We provide a complete range of applications hosting, server management and co-location services in our state-of-the-art data centers, and network management expertise in connection with our customers' own data centers. The e-business applications delivered over our network are accessed globally in the same way as any Web site, but with a significant difference: these e-business applications are highly available and are designed to operate substantially faster and with greater functionality than sites that rely solely on the public Internet.

We target multinational corporations that are increasingly relying on the Internet to conduct business but are constrained by its unreliability, slow performance and lack of functionality. Our Global Internet Protocol Applications Network and value-added services enable customers to effectively deploy and manage global applications by combining the reliability, performance, and functionality of private wide area networks with the global access of the public Internet. We also offer service level guarantees, customized billing, security services, network management and other application services designed to improve the performance of applications deployed on our network. Our customers, which include multinational corporations such as Autodesk, Cisco Systems, E*TRADE Group and National Semiconductor, use our services and proprietary technology to facilitate the deployment of a wide variety of applications, including electronic commerce, online customer service, software and multimedia document distribution, sales force automation and distance learning.

The public Internet infrastructure was designed for applications requiring limited bandwidth and for uses which were not business-critical. For enterprises requiring global solutions, the U.S.-centric nature of the public Internet results in poor response times, particularly for applications

requiring large file transfers, real time interaction and overseas transport. This occurs because data transmitted between countries must make a large number of connections or "hops" through various regional and national Internet service providers before reaching a destination. Data packets often become lost in the transfer process, especially data-intensive transfers involving large software downloads, multimedia document distribution and audio and video streaming. In seeking to address the performance issues of the public Internet, enterprises have increasingly found that investing in the resources and personnel required to maintain in-house private wide area networks is cost-prohibitive and extremely difficult given the shortage of technical talent and risk of technological obsolescence.

Our Global Internet Protocol Applications Network consists of a proprietary asynchronous transfer mode backbone connecting four strategically located data centers in Honolulu, London, New York City and Santa Clara, California. This core network architecture connects over dedicated lines directly to local Internet service providers in 17 countries. This enables our customers to transmit Internet traffic seamlessly over our proprietary backbone with dedicated transoceanic capacity and to connect directly to international users through local

points of presence. We also offer content distribution services, including mirroring and caching, which enable us to forward deploy our customers' applications in locations close to their end-users. This allows our customers to benefit from the lower overall cost of data storage versus transport and to provide a better online experience for their end-users.

We offer a variety of services that allow customers to benefit from the Digital Island global e-business network. Customers can take advantage of our extensive server management and hosting services offered at our four data centers and can purchase a range of transport options, including open, reserved or managed bandwidth. Our outsourced solutions are designed to allow customers to transfer to us the burden of attracting and retaining scarce technical staff and adopting continuously changing technologies, while lowering their operating costs and speeding deployment.

Our objective is to be the leading global e-business network. In order to achieve this objective, we intend to continue to:

- focus or leading multinational customers in targeted industries which utilize Internet technologies;

- extend our leadership in the market for global Internet protocol application services by continuing to expand our base of customers, and by increasing demand for network usage among our existing customers;

- develop and implement new Internet protocol technology and services that will allow our customers to optimize their deployment and operation of applications globally;

- expand strategic relationships with potential partners such as system integrators, software vendors, application services, and certain of our customers in targeted vertical markets; and

- expand our distribution capabilities in the U.S., Asia and Europe by hiring more direct sales personnel and developing additional agents and reseller channels.

We were incorporated in the State of California on February 10, 1994 and changed our name to Digital Island, Inc. on August 15, 1996. Our principal headquarters are located at 353 Sacramento Street, Suite 1520, San Francisco, California 94111, and our telephone number is (415) 228-4100. Information contained on our web site is not a part of this Prospectus.

Unless we indicate otherwise, all information in this prospectus assumes:

- the reincorporation of Digital Island in Delaware at or prior to the consummation of this offering;

- the conversion of each outstanding share of our convertible preferred stock of Digital Island into common stock immediately prior to the consummation of this offering;

- the exercise of outstanding warrants to purchase 95,000 shares of our common stock at an exercise price of $0.10 per share upon the consummation of this offering; and

- no exercise of the underwriters' over-allotment option.

<PAGE>

THE OFFERING

<TABLE>

<C>	<S>
Common Stock being offered.....	shares
Common Stock outstanding after this offering..	shares

Use of proceeds..... We plan to use the net proceeds from this offering for capital expenditures and working capital needs.

Proposed Nasdaq National Market symbol..... ISLD
</TABLE>

The common stock outstanding after this offering is based on the number of shares outstanding as of March 31, 1999, and excludes:

- 4,218,839 shares of common stock issuable upon exercise of outstanding options with a weighted average exercise price of $2.13 per share;

- 7,544,000 shares reserved for future issuance under our 1999 Stock Incentive Plan; and

- 300,000 shares reserved for future issuance under our 1999 Employee Stock Purchase Plan.

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SUMMARY CONSOLIDATED FINANCIAL DATA

<TABLE>
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	Years Ended September 30,		Six Months Ended March 31, (unaudited)	
	1997	1998	1998	1999
	(in thousands, except per share data)			
<S>	<C>	<C>	<C>	<C>
Statements of Operations Data:				
Revenue.....	$ 218	$ 2,343	$ 691	$ 3,795
Total costs and expenses.....	(5,594)	(18,971)	(7,547)	(18,410)
Loss from operations.....	(5,376)	(16,629)	(6,856)	(14,615)
Net loss.....	(5,289)	(16,277)	(6,793)	(14,360)
Basic and diluted loss per share.....	$ (3.53)	$ (7.28)	$ (3.07)	$ (6.07)
Shares used in basic and diluted loss per share.....	1,497,711	2,236,452	2,215,875	2,366,951
Basic and diluted pro forma				

loss per share.....	$ (1.35)	$ (.78)
Shares used in basic and diluted pro forma loss per share.....	12,042,539	18,353,258

<TABLE>
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	March 31, 1999	
		Pro Forma
	Actual	As Adjusted
	(in thousands)	
<S>	<C>	<C>
Balance Sheet Data:		
Cash, cash equivalents and short-term investments.....	$50,666	$
Total assets.....	62,359	
Long-term obligations, including current portion.....	4,039	
Total stockholders' equity.....	49,149	

</TABLE>

The above balance sheet data is shown:

- on an actual basis; and

- on a pro forma basis assuming the conversion of all outstanding shares of convertible preferred stock into common stock and the exercise of outstanding warrants to purchase 95,000 shares of common stock at an exercise price of $0.10 per share upon the consummation of this offering, and as adjusted to reflect the sale of shares of common stock by Digital Island at an assumed initial public offering price of $ per share and after deducting the underwriting discounts and commissions and estimated offering expenses.

See Notes 2 and 9 of Notes to Consolidated Financial Statements for the determination of shares used in computing basic and diluted loss per share.

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CAUTIONARY NOTE ON FORWARD-LOOKING STATEMENTS

Some of the matters discussed under the captions "Prospectus Summary," "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations," "Business" and elsewhere in this prospectus include

forward-looking statements. We have based these forward-looking statements on our current expectations and projections about future events, including, among other things,

- implementing our business strategy;
- obtaining and expanding market acceptance of the services we offer;
- forecasts of Internet and our market size and growth;
- predicting pricing trends in domestic and foreign telecommunications;
- meeting our requirements under key contracts; and
- competition in our market.

In some cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "potential," "continue," "expects," "anticipates," "intends," "plans," "believes," "estimates" and similar expressions. These statements are based on our current beliefs, expectations and assumptions and are subject to a number of risks and uncertainties. Actual results and events may vary significantly from those discussed in the forward-looking statements. A description of certain risks that could cause our results to vary appears under the caption "Risk Factors" and elsewhere in this prospectus. These forward-looking statements are made as of the date of this prospectus, and we assume no obligation to update them or to explain the reasons why actual results may differ. In light of these assumptions, risks and uncertainties, the forward-looking events discussed in this prospectus might not occur.

TRADEMARKS

The Digital Island name and logo, Digital Island Intelligent Network, Digital Island Global IP Applications Network, Digital Island Application Hosting and Content Distribution, Globeport, Digital Island Local Content Managers, TraceWare and the names of products and services offered by Digital Island (including those referred to in "Business") are trademarks, registered trademarks, service marks or registered service marks of Digital Island. This prospectus also includes product names, trade names and trademarks of other companies.

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RISK FACTORS

An investment in our shares is extremely risky. This section describes some, but not all, of the risks involved in purchasing our common stock. You should consider carefully the following risks, in addition to the other information

presented in this prospectus, in evaluating us and our business. Any of the following risks, as well as other risks not mentioned here, could seriously harm our business and prospects and cause the trading price of our common stock to decline, which in turn could cause you to lose all or part of your investment.

Risks Related to Digital Island

We have a short operating history, have incurred operating losses since our inception and expect future operating losses.

We were incorporated in 1994, and began offering our global IP applications network services in January 1997. Prior to such time, we were engaged in activities unrelated to our current operations, and as a result, the results of operations for such periods are not comparable to our results of operations for 1997 or any subsequent periods. We have a limited operating history and some of the members of our senior management team have been working together at Digital Island for less than one year. From inception, we have experienced operating losses, negative cash flows from operations and net losses in each quarterly and annual period. As of March 31, 1999, we had an accumulated deficit of approximately $36.0 million. The revenue and income potential of our business and market is unproven, and our limited operating history makes it difficult to evaluate us and our prospects.

Currently, we anticipate making significant investments in our network infrastructure and product development as well as our sales and marketing programs and personnel. Therefore, we believe that we will continue to experience significant losses on a quarterly and annual basis for the foreseeable future. You must consider us and our prospects in light of the risks and difficulties encountered by companies in new and rapidly evolving markets. Our ability to address these risks depends on a number of factors which include our ability to:

- market our brand name effectively;
- provide scalable, reliable and cost-effective services;
- continue to grow our infrastructure to accommodate new IP developments and increased capacity utilization of our network;
- expand our channels of distribution;
- retain and motivate qualified personnel; and
- respond to competition.

We may not be successful in meeting these challenges and addressing these risks and uncertainties. If we are unable to do so, our business will not be successful and the value of your investment in us will decline.

Although we have experienced growth in revenues in recent periods, this growth rate may not be indicative of future operating results. We may never be able to achieve or sustain profitability.

There are many factors beyond our control which may cause fluctuations in our quarterly operating results.

We expect to experience significant fluctuations in our future results of operations due to a variety of factors, many of which are outside of our control, including:

- demand for and market acceptance of our products and services;
- introductions of products and services or enhancements by us and our competitors;
- competitive factors that affect our pricing;

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- capacity utilization of our global IP applications network;
- reliable continuity of service and network availability;
- the availability and cost of bandwidth and our ability to increase bandwidth as necessary;
- the timing of customer installations;
- the mix of products and services we sell;
- the timing and magnitude of capital expenditures, including costs relating to the expansion of operations;
- the timing of expansion of our network infrastructure;
- fluctuations in bandwidth used by customers;
- the retention of key personnel;
- conditions specific to the Internet industry and other general economic factors; and
- new government legislation or regulation.

In addition, a relatively large portion of our expenses are fixed in the short-term, particularly with respect to telecommunications capacity,

depreciation, real estate and interest expenses and personnel, and therefore our results of operations are particularly sensitive to fluctuations in revenues. Due to the foregoing factors, we believe that period-to-period comparisons of our operating results are not necessarily meaningful and that such comparisons cannot be relied upon as indicators of future performance.

The success of our business is dependent upon our ability to price our services above the overall cost of bandwidth.

We purchase our bandwidth capacity on a fixed-price basis in advance of the sale of our services for such bandwidth. We sell our services, by contract, on the basis of actual usage. Our bandwidth costs currently are exceeding our revenues from the sale of services, which results in negative gross profit. In the future, we must obtain enough bandwidth to meet our projected customer needs, and we must realize adequate volume from our customers to support and justify such bandwidth capacity and expense. If we do not obtain adequate bandwidth capacity on acceptable terms and realize appropriate customer volume for such bandwidth, we will not achieve positive gross profit, and our business and prospects will suffer.

We expect that our cost to obtain bandwidth capacity for the transport of data over our network will decline over time as a result of, among other things, the large amount of capital currently being invested to build infrastructure providing additional bandwidth. We expect the prices we charge for data transported over our network will also decline over time as a result of, among other things, the lower cost of obtaining bandwidth and existing and new competition in the markets we address. As a result, our historical revenue rates are not indicative of future revenue based on comparable traffic volumes. More generally, our business is dependent on our ability to accurately predict the decline in costs of bandwidth and to sell our services at prices sufficient to enable our business to become profitable. Many of our existing and potential competitors have significantly greater resources than us, which could enable them to provide services at lower costs in order to capture new business and to expand or establish market share. If we fail to accurately predict the decline in costs of bandwidth and, in any event, if we are unable to sell our services at acceptable prices relative to our bandwidth costs, our business and prospects will suffer.

Our mirroring and caching business is compelling because these services eliminate a significant portion of the cost of transporting data by deploying data in close proximity to the end users. To the extent bandwidth costs decrease, the prices we may charge for these services will decrease as well. If the cost of bandwidth decreases in excess of our expectations, the value of these could be substantially reduced, which would harm our business and prospects.

Our business and prospects will suffer if we do not retain and expand our customer base.

Our success depends on the continued growth of our customer base and the retention of our customers. Our ability to attract new customers depends on a variety of factors, including:

- the willingness of businesses to outsource their Internet operations;
- the reliability and cost-effectiveness of our services; and
- our ability to effectively market such services.

To attract new customers we intend to significantly increase our sales and marketing expenditures. However, our efforts might not result in more sales as a result of the following factors:

- we may be unsuccessful in implementing our marketing strategies;
- we may be unsuccessful in hiring a sufficient number of qualified sales and marketing personnel; and
- any implemented strategies might not result in increased sales.

Any failure of our network infrastructure could negatively impact our business and prospects.

Our operations are dependent upon our ability to protect our network infrastructure against damage from:

- human error;
- fire;
- earthquakes;
- floods;
- power loss;
- telecommunications failures;
- sabotage;
- intentional acts of vandalism; and
- similar events.

Despite precautions taken by us, the occurrence of a natural disaster or other unanticipated problems at one or more of our data centers could result in service interruptions or significant damage to equipment. We have experienced temporary service interruptions in the past, and we could experience similar interruptions in the future. In addition, failure of our telecommunications providers to provide required data communications capacity to us could result in interruptions in our services. A reduction in, or termination of, services to our customers could cause our business and prospects to suffer.

Our customer contracts currently provide a limited service level warranty related to the continuous availability of service on a 24 hours a day, seven days per week basis, except for certain scheduled maintenance periods. This warranty is generally limited to a credit consisting of free service for a specified limited period of time for disruptions in Internet transmission services. To date, we have had no material expense related to such service level warranty. Should we incur significant obligations in connection with system downtime, our liability insurance may not be adequate to cover such expenses. Although our customer contracts typically provide for no recovery with respect to incidental, punitive, indirect and consequential damages resulting from damages to equipment or disruption of service, in the event of such damages, we may be found liable, and, in such event, such damages may exceed our liability insurance.

Due to the limited deployment of our services to date, the ability of our network to connect and manage a substantially larger number of customers at high transmission speeds is as yet unknown. Our network may not be able to be scaled up to expected customer levels while maintaining superior performance or that additional network capacity will be available from third-party suppliers as it is needed by us. In addition, as customers' usage of bandwidth increases, we will need to make additional investments in our infrastructure to maintain adequate downstream data transmission speeds, the availability of which may be limited or the cost of which may be significant. In addition, as we upgrade our infrastructure, we may encounter certain delays or failures. As a result, our network may be unable to achieve or maintain a sufficiently high capacity of data transmission as usage by our customers increases. Our failure to achieve or maintain high capacity data transmission could significantly reduce demand for our services and our business and prospects could suffer.

We cannot accurately predict the size of our market, and widespread acceptance of our products and services is uncertain.

We cannot accurately estimate the size of our market or the potential demand for our services. For the six months ended March 31, 1999, we had 48 billing customers, of which one, E*TRADE, accounted for approximately 16% of our revenues. We believe that market acceptance depends principally on our:

- marketing strategy and efforts;
- product and service differentiation and quality;
- extent of coverage;
- customer support;
- distribution and pricing strategies as compared to our competitors;
- industry reputation; and
- general economic conditions.

Some of the foregoing factors are beyond our control. If our customer base does not expand, our business and prospects will be harmed.

We may require additional capital in the future and may not be able to secure adequate funds on terms acceptable to us.

The expansion and development of our business will require significant capital to fund our operating losses, working capital needs and capital expenditures. Our principal capital expenditures and lease payments include the purchase, lease and installation of network equipment such as switches, routers, servers and storage devices. Our working capital is primarily comprised of accounts receivable, accounts payable and accrued expenses. The timing and amount of our future capital requirements may vary significantly depending on numerous factors, including regulatory, technological, competitive and other developments in our industry. During the next twelve months, we expect to meet our cash requirements with existing cash, cash equivalents and short-term investments, the net proceeds from this offering, cash flow from sales of our services and proceeds from existing and future working capital lines of credit and other borrowings. Our failure to generate sufficient cash flows from sales of services or to raise sufficient funds may require us to delay or abandon some or all of our development and expansion plans or otherwise forego market opportunities. Due to the uncertainty of these factors, our actual revenues and costs may vary from expected amounts, possibly to a material degree, and such variations are likely to affect our future capital requirements.

We may not be able to obtain future equity or debt financing on favorable terms or at all. In addition, our credit agreements contain certain covenants restricting our ability to incur further indebtedness, and future borrowing instruments such as credit facilities and lease agreements are likely to contain similar or more restrictive covenants and will likely require us to pledge assets as security for borrowings thereunder. Our

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inability to obtain additional capital on satisfactory terms may delay or prevent the expansion of our business which could cause our business and prospects to suffer.

Our failure to manage growth could adversely affect us.

The planned expansion of our operations will place a significant strain on our management, financial controls, operations systems, personnel and other resources. Our ability to manage our future growth, should it occur, will depend in large part upon a number of factors, including our ability to:

- control costs;
- maintain regulatory compliance;
- maintain effective quality controls;
- significantly expand our internal management and financial control systems;
- acquire a significant amount of equipment to support our network systems; and
- attract, assimilate and retain qualified personnel.

We expect that our customers increasingly will demand additional information and reports with respect to the services we provide. To do so, we must develop and implement an automated customer service system to handle these demands and enable future traffic growth. In addition, if we are successful in implementing our marketing strategy, we also expect the demands on our network infrastructure and technical support resources to grow rapidly, and we may experience difficulties responding to customer demand for our services and providing technical support in accordance with our customers' expectations. We expect that these demands will require not only the addition of new management personnel, but also the development of additional expertise by existing management personnel and the establishment of long-term relationships with third-party service vendors. We may not be able to keep pace with any growth, successfully implement and maintain our operational and financial systems or successfully obtain, integrate and utilize the employees, facilities, third-party vendors and equipment, or management, operational and financial resources necessary to manage a developing and expanding business in our evolving and increasingly competitive industry. If we are unable to manage growth effectively, our business and prospects will suffer.

Breaches of our network security could disrupt our services and jeopardize the security of confidential information stored in our computer systems.

Despite the implementation of network security measures, our network infrastructure is vulnerable to computer viruses, break-ins and similar disruptive problems caused by our customers or Internet users. Computer viruses, break-ins or other problems caused by third parties could lead to interruptions, delays or cessation in service to our customers and subscribers. Furthermore, such inappropriate use of the network by third parties could also potentially jeopardize the security of confidential information stored in our computer systems and our customers computer systems, which may result in liability to and may also deter potential customers. Although we intend to continue to implement industry-standard security measures, any measures we implement may be circumvented in the future. The costs and resources required to eliminate computer viruses and alleviate other security problems may result in interruptions or delays to our customers that could cause our business and prospects to suffer.

Our management team is new and we may not be able to recruit and retain the personnel we need to succeed.

We have recently hired a number of key employees and officers including our Chief Financial Officer and Vice President of Sales, each of whom has been with us for less than six months. The integration of new personnel has resulted and will continue to result in some disruption to our ongoing operations. Our failure to complete this integration in an efficient manner could harm our business and prospects.

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We are highly dependent on certain members of our management and engineering staff, including, without limitation, our President and Chief Executive Officer, Chief Technology Officer and Vice President of Marketing. The loss of one or more of these officers might impede the achievement of our business objectives. Furthermore, recruiting and retaining qualified technical personnel to perform research, development and technical support work is critical to our success. If our business grows, we will also need to recruit a significant number of management, technical and other personnel for our business. Competition for employees in our industry is intense. We may not be able to continue to attract and retain skilled and experienced personnel on acceptable terms.

We depend on third party suppliers for key components of our network infrastructure.

We are dependent on other companies to supply certain key components of our infrastructure, including bandwidth capacity leased from telecommunications network providers and networking equipment that, in the quantities and quality demanded by us, are available only from sole or limited sources. While we have entered into various agreements for carrier line capacity, any failure to obtain additional capacity, if required, would cause our business and prospects

to suffer. The routers and switches used in our infrastructure are currently supplied primarily by Cisco Systems. We purchase these components pursuant to purchase orders placed from time to time, we do not carry significant inventories of these components and, we have no guaranteed supply arrangements with this vendor. Any failure to obtain required products or services on a timely basis and at an acceptable cost would cause our business and prospects to suffer. In addition, any failure of our sole or limited source suppliers to provide products or components that comply with evolving Internet and telecommunications standards or that interoperate with other products or components used by us in our communications infrastructure could cause our business and prospects to suffer.

Our failure to adequately protect our proprietary rights may adversely affect us, and there is a risk of infringement.

We believe that patents and other proprietary rights are important to our business. Our policy is to file patent applications to protect our technology, inventions and improvements to our inventions that we consider important to our business. We principally rely upon a combination of copyright, trademark and trade secret laws, and contractual restrictions to protect our proprietary technology.

Patents. We believe the protection of patentable inventions is important to our future success. We currently have one U.S. patent application pending, relating to our TraceWare technology. However, none of our technology is patented abroad, nor do we currently have any international patent applications pending. Moreover, it is possible that:

- our pending patent application may not result in the issuance of patents;
- any patents that may be issued to us could still be successfully challenged by third parties, which could result in our loss of the right to prevent others from exploiting the inventions claimed in those patents;
- current and future competitors may independently develop similar technology, duplicate our products or design around any patents that may be issued to us;
- effective patent protection may not be available in every country in which we do business; and
- any patents that may be issued to us may not provide significant proprietary protection or commercial advantage to us.

Trademarks, Copyrights and Trade Secrets. We believe the protection of our copyrightable materials, trademarks and trade secrets is important to our future success. We rely on a combination of laws, such as copyright, trademark

and trade secret laws, and contractual restrictions, such as confidentiality agreements and licenses, to establish and protect our proprietary rights. In particular, we generally enter into confidentiality or

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license agreements with our employees and consultants and with our customers and corporations with whom we have strategic relationships, and maintain control over access to and distribution of our software, documentation and other proprietary information. In addition, we generally register our important trademarks with the United States Patent and Trademark Office, or PTO, to preserve their value and establish proof of our ownership and use of these trademarks. We have registered the mark "Digital Island" with the PTO and we have a pending trademark application for the mark "TraceWare" with the PTO. Our "Digital Island" mark is either registered or pending in several foreign countries. Despite any precautions that we have taken:

- laws and contractual restrictions may not be sufficient to prevent misappropriation of our technology or deter others from developing similar technologies;

- other companies may claim common law trademark rights based upon state or foreign law that precede our federal registration of such marks;

- effective trademark, copyright and trade secret protection may be unavailable or limited in certain foreign countries;

- policing unauthorized use of our products and trademarks is difficult, expensive and time-consuming and we are unable to determine the extent to which piracy of our products and trademarks may occur, particularly overseas; and

- any trademarks that may be issued to us may not provide significant proprietary protection or commercial advantage to us.

Our commercial success will also depend in part on our not infringing the proprietary rights of others and not breaching technology licenses that cover technology used in our products. It is uncertain whether any third party patents will require us to develop alternative technology or to alter our products or processes, obtain licenses or cease certain activities. If any such licenses are required, we may not be able to obtain such licenses on commercially favorable terms, if at all. Our failure to obtain a license to any technology that we may require to commercialize our products and services could cause our business and prospects to suffer. Litigation, which could result in substantial cost to us, may also be necessary to enforce any patents issued or licensed to us or to determine the scope and validity of third party proprietary rights.

We are subject to risks associated with entering into joint ventures.

Our strategy is to pursue international expansion through relationships and joint ventures with local Internet service providers and telecommunications carriers in other countries. We may not have a majority interest or control of the governing body of any such local operating joint venture. In any such joint venture in which we may participate, there will be a risk that the other joint venture partner may at any time have economic, business or legal interests or goals that are inconsistent with those of the joint venture or us. The risk also will be present that a joint venture partner may be unable to meet its economic or other obligations and that we may be required to fulfill those obligations. In addition, in any joint venture in which we do not have a majority interest, we may not have control over the operations or assets of such joint venture. We may not be able to establish peering relationships or joint ventures with local Internet service providers and telecommunications carriers in other countries on favorable terms or at all. Our failure to establish these relationships may cause our business and prospects to suffer.

Risks Related to Our Industry

The market in which we operate is highly competitive and has many more established competitors.

The market we serve is highly competitive. There are few substantial barriers to entry and we expect that this market will face additional competition from existing competitors and new market entrants in the future. The principal competitive factors in this market include:

- system engineering and technical expertise;
- IP network reliability and security;
- quality of service and scalability;
- broad geographic presence;
- customer service;
- brand name recognition;
- the variety of services offered;
- price;

. financial resources; and

. conformity with industry standards.

We may not have the resources or expertise to compete successfully in this market in the future. Our current and potential competitors in the market include:

. information technology and Internet outsourcing firms;

. national and regional Internet service providers; and

. global, regional and local telecommunications companies.

Our competitors may operate in one or more of these areas and include companies such as AboveNet Communications, Inc., AT&T Corp., Exodus Communications, Inc., GTE Corporation, MCI WorldCom, Inc. and certain business units of Frontier GlobalCenter, Inc. Many of our competitors have substantially greater financial, technical and marketing resources, larger customer bases, longer operating histories, greater name recognition and more established relationships in the industry than we do. As a result, certain of these competitors may be able to develop and expand their network infrastructures and service offerings more quickly, adapt to new or emerging technologies and changes in customer requirements more quickly, take advantage of acquisition and other opportunities more readily, devote greater resources to the marketing and sale of their products and services, and adopt more aggressive pricing policies than we are able to implement. In addition, these competitors have entered and will likely continue to enter into joint ventures or consortiums to provide additional services which are competitive with those provided by us.

Certain of our competitors may be able to provide customers with additional benefits in connection with their Internet systems and network solutions, including reduced communications costs, which could reduce the overall costs of their services relative to us. We may not be able to offset the effects of any such price reductions. In addition, we believe that the businesses in which we compete are likely to encounter consolidation in the near future, which could result in increased price and other competition that could cause our business and prospects to suffer.

Our market changes rapidly due to changing technology and evolving industry standards. Our future success will depend on our ability to meet the sophisticated needs of our customers.

The market for our services is characterized by rapidly changing technology, evolving industry standards and frequent new service introductions. Our future success will depend to a substantial degree on our ability to offer services that incorporate leading technology, address the increasingly sophisticated and varied needs of our current and prospective customers and respond to technological advances and emerging industry standards and practices on a

timely and cost-effective basis. You should be aware that:

- our technology or systems may become obsolete upon the introduction of alternative technologies;

- we may not have sufficient resources to develop or acquire new technologies or to introduce new services capable of competing with future technologies or service offerings; and

- the price of the services provided by us is expected to decline as rapidly as the cost of any competitive alternatives.

We may not be able to effectively respond to the technological requirements of the changing market. To the extent we determine that new technologies and equipment are required to remain competitive, the development, acquisition and implementation of such technologies and equipment are likely to continue to require significant capital investment by us. Sufficient capital may not be available for this purpose in the future, and even if it is available, investments in new technologies may not result in commercially viable technological processes and there may not be commercial applications for such technologies. However, if we do not develop and introduce new products and services and achieve market acceptance in a timely manner, our business and prospects may suffer.

We depend on demand for and market acceptance of the Internet and its infrastructure development.

The increased use of the Internet for retrieving, sharing and transferring information among businesses, consumers, suppliers and partners has only begun to develop in recent years, and our success will depend in large part on continued growth in the use of the Internet. Critical issues concerning the commercial use of the Internet, including security, reliability, cost, ease of access, quality of service, regulatory initiatives and necessary increases in bandwidth availability, remain unresolved and are likely to affect the development of the market for our services. The adoption of the Internet for information retrieval and exchange, commerce and communications generally will require the acceptance of a new medium of conducting business and exchanging information. Demand for and market acceptance of the Internet are subject to a high level of uncertainty and are dependent on a number of factors, including:

- the growth in consumer access to and acceptance of new interactive technologies;

- the development of technologies that facilitate interactive communication between organizations; and

. increases in user bandwidth.

If the Internet as a commercial or business medium fails to develop or develops more slowly than expected, our business and prospects could suffer.

We are subject to risks associated with information disseminated through our network.

The law relating to the liability of online services companies and Internet access providers for information carried on or disseminated through their networks is currently unsettled. It is possible that claims could be made against online services companies and Internet access providers under both United States and foreign law for defamation, negligence, copyright or trademark infringement, or other theories based on the nature of the data or the content of the materials disseminated through their networks. Several private lawsuits seeking to impose such liability upon online services companies and Internet access providers are currently pending. In addition, certain countries, such as China, regulate or prohibit the transport of telephony data in their territories. The imposition upon us and other Internet network providers of potential liability for information carried on or disseminated through their systems could require us to implement measures to reduce our exposure to such liability, which may require the expenditure of substantial resources, or to discontinue certain service or product offerings. Our ability to limit the types of data or content distributed through our network is limited. Failure to comply with such regulation in a particular jurisdiction could result in fines or penalties or the termination of our service in such jurisdiction. The increased attention focused upon liability issues as a result of these lawsuits and legislative proposals could impact the growth of Internet use. Our professional liability insurance may not be adequate to compensate or may not cover us in the event we become liable for

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information carried on or disseminated through our networks. Any costs not covered by insurance incurred as a result of such liability or asserted liability could harm our business and prospects.

We are subject to risks associated with operating in international markets.

There are certain risks inherent in conducting business internationally, such as:

. changes in regulatory requirements;

. export restrictions, tariffs, differing regulatory regimes and other trade barriers;

- challenges in staffing and managing foreign operations;
- differing technology standards;
- longer payment and sales cycles;
- problems in collecting accounts receivable;
- political and economic instability;
- fluctuations in currency exchange rates;
- imposition of currency exchange controls;
- costs of customizing products for foreign countries;
- protectionist laws and business practices favoring local competition;
- dependence on local vendors;
- seasonal reductions in business activity; and
- potentially adverse tax consequences.

Any of these risks could harm our international operations. For example, certain European countries already have laws and regulations related to certain content distributed on the Internet and technologies used on the Internet that are more strict than those currently in force in the United States. Furthermore, there is an on-going debate in Europe as to the regulation of certain technologies we use, including caching and mirroring. The European Parliament has recently adopted a directive relating to the reform of copyright in the European Community which will, if made into law, restrict caching and mirroring. Any or all of these factors could cause our business and prospects to suffer. In addition, we may not be able to obtain the necessary telecommunications infrastructure in a cost-effective manner or compete effectively in international markets.

We currently pay some of our suppliers in foreign currencies which subject us to currency fluctuation risks. To date, all of our customers have paid for our services in U.S. dollars. However, we believe that in the future an increasing portion of our revenues will be denominated in foreign currencies. In particular, we expect that with the introduction of the Euro, an increasing portion of our international sales may be Euro-denominated. Fluctuations in the value of the Euro or other foreign currencies may cause our business and prospects to suffer. We currently do not engage in foreign exchange hedging activities and our international revenues are currently subject to the risks of foreign currency fluctuations.

Year 2000 compliance could harm our business.

Many currently installed computer systems are not able to distinguish 21st century dates from 20th century dates. As a result, in less than one year, computer systems and software used by many companies and organizations in a wide variety of industries (including technology, transportation, utilities, finance, telecommunications, among others) will experience operating difficulties unless they are adequately modified or upgraded to process information related to the century change. Significant uncertainty exists in the software and other industries concerning the scope and magnitude of problems associated with the century change. We

recognize the need to ensure that our operations will not be adversely affected by Year 2000 software failures. We are assessing the potential overall impact of the impending century change on our business and prospects.

Based on our assessment to date, we believe the current versions of our software products and services are Year 2000 compliant, that is, they are capable of adequately distinguishing 21st century dates from 20th century dates. However, our products are generally integrated into enterprise systems involving sophisticated hardware and complex software products, which may not be Year 2000 compliant. We may in the future be subject to claims based on Year 2000 problems in others' products, or issues arising from the integration of multiple products within an overall system. Although we have not been a party to any litigation or arbitration proceeding to date involving our products or services and related to Year 2000 compliance issues, there can be no assurance that we will not in the future be required to defend our products or services in such proceedings, or to negotiate resolutions of claims based on Year 2000 issues. The costs of defending and resolving Year 2000-related disputes, regardless of the merits of such disputes, and any potential liability on our part for Year 2000-related damages, including consequential damages, could cause our business and prospects to suffer. In addition, we believe that purchasing patterns of customers and potential customers may be affected by Year 2000 issues as companies expend significant resources to correct or upgrade their current software systems for Year 2000 compliance. These expenditures may reduce funds available to purchase software products such as those offered by us. To the extent that Year 2000 issues cause significant delay in, or cancellation of, decisions to purchase our products or services, our business and prospects could suffer.

We are reviewing our internal management information and other systems in order to identify and modify any products, services or systems that are not Year 2000 compliant. To date, we have not encountered any material Year 2000 problems with our computer systems or any other equipment which might be subject to these problems. Our plan for the Year 2000 calls for compliance verification of external vendors supplying software and information systems to

us and communication with significant suppliers to determine their ability to remediate their own Year 2000 issues. As part of our assessment, we are evaluating the level of validation we will require of third parties to ensure their Year 2000 readiness. In the event that any of these third parties cannot timely provide us with products, services or systems that meet the Year 2000 requirements, our business and prospects could suffer. Our business and our ability to deliver our products and services could be severely affected, at least for a certain period of time, in the event that Year 2000 related problems were to cause disruption or failure in the Internet as a means of delivery of our products and services or more generally, disruption to the infrastructure. The total cost of these Year 2000 compliance activities has not been, and is not anticipated to be, material to our business, results of operations and financial condition. These costs and the timing in which we plan to complete our Year 2000 modification and testing processes are based on our management's estimates. We may not be able to remediate all significant Year 2000 problems on a timely basis. Our remediation efforts may involve significant time and expense, and could cause our business and prospects to suffer.

We may be subject to government regulation and legal uncertainties which could harm us.

We provide value-added IP-based network services which include transmitting data over public telephone lines. These transmissions are governed by the regulations and policies of the Federal Communications Commission, or "FCC," and the state public utility commissions. However, our services are deemed to be enhanced or information services (as opposed to common carrier services) and are not currently subject to direct regulation by the FCC or any other federal or state communications regulatory agency.

The nature, scope and prices of our services could be affected by changes in law or regulation in the telecommunications arena, especially changes relating to Internet connectivity and telecommunications markets. Such changes could directly or indirectly affect our costs, limit usage or subscriber-related information, and increase the likelihood or scope of competition from Regional Bell Operating Companies or other telecommunications companies. For example, proceedings are pending at the FCC to determine whether and to what extent information service providers, including Internet service providers that provide Internet-related

services like ours, should be considered telecommunications carriers. An affirmative response to that inquiry could subject such companies to various regulations, including, but not limited to:

. an obligation to contribute monies to the Universal Service Fund, or "USF";

- FCC entry and exit regulations;
- reporting, fee and record-keeping requirements;
- marketing restrictions; and
- access charge obligations for use of the public switched telephone network.

Although the FCC has decided for the time being that information service providers, including Internet service providers, are not telecommunications carriers, that decision is not yet final and is being challenged by various parties, including the Regional Bell Operating Companies. Some members of Congress have also disagreed with the FCC's conclusion. Congressional dissatisfaction with the FCC's conclusions could result in further changes to the FCC's governing statute. As our services become available over the Internet in foreign countries, and as we facilitate sales by our customers to end users located in such foreign countries, such jurisdictions may claim that we are required to qualify to do business in the particular foreign country. Our failure to qualify as a foreign corporation in a jurisdiction where we are required to do so could subject us to taxes and penalties and could result in our inability to enforce contracts in such jurisdictions. It is possible that claims could be made against online service companies and Internet service providers under foreign law for defamation, negligence, copyright or trademark infringement, or other theories based on the nature and content of the materials disseminated through their networks.

Implementation of any future changes in law or regulation, including those discussed herein, could cause our business and prospects to suffer. Our business and prospects may also be harmed by the imposition of certain tariffs, duties and other import restrictions on facilities and resources that we obtain from non-domestic suppliers. As a result, changes in law or regulation in the United States or elsewhere could cause our business and prospects to suffer.

Risks Related to Our Offering

Our stock will likely be subject to substantial price and volume fluctuations due to a number of factors, some of which are beyond our control.

Stock prices and trading volumes for many Internet companies fluctuate widely for a number of reasons, including some reasons which may be unrelated to their businesses or results of operations. This market volatility, as well as general domestic or international economic, market and political conditions, could materially adversely affect the price of our common stock without regard to our operating performance. In addition, our operating results may be below the expectations of public market analysts and investors. If this were to occur, the market price of our common stock would likely significantly decrease.

After this offering, our officers, directors, and their affiliates, in the aggregate, will control % of our voting stock.

Some of our stockholders own a large enough stake in us to have an influence on the matters presented to stockholders. As a result, these stockholders may have the ability to control all matters requiring stockholder approval, including the election and removal of directors, the approval of significant corporate transactions, such as any merger, consolidation or sale of all or substantially all of Digital Island's assets, and the control of the management and affairs of Digital Island. Accordingly, such concentration of ownership may have the effect of delaying, deferring or preventing a change in control of Digital Island, impede a merger, consolidation, takeover or other business combination involving Digital Island or discourage a potential

acquirer from making a tender offer or otherwise attempting to obtain control of Digital Island, which in turn could have an adverse effect on the market price of Digital Island's common stock.

The sale of shares eligible for future sale in the open market could depress our stock price.

Sales of substantial amounts of our common stock (including shares issued upon the exercise of outstanding options and warrants) in the public market after this offering could adversely affect the market price of our common stock. Such sales also might make it more difficult for us to sell equity-related securities in the future at a time and price that we deem appropriate. In addition to the shares of common stock offered hereby (assuming no exercise of the underwriters' over-allotment option), as of the date of this prospectus, there will be shares of common stock outstanding, all of which are restricted shares under the Securities Act of 1933, as amended. As of such date, no restricted shares will be eligible for sale in the public market. Following the expiration of the 180-day lock-up agreements with the representatives of the underwriters, restricted shares will be available for sale in the public market and the remaining restricted shares will be eligible for sale from time to time thereafter upon expiration of applicable holding periods under Rule 144, 144(k) or 701 promulgated under the Securities Act. In addition, as of March 31, 1999, there were outstanding options to purchase 4,218,839 shares of common stock and warrants to purchase 95,000 shares of common stock (all of which warrants are expected to be exercised on or before the closing of this offering). Bear, Stearns & Co. Inc. may, in its sole discretion and at any time without notice, release all or any portion of the securities subject to lock-up agreements. In addition, the holders of restricted shares and options to purchase shares of our common stock are entitled to certain rights with respect to registration of such shares for sale in the public market. If such holders sell

in the public market, such sales could have a material adverse effect on the market price of our common stock.

Our management will have broad discretion in allocating proceeds from this offering.

The net proceeds to us from this offering, after deducting underwriting commissions and expenses payable by us, are estimated to be approximately $ million. The primary purposes of this offering are to fund capital expenditures, working capital and operating losses expected to be incurred in connection with the execution of our business plan, including the expansion of our operations. A portion of the net proceeds also may be used to repay currently outstanding or future indebtedness, or to acquire or invest in complementary businesses or products. Accordingly, our management will retain broad discretion as to the allocation of most of the proceeds of this offering. The failure of management to apply these funds effectively could negatively impact on our business and prospects.

There is no current market for our common stock.

Prior to this offering, there has been no public market for Digital Island's common stock, and an active public market may not develop or be sustained after this offering and investors may not be able to sell the common stock should they desire to do so. The initial public offering price will be determined by negotiations between Digital Island and the representatives of the Underwriters and may bear no relationship to the price at which the common stock will trade upon completion of this offering. See "Underwriting" for a discussion of the factors to be considered in determining the initial public offering price.

We have certain anti-takeover defenses that could delay or prevent an acquisition of Digital Island.

Certain provisions of our certificate of incorporation and bylaws and the provisions of Delaware law could have the effect of delaying, deferring or preventing an acquisition of Digital Island. For example, our board of directors is divided into three classes to serve staggered three-year terms, we may authorize the issuance of up to 10,000,000 shares of "blank check" preferred stock, our stockholders may not take actions by written consent and our stockholders are limited in their ability to make proposals at stockholder meetings. See "Description of Capital Stock" for a further discussion of these provisions.

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USE OF PROCEEDS

The net proceeds from this offering, at an assumed initial public offering price of $ per share, are estimated to be $ million, after

deducting estimated underwriting discounts and commissions and expenses payable by us. We expect to use the net proceeds from this offering, together with existing cash, to fund operating losses, working capital needs and capital expenditures expected to be incurred in connection with our operations. Our management will retain broad discretion in the allocation of such net proceeds. Although we may use a portion of the net proceeds to pursue possible acquisitions of, or enter into joint ventures with respect to, complementary businesses, technologies or products in the future, there are no present understandings, commitments or agreements with respect to any such acquisitions or joint ventures. Pending the use of such net proceeds, we intend to invest these funds in short-term, investment grade securities.

DIVIDEND POLICY

We have not declared or paid any dividends since our inception and do not intend to pay cash dividends on our capital stock in the foreseeable future. We anticipate that we will retain all future earnings, if any, for use in our operations and the expansion of our business. Certain of our credit agreements restrict our ability to declare or pay any dividends while the credit agreement is in effect. See "Management's Discussion and Analysis of Financial Condition and Results of Operations--Liquidity and Capital Resources."

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CAPITALIZATION

The following table sets forth, as of March 31, 1999:

- Our actual capitalization;
- Our pro forma capitalization, assuming the conversion of outstanding shares of our convertible preferred stock into common stock and the exercise of warrants to purchase 95,000 shares of our common stock; and
- Our pro forma capitalization, as adjusted to give effect to the sale of shares of common stock offered by us in this offering at an assumed initial public offering price of $ per share, after deducting the underwriting discounts and commissions and estimated offering expenses payable by us, and the application of the estimated net proceeds from this offering.

This information should be read in conjunction with our Consolidated Financial Statements and the Notes related thereto appearing elsewhere in this prospectus. See "Use of Proceeds."

<TABLE>
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	March 31, 1999		
	(unaudited)		
	Actual	Pro Forma	As Adjusted
	(in thousands, except share data)		
<S>	<C>	<C>	<C>
Long-term obligations, less current portion....	$ 2,219	$ 2,219	
Stockholders' equity:			
Convertible preferred stock, no par value, Series A, Series B, Series C, Series D and Series E, 30,000,000 shares authorized, $86,894,973 aggregate liquidation preference, 25,070,363 shares issued and outstanding on an actual and pro forma basis and no shares issued and outstanding as adjusted.....	$ 84,226	--	
Preferred stock, $0.001 par value, 10,000,000 shares authorized; no shares issued and outstanding on an actual basis and as adjusted.....	--	--	
Common stock, no par value, 40,000,000 shares authorized, 2,622,225 shares issued and outstanding on an actual basis and 27,965,736 issued and outstanding on a pro forma basis; $0.001 par value, 100,000,000 shares authorized, shares issued and outstanding on an as adjusted basis	484	84,720	
Stockholder note receivable.....	(110)	(110)	
Common stock warrants.....	29	--	
Additional paid-in capital.....	5,486	5,515	
Deferred compensation.....	(4,969)	(4,969)	
Accumulated deficit.....	(35,997)	(35,997)	
Total stockholders' equity.....	49,149	49,159	
Total capitalization.....	$ 51,368	$ 51,378	$

</TABLE>

The table above excludes 4,218,839 shares of common stock issuable upon exercise of options outstanding with a weighted average exercise price of $2.13 per share and 7,544,000 shares reserved for future issuances under our 1999 Stock Incentive Plan. See "Executive Compensation and Other Information--Employee Benefit Plans."

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DILUTION

Our net tangible book value as of March 31, 1999 was approximately $49.1 million, or $1.76 per share of common stock. Net tangible book value per share is calculated by subtracting our total liabilities from our total tangible assets, which equals total assets less intangible assets, and dividing this amount by the number of shares of common stock outstanding as of March 31, 1999. Assuming the sale by us of shares of common stock offered in this offering at an assumed initial public offering price of $ per share and the application of the estimated net proceeds from this offering, our net tangible book value as of March 31, 1999 would be $ million, or $ per share of common stock. Assuming completion of this offering, there will be an immediate increase in the net tangible book value of $ per share to our existing stockholders and an immediate dilution in the net tangible book value of $ per share to new investors. The following table illustrates this per share dilution:

<TABLE>

<S>	<C>	<C>
Assumed initial public offering price per share.....		$
Pro forma net tangible book value per share as of March 31, 1999.....	$1.76	
Pro forma increase attributable to new investors.....		$
Pro forma net tangible book value per share after the offering.....		$
Pro forma dilution per share to new investors.....		$

</TABLE>

The following table summarizes the total number of shares of common stock purchased from us, the total consideration paid to us and the average price per share paid by existing stockholders and by new investors, in each case based upon the number of shares of common stock outstanding as of March 31, 1999.

<TABLE>
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	Shares Purchased		Total Consideration		Average Price
	Number	Percent	Amount	Percent	Per Share
<S>	<C>	<C>	<C>	<C>	<C>
Existing stockholders..	27,692,588	%	$84,710,367	%	$3.06
New investors.....		%	$	%	$
Total.....		%	$	%	

</TABLE>

If the underwriters' over-allotment is exercised in full, the number of shares of common stock held by existing stockholders will be reduced to , or % of the total number of shares of common stock to be outstanding after this offering, and will increase the number of shares of common stock held by the new investors to , or % of the total number of shares of common stock to be outstanding immediately after this offering. See "Principal Stockholders."

The tables and calculations above assume no exercise of outstanding options. At March 31, 1999, there were 4,218,839 shares of common stock issuable upon exercise of options outstanding with a weighted average exercise price of $2.13 per share and 7,544,000 shares reserved for future issuance under our 1999 Stock Incentive Plan. To the extent that these options are exercised, there will be further dilution to new investors. See "Executive Compensation and Other Information--Employee Benefit Plans."

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SELECTED CONSOLIDATED FINANCIAL DATA

The following selected consolidated financial data should be read in conjunction with our Consolidated Financial Statements and Notes thereto and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere in this prospectus. The statement of operations data for each of the years in the three-year period ended September 30, 1998 and the balance sheet data at September 30, 1997 and 1998, are derived from our financial statements that have been audited by PricewaterhouseCoopers LLP, independent accountants, included elsewhere in this prospectus. The statement of operations data for the year ended September 30, 1995 and the balance sheet data at September 30, 1995 and 1996, are derived from our audited financial statements that are not included in this prospectus. The statement of operations data for the six months ended March 31, 1998 and 1999, and the balance sheet data at March 31, 1999, are derived from our unaudited financial statements included elsewhere in this prospectus. The statement of operations data for the period from inception to September 30, 1994 and the balance sheet data at September 30, 1994 are derived from our unaudited financial statements that are not included in this prospectus. We did not begin offering our global IP applications network services until January 1997; prior to such time, we were engaged in activities unrelated to our current operations. Accordingly, our results of operations prior to 1997 are not comparable to our results of operations for 1997 or any subsequent periods.

<TABLE>
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	Period from inception to	Years Ended September 30,			Six Months Ended March 31,	

	September 30,						
	1994	1995	1996	1997	1998	1998	1999
				(in thousands, except per share			
	(unaudited)			data)		(unaudited)	
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Statement of Operations Data:							
Revenue	$ --	$ --	$ --	$ 218	$ 2,343	$ 691	$ 3,795
Costs and expenses:							
Cost of revenue	--	--	--	2,508	9,039	4,026	7,750
Sales and marketing	--	--	--	1,205	4,847	1,787	5,171
Product development	--	--	--	378	1,694	571	2,010
General and administrative	33	7	26	1,502	3,392	1,164	2,963
Stock compensation expense	--	--	--	--	--	--	516
Total cost and expenses	33	7	26	5,594	18,971	7,547	18,410
Loss from operations	(33)	(7)	(26)	(5,376)	(16,629)	(6,856)	(14,615)
Interest income (expense), net	--	(2)	(1)	87	353	64	257
Loss before income taxes	(33)	(9)	(26)	(5,288)	(16,275)	(6,792)	(14,358)
Provision for income taxes	--	1	1	1	2	1	2
Net loss	$ (33)	$ (10)	$ (27)	$ (5,289)	$ (16,277)	$ (6,793)	$ (14,360)
Basic and diluted loss per share(1)	$ (0.12)	$ (0.04)	$ (0.10)	$ (3.53)	$ (7.28)	$ (3.07)	$ (6.07)
Shares used in basic and diluted loss per share(1)	275,000	275,000	275,000	1,497,711	2,236,452	2,215,875	2,366,951
Other Data:							
Depreciation and amortization	--	--	--	$ 158	$ 811	$ 293	$ 924
Capital expenditures(2)	--	--	$ 2	$ 2,128	$ 3,640	$ 412	$ 3,024

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	September 30,	
		March 31,

	1994	1995	1996	1997	1998	1999
	(unaudited)	(in thousands)				(unaudited)
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Balance Sheet Data:						
Cash and cash equivalents....	$ 20	$ 7	$344	$4,584	$ 5,711	$29,751
Investments.....	--	--	--	1,983	10,123	20,915
Working capital.....	15	5	76	4,613	12,883	44,010
Total assets.....	107	93	432	9,223	22,617	62,359
Long-term obligations, including current portion...	--	--	--	705	3,992	4,039
Total stockholders' equity...	$ 97	$86	$ 84	$6,265	$15,490	$49,149

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(1) See Notes 2 and 9 of Notes to Consolidated Financial Statements for the determination of shares used in computing basic and diluted loss per share.

(2) Capital expenditures represent purchases of property and equipment, including non-cash transactions such as the acquisition of equipment under capital leases.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of the financial condition and results of operations of Digital Island should be read in conjunction with the Consolidated Financial Statements and Notes thereto included elsewhere in this prospectus. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ from those anticipated in these forward-looking statements as a result of various factors including but not limited to, those discussed in "Risk Factors," "Business" and elsewhere in this prospectus.

Overview

Digital Island offers a leading global e-business network for companies that are using the Internet for worldwide deployment of business-critical applications. We serve multinational corporations that are increasingly relying on the Internet to conduct business but are constrained by the unreliability, slow performance and lack of functionality of the public Internet. The Digital Island Global IP Applications Network and value-added services enable customers to effectively deploy and manage global IP applications by combining the reliability, performance and functionality of private wide area networks with the global access of the public Internet. We also offer service level guarantees, customized billing, security services, network management and other application services designed to improve the performance of applications deployed on our network.

We did not begin offering our Global IP Applications Network services until January 1997; prior to such time we were engaged in activities unrelated to our current operations. Since inception, we have incurred net losses and experienced negative cash flow from operations. We expect to continue to operate at a net loss and to experience negative cash flows at least through the year 2000. Our ability to achieve profitability and positive cash flow from operations will be dependent upon our ability to grow our revenues substantially and achieve other operating efficiencies.

We derive our revenues from a family of services, which include Application Hosting and Content Distribution Services, consisting of server management, hardware management and co-location services, and Network Services, consisting of the sale of open, reserved and managed bandwidth. We currently sell our services under contracts having terms of one or more years.

Cost of revenues consists primarily of the cost of contracting for lines from telecommunication providers worldwide and, to a lesser extent, the cost of our network operations. We lease lines under contracts of one year or more. The leasing of transoceanic lines comprises the largest component of our telecommunications expense, with additional costs arising from leasing local circuits between our data centers and points of presence in the United States and international markets. In the future, we expect to increase the size and number of circuits leased based on increases in network volume and geographic expansion. The cost of our network operations is comprised primarily of data centers, equipment maintenance, personnel and related costs associated with the management and maintenance of the network.

Certain options granted and common stock issued during the six months ended March 31, 1999 have been considered to be compensation. Total stock compensation expense associated with such equity transactions as of March 31, 1999 amounted to $5.5 million. These amounts are being amortized over the vesting periods of such securities. Of the total stock compensation expense, $516,000 was amortized in the six months ended March 31, 1999. We expect amortization of $2.3 million and $1.8 million in the years ending September 30, 1999 and 2000, respectively, relating to these grants.

Six Months Ended March 31, 1999 and 1998

Revenue. Revenue increased to $3.8 million for the six months ended March 31, 1999 from $691,000 for the six months ended March 31, 1998. The increase in revenue was due primarily to an increase in the number of customers and increased usage by existing customers.

Cost of Revenue. Cost of revenue increased to $7.7 million for the six months ended March 31, 1999 from $4.0 million for the six months ended March

31, 1998. The increase in cost of revenue was due to spending for additional network capacity as well as the addition of network operations personnel. We anticipate that our cost of revenue will grow significantly in future periods in order to accommodate planned increases in the number of customers and increased usage by existing customers.

Sales and Marketing. Sales and marketing expenses consist primarily of staffing and marketing personnel and marketing programs, salespeople, sales engineering, customer service personnel and administrative personnel. Sales and marketing expenses increased to $5.2 million for the six months ended March 31, 1999 from $1.8 million for the six months ended March 31, 1998. This increase was due primarily to the addition of direct sales personnel and related costs and program expenses. We expect sales and marketing expenses to increase in future periods.

Product Development. Product development expenses consist primarily of costs associated with personnel and related costs and those costs associated with new product introductions. Product development expenses increased to $2.0 million for the six months ended March 31, 1999 from $571,000 for the six month period ended March 31, 1998. This increase was due primarily to growth in personnel and related costs and to new product initiatives including TraceWare, mirroring and caching. We expect product development expenses to increase in future periods.

General and Administrative. General and administrative expenses consist of personnel related expenses and other costs associated with office facilities, professional services and other administrative related expenses. General and administrative expenses increased to $3.0 million for the six months ended March 31, 1999 from $1.2 million for the six months ended March 31, 1998. This increase was due to growth in personnel and related expenses, office facility expenses, legal and accounting fees and other administrative related expenses. We expect general and administrative expenses to increase in future periods to support expected growth in future revenues and costs related to being a public company.

Interest Income, net. Interest income, net, includes interest income from our cash and cash equivalents, and investments. Interest expense relates to our financing obligations, including bank borrowings and borrowings associated with equipment leasing. Interest income, net, increased to $257,000 for the six months ended March 31, 1999 from $64,000 for the six months ended March 31, 1998. This increase was due primarily to a higher average cash balance as a result of the proceeds of the issuance of shares of our preferred stock.

Provision for Income Taxes. Digital Island has had net operating losses for every period through March 31, 1999. We may not be able to utilize all or any of these tax loss carry-forwards as a result of this offering and prior financings. We have not recognized a provision for income taxes due to the uncertainty surrounding the realization of the favorable tax attributes in future tax returns and we have placed a valuation allowance against our net

deferred tax assets.

Years Ended September 30, 1998 and 1997

We did not begin offering our Global IP Applications Network services until January 1997; prior to such time we were engaged in activities unrelated to our current operations. Additionally, during the periods prior to January 1997, we had no revenues and our operating expenses, although not material, consisted of general and administrative expenses associated with an unrelated technology business venture. Accordingly, our results of operations prior to 1997 are not comparable to our results of operations for 1997 or any subsequent periods, and comparisons to periods prior to 1997 have not been made.

Revenue. Revenue increased to $2.3 million for the year ended September 30, 1998 from $218,000 for the year ended September 30, 1997. The increase in revenue was due primarily to an increase in the number and usage of new customers and increased usage by existing customers.

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Cost of Revenue. Cost of revenue increased to $9.0 million for the year ended September 30, 1998 from $2.5 million for the year ended September 30, 1997. The increase in cost of revenue was due to an increase in network capacity as well as an increase in new lines deployed.

Sales and Marketing. Sales and marketing expenses increased to $4.8 million for the year ended September 30, 1998 from $1.2 million for the year ended September 30, 1997. This increase was due primarily to growth in personnel and related costs and program expenses.

Product Development. Product development expenses increased to $1.7 million for the year ended September 30, 1998 from $378,000 for the year ended September 30, 1997. This increase was due primarily to the growth of personnel and related costs and to new product initiatives.

General and Administrative. General and administrative expenses increased to $3.4 million for the year ended September 30, 1998 from $1.5 million for the year ended September 30, 1997. This increase was due to growth in personnel and related expenses, office facility expenses, legal and accounting fees and other administrative related expenses.

Interest Income, net. Interest income, net, increased to $353,000 for the year ended September 30, 1998 from $87,000 for the year ended September 30, 1997. This increase was primarily due to a higher average cash balance as a result of the proceeds of the issuance of shares of our preferred stock.

Quarterly Results of Operations

The following tables set forth certain unaudited statements of operations for the six quarters ended March 31, 1999. This data has been derived from the unaudited interim financial statements prepared on the same basis as the audited Consolidated Financial Statements contained in this prospectus, and in the opinion of management include, all adjustments consisting only of normal recurring adjustments that we consider necessary for a fair presentation of such information when read in conjunction with the Consolidated Financial Statements and Notes thereto appearing elsewhere in this prospectus. The operating results for any quarter should not be considered indicative of results of any future period.

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	Three Months Ended					
	(unaudited)					
	Dec. 31, 1997	Mar. 31 1998	June 30, 1998	Sept. 30 1998	Dec. 31, 1998	Mar. 31 1999
	(in thousands)					
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Statement of Operations Data:						
Revenue	$ 277	$ 414	$ 725	$ 927	$ 1,385	$ 2,411
Costs and expenses:						
Cost of revenue	1,961	2,065	2,267	2,746	2,923	4,827
Sales and marketing	860	927	1,296	1,764	2,046	3,125
Product development	214	357	538	585	843	1,167
General and administrative	531	632	902	1,326	1,260	1,703
Stock compensation expense	--	--	--	--	61	455
Total cost and expenses	3,566	3,981	5,003	6,421	7,133	11,277
Loss from operations	(3,289)	(3,567)	(4,278)	(5,494)	(5,748)	(8,866)
Interest income (expense), net	45	19	123	166	96	160
Loss before income taxes	(3,244)	(3,548)	(4,155)	(5,328)	(5,652)	(8,706)
Provision for income taxes	--	1	--	1	2	--
Net loss	$(3,244)	$(3,549)	$(4,155)	$(5,329)	$(5,654)	$(8,706)

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We expect to experience significant fluctuations in our future results of operations due to a variety of factors, many of which are outside of our control, including:

- demand for and market acceptance of our products and services;
- introductions of products and services or enhancements by us and our competitors;
- competitive factors that affect our pricing;
- capacity utilization of our global IP applications network;
- reliable continuity of service and network availability;
- the availability and cost of bandwidth and our ability to increase bandwidth as necessary;
- the timing of customer installations;
- the mix of products and services we sell;
- the timing and magnitude of capital expenditures, including costs relating to the expansion of operations;
- the timing of expansion of our network infrastructure;
- fluctuations in bandwidth used by customers;
- the retention of key personnel;
- conditions specific to the Internet industry and other general economic factors; and
- new government legislation or regulation.

In addition, a relatively large portion of our expenses are fixed in the short-term, particularly with respect to telecommunications capacity, depreciation, real estate and interest expenses and personnel, and therefore our results of operations are particularly sensitive to fluctuations in revenues. Due to the foregoing factors, we believe that period-to-period comparisons of our operating results are not necessarily meaningful and that such comparisons cannot be relied upon as indicators of future performance.

Liquidity and Capital Resources

From inception through March 31, 1999, we financed our operations primarily

through private equity placements of $86.9 million dollars and borrowings under notes payable and capital leases from financial institutions of $5.7 million. At March 31, 1999, we had an accumulated deficit of $36.0 million and cash and cash equivalents and short-term investments of $50.7 million.

Net cash used in our operating activities for the six months ended March 31, 1999 was $10.4 million. The net cash used by operations was primarily due to working capital requirements and net losses, offset by increases in accounts payable and accrued expenses. Net cash used in investing activities was $12.9 million for the period ended March 31, 1999 and is comprised of equipment purchases of $2.3 million and investments of $10.6 million. Net cash provided by financing activities was $47.3 million and is related primarily to the issuance of our Series E Preferred Stock, as well as net borrowing under our bank and leasing lines of credit.

We have a $750,000 revolving line of credit with a commercial bank for the purpose of financing equipment purchases. As of March 31, 1999, $451,000 was outstanding thereunder. The loan contains certain standard covenants. Interest on borrowings thereunder accrues at the lender's prime rate plus 0.75% (which was 8.5% at March 31, 1999), and is payable monthly. No further advances were permitted following October 18, 1997, and any outstanding amounts are payable on or before October 18, 2000.

We also have a $7.5 million line of credit with a commercial bank, consisting of a revolving credit facility of up to $5 million and other facilities of up to $2.5 million. As of March 31, 1999, approximately $230,000

was outstanding under the revolving credit facility, and approximately $718,000 was outstanding under equipment loan facilities. No further amounts may be borrowed under the equipment loan facilities. Advances under the line of credit are limited to a percentage of our recurring contract revenue. The loan contains certain standard covenants. Interest on borrowings thereunder accrues at the lender's prime rate plus 0.25% (which was 8.00% at March 31, 1999), and is payable monthly. Under the terms of the equipment loan facilities, interest is charged at the lender's prime rate plus 0.75%, which was 8.5% at March 31, 1999. The loans mature at various times in 2001. Subsequent to September 30, 1998, we did not comply with certain financial covenants. We obtained waivers for all covenant violations from October 1, 1998 to January 31, 1999. Additionally, we have two lease lines of credit totaling $4.4 million for equipment purchased. Total borrowings under these two lease lines of credit were $2.6 million at March 31, 1999.

We believe that the estimated net proceeds from this offering, together with our existing cash and funds available under our existing credit facilities, will be sufficient to fund our capital expenditures, cash needs and operating losses for at least the next 12 months. The execution of our business plan will

require substantial additional capital to fund our operating losses, sales and marketing expenses, capital expenditures, lease payments and working capital requirements thereafter. We intend to continue to consider our future financing alternatives, which may include the incurrence of indebtedness, additional public or private equity offerings or an equity investment by a strategic partner. Actual capital requirements may vary based upon the timing and success of the expansion of our operations. Our capital requirements may change based upon technological and competitive developments. In addition, several factors may affect our capital requirements:

. demand for our services or our anticipated cash flow from operations being less than expected;

. our development plans or projections proving to be inaccurate;

. our engaging in acquisitions or other strategic transactions; or

. our accelerating deployment of our network services or otherwise altering the schedule of our expansion plan.

Other than the current bank note payable and lease financing, we have no present commitments or arrangements assuring us of any future equity or debt financing, and there can be no assurance that any such equity or debt financing will be available to us on favorable terms, or at all. If we do not obtain additional financing, we believe that our existing cash resources will be adequate to continue expanding operations on a reduced scale.

Recent Accounting Pronouncements

On March 4, 1998, the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants (AICPA) issued Statement of Position No. 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use" (SOP 98-1). SOP 98-1 requires computer software costs related to internal software that are incurred in the preliminary project stage should be expensed as incurred. Once the capitalization criteria of SOP 98-1 have been met, external direct costs of materials and services consumed in developing or obtaining internal-use computer software; payroll and payroll-related costs for employees who are directly associated with and who devote time to the internal-use computer software project (to the extent of the time spent directly on the project); and interest costs incurred when developing computer software for internal use should be capitalized. SOP 98-1 is effective for financial statements for fiscal years beginning after December 15, 1998. Accordingly, we will adopt SOP 98-1 in our consolidated financial statements for the year ending September 30, 2000.

On April 3, 1998, the Accounting Standards Executive Committee of the AICPA issued Statement of Position No. 98-5 (SOP 98-5), "Reporting on the Costs of Start-Up Activities", which provides guidance on the financial reporting of start-up costs and organization costs. SOP 98-5 requires costs of start-up

activities and organization costs to be expensed as incurred. SOP 98-5 is effective for financial statements for fiscal years

beginning after December 15, 1998. As we have not capitalized such costs, the adoption of SOP 98-5 is not expected to have a material impact on our consolidated financial statements.

In June 1998, the FASB issued Statement of Financial Accounting Standards No. 133 (SFAS 133), "Accounting for Derivative Instruments and Hedging Activities." SFAS 133 establishes accounting and reporting standards for derivative instruments and for hedging activities. SFAS 133 is effective for fiscal years beginning after June 15, 1999. We do not believe the adoption of SFAS 133 will have a material effect on our consolidated results of operations or financial condition.

Year 2000 Compliance

Many currently installed computer systems are not able to distinguish 21st century dates from 20th century dates. As a result, in less than one year, computer systems and software used by many companies and organizations in a wide variety of industries (including technology, transportation, utilities, finance, telecommunications, among others) will experience operating difficulties unless they are adequately modified or upgraded to process information related to the century change.

We recognize the need to ensure that our operations will not be adversely affected by Year 2000 software failures. We are reviewing our internal management information and other systems in order to identify and modify any products, services or systems that are not Year 2000 compliant. To date, we have not encountered any material Year 2000 problems with our computer systems or any other equipment which might be subject to these problems.

We have made inquiries of our vendors of software and information systems regarding their own Year 2000 readiness. Although we have received various assurances, we have not received affirmative documentation of Year 2000 compliance from any of these vendors and we have not performed any operational tests on our internal systems. As part of our assessment, we are evaluating the level of validation we will require of third parties to ensure their Year 2000 readiness. In the event that any of these third parties cannot timely provide us with products, services or systems that meet the Year 2000 requirements, our business, results of operations and financial condition could be materially adversely affected.

We anticipate that our review of Year 2000 issues and any remediation efforts will continue throughout calendar 1999. The total cost of our Year 2000 compliance activities has not been, and is not anticipated to be, material to

our business, results of operations and financial condition. We have derived these estimates using a number of assumptions, including the assumption that we have already identified our most significant Year 2000 issues. However, these assumptions may not be accurate, and actual results could differ materially from those anticipated. In view of our Year 2000 review and remediation efforts to date, we do not consider contingency planning to be necessary at this time. However, the cost of developing and implementing such a plan, if necessary, could be material. See "Risk Factors--Year 2000 compliance could harm our business."

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BUSINESS

Overview

Digital Island offers a leading global e-business network for companies that are using the Internet for worldwide deployment of business-critical applications. We target multinational corporations that are increasingly relying on the Internet to conduct business but are constrained by its unreliability, slow performance, and lack of functionality. Our global Internet protocol, or "IP," applications network and value-added services enable customers to effectively deploy and manage global IP applications by combining the reliability, performance and functionality of private wide area networks with the global access of the public Internet. We also offer service level guarantees, customized billing, security services, network management and other application services designed to improve the performance of applications deployed on our network. Our customers, which include Autodesk, Cisco Systems, E*TRADE Group and National Semiconductor, use our services and proprietary technology to facilitate the deployment of a wide variety of applications, including electronic commerce, online customer service, software and multimedia document distribution, sales force automation and distance learning. As of March 31, 1999, we had contracts with 62 customers, of which 48 were deployed and generating revenues.

We use the Digital Island Global IP Applications Network to avoid congestion points common on the public Internet and to intelligently allocate bandwidth and storage. The e-business applications delivered over our network are accessed globally in the same way as any Web site, with a noticeable difference: these e-business applications are highly available and are designed to operate substantially faster and with greater functionality than sites that rely solely on the public Internet.

The Digital Island Global IP Applications Network consists of a proprietary asynchronous transfer mode, or "ATM," backbone connecting four strategically located data centers in Honolulu, London, New York City and Santa Clara, California. This core network architecture connects over dedicated lines directly to local Internet service providers, in 17 countries. This enables our

customers to transmit Internet traffic seamlessly over our proprietary backbone with dedicated transoceanic capacity and to connect directly to international users through local points of presence. We also offer content distribution services including mirroring (replicating) and caching (storing) which enable us to forward deploy our customers' applications in locations close to their end-users. This allows our customers to benefit from the low cost of data storage versus transport, and to provide a better online experience for their end-users. For example, Digital Island Local Content Managers enable us to help customers readily store files which are repeatedly accessed in specific geographic regions.

Digital Island offers a variety of services that allow customers to benefit from the Digital Island Global e-business network. Customers can take advantage of our extensive server management and hosting services offered at our four data centers, and can purchase a range of transport options, including open, reserved, or managed bandwidth. Our outsourced solutions are designed to allow customers to transfer to us the burden of attracting and retaining scarce technical staff and adopting continuously changing technologies, while lowering their operating costs and speeding deployment.

Industry Background

The Internet continues to experience rapid growth and expansion as an important global medium for communications and e-business. E-business is the use of the Internet and emerging technologies to replace or maximize traditional business channels and practices. International Data Corporation, or IDC, has estimated that the total number of Internet users in the world reached approximately 69 million in 1997 and will increase to approximately 319 million in 2002, a 36% compound annual growth rate. As the numbers of Internet users has grown, enterprises have increasingly viewed the Internet as an opportunity to interact rapidly with a larger number of geographically distributed offices, employees, customers, suppliers and partners. Many enterprises that focus solely on delivering services over the Internet have emerged as well as offline businesses that have implemented Internet sites incorporating e-commerce applications. As the Internet has emerged as a

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strategic component of business, investment in Internet services has begun to increase dramatically. According to IDC, the demand for U.S. Internet and e-commerce services was $2.9 billion in 1997 and is expected to grow to $22.1 billion by 2002, a 50% compound annual growth rate. In addition, demand for data transport services is growing rapidly as evidenced by IDC's estimate that Internet service providers' corporate access revenues are expected to grow from $2.9 billion in 1998 to $12.0 billion by 2003, a 33% compound annual growth rate.

Increasing Reliance on E-Business Applications. As use of the Internet

grows, enterprises are increasing the breadth and depth of their Internet product and service offerings. Businesses have begun to use the Internet for an expanding variety of commercial applications, including customer service, electronic sales, software and multimedia document distribution, sales force automation and distance learning. For many enterprises, loss of the availability of such business-critical applications often results in loss of revenue and impairment of customer good will. As a result, enterprises are increasingly demanding that their IP networks deliver consistent, fast global performance, remain easy to upgrade as the scale and complexity of applications grows and technologies change, operate continuously 24 hours per day, seven days per week, and offer the applications support and functionality (e.g. security, user location, identification and usage patterns) previously provided only in wide area networks.

Inherent Problems with the Internet/Need for a Robust Global Solution. The public Internet infrastructure was designed for applications requiring limited bandwidth and for uses which were not business-critical. For enterprises requiring global solutions, the U.S.-centric nature of the public Internet results in poor response times, particularly for applications requiring large file transfers, real time interaction and overseas transport. This is because data transmittal between countries must make a large number of connections or "hops" through various regional and national Internet service providers before reaching its destination. Data packets often become lost in the transfer process, especially for data-intensive transfers involving large software downloads, multimedia document distribution and audio or video streaming.

Trend Toward Outsourcing of Internet Operations. In seeking to address the performance issues of the public Internet, enterprises have increasingly found that investing in the resources and personnel required to maintain in-house private wide area IP networks is cost-prohibitive and extremely difficult given the shortage of technical talent and risk of technological obsolescence. With the failure of in-house solutions to address their needs, today's enterprises have increasingly sought third party providers to support their IP applications deployment, operations and ongoing maintenance. Regional and national Internet service providers, however, often fail to provide an adequate solution because they lack the geographically distributed network capability necessary to deliver content globally using replication and caching technologies, which are becoming increasingly important as the Internet usage and bandwidth demand increase. IDC estimates that corporate spending on web hosting services will increase from approximately $414 million in 1997 to $11.8 billion by 2002, a 95% compound annual growth rate. Enterprises are increasingly seeking companies that combine hosting services and geographically dispersed data centers that deploy the enterprise's applications closer to the end-user to provide value-added solutions.

The Digital Island Solution

Digital Island offers a leading global e-business network for companies that need worldwide deployment of business-critical applications over the Internet.

Our solution provides the following key advantages:

Global Connectivity and Availability. The Digital Island Global IP Applications Network currently has points of presence in 17 countries in Asia, Europe, North America, South America and Australia. We believe that this global reach provides our customers with local access to the majority of existing Internet users.

High Performance and Scalability. The Digital Island Global IP Applications Network bypasses the primary congestion points of the public Internet to provide fast, consistent performance for our customers. By routing and managing Internet traffic over an ATM backbone directly between our strategic, globally

distributed data centers and local points of presence, our solution avoids transmission of data over multiple routers, switches and network access points in the public Internet, thereby substantially reducing transmission time and improving network security and performance. Our network architecture is reliable, scalable and enables a consistent end user experience independent of time of day and geography.

Local Content Management. We own and operate a growing number of Digital Island Local Content Managers in high volume markets around the world. Using technology developed in conjunction with other leading industry suppliers, we have created "digital warehouses" where we help customers readily store files which are repeatedly accessed within the regional area. This solution is a more cost effective and scalable solution when supporting high volume global access to information. It also allows for a more geographically localized experience (e.g. language and currency). We currently operate Digital Island Local Content Manager sites in Germany, Japan, Australia, the U.S., and the United Kingdom and plan to continue our current expansion.

Cost-Effective Outsourcing Solution. Our customers directly benefit from the significant investments of technical expertise and other resources that we have made to develop our unique Digital Island Global IP Applications Network. Most enterprises today do not have the infrastructure that mission-critical Internet operations require, including strategic, globally distributed data centers, 24 hours per day, seven days per week operations and specialized Internet technology expertise. Our solution allows customers to address shortages of technical resources and continuously changing technologies, while substantially lowering the application deployment and operational costs of new IP applications. We believe that our solutions and economies of scale are significantly more cost-effective than most in-house alternatives.

Innovative Solutions. We believe that, as a result of our advanced network architecture and highly experienced product development team, we are able to provide a unique set of value-added product offerings. For example, we offer

open, reserved and managed bandwidth products that enable our customers to allocate their bandwidth purchases according to their changing needs. In addition, our proprietary technology enables us to bill our customers according to the number of bits of data transmitted over our network, geographic destination of transmission and time of day, as opposed to traditional flat-rate billing. This allows us to provide more flexible service pricing, and benefits the customer by more accurately correlating network cost to actual network utilization by geography. We are developing and deploying our proprietary TraceWare technology that enables customers to identify the source of IP requests. Being able to correlate the source and destination (where the data enters and exits our network) provides our customers with significant service and product opportunities, such as tiered and regional pricing, localization of content and currency, assistance in fraud detection, authentication and compliance with export regulations and the enhancement of other applications deployed across our network.

Business Strategy

Our objective is to be the leading global e-business network. In order to achieve this objective, we are implementing a business strategy focused on the following key elements:

Target Multinational Corporations. We have designed our network to address the sophisticated needs of multinational customers, who are increasingly relying on the Internet to conduct business and require consistent levels of high performance and reliability. We primarily target leading customers in industries which are early adopters of Internet technologies, such as the financial services, technology, media publishing, entertainment and other Internet-centric sectors. We have tailored our services to enhance the performance of our customers in electronic commerce, electronic services and electronic fulfillment, such as digital media distribution. The Digital Island Global IP Applications Network has points of presence in 17 countries worldwide, providing our customers with access to a significant majority of existing Internet users, and we plan to expand our global reach through additional points of presence in the future.

Expand Customer Relationships. We plan to extend our leadership in the market for global IP application services by continuing to expand our base of customers. By integrating other value-added services into the Digital Island Global IP Applications Network, and by providing high-quality customer support, we believe that businesses will increasingly rely on us for their e-business needs, which in turn should enhance customer retention and increase demand for both application services and network usage. For example, Autodesk initially used our network to deploy applications in a single country; subsequently, Autodesk chose to deploy applications in other countries served by Digital Island and added additional applications and extended usage of our services to

key subsidiaries.

Develop Additional Value-Added Services. We seek to be a leader in designing and deploying a global e-business network that enables customers to capture the benefits of ubiquitous access to applications and the performance and functionality of private wide area networks. We are committed to investing resources to implement new IP technology and services that will allow our customers to optimize their deployment and operation of applications globally. To this end, we collaborate with providers of leading Internet technologies to develop and deploy proprietary technologies in order to enhance our service offerings and to address our customers' evolving needs. Some of our recent innovations have included reserved and managed bandwidth technologies that allow customers to tailor bandwidth to their individual needs and benefit from usage-based billing, and our TraceWare technology, which is not yet commercially released, that enables customers to identify the source of Internet traffic. Our Digital Island Local Content Managers enable customers to readily store files which are repeatedly accessed within specific geographical regions. We believe that continuing leading edge innovation is the key to differentiating Digital Island's products and services in the long term.

Expand Strategic Relationships. We believe that strategic relationships should enhance our ability to reach new customers. Potential partners include system integrators, software vendors and application service providers. Further, strategic relationships with our customers in our target vertical markets, such as with E*TRADE, bring not only a high level of understanding of the specific needs of that market but also credibility and visibility with potential new customers. We are also targeting partners which can enhance our ability to develop and deliver new application services. Through these relationships we hope to leverage these enterprises' research and development expertise to cost effectively develop new value-added services.

Expand Global Sales Capabilities. We target our customers predominately through a direct sales channel complimented by a range of external alliances and channels. We currently have 45 professionals in our sales organization in offices in the U.S., Asia and Europe and intend to grow our sales organization substantially over the next year. Our Global Partner Program is targeted at increasing the effectiveness of our direct channel. In addition to co-marketing, we have a growing number of sales channel partners which represent our products and services either as a sales agent or a reseller.

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[GRAPHIC APPEARS HERE]

Network Architecture

The Digital Island Intelligent Network consists of an ATM backbone that connects four geographically dispersed data centers. This ATM backbone router

core connects to points of presence in 17 countries forming a distributed star architecture that minimizes the number of separate transmissions, or hops, necessary to transmit data, resulting in greater speed and reliability for our customers' end-users. Our four distributed data centers permit us to disseminate information reliably on a global basis and, using our sophisticated data tracking capability, allow us to optimize data transmissions internationally, minimizing the use of expensive transoceanic fiber optic circuits. The Digital Island network is designed to increase the speed and reliability of data transmission and circumvents a design weakness of the public Internet, which requires transmission of information over numerous routers and network inter-exchange points, often leading to delays and loss of data. Local Content Managers, where customers can store files which are repeatedly accessed within the regional area, are located in Australia, Japan, Germany, the United Kingdom and all three U.S. data centers. We believe our distributed star architecture is superior to traditional meshed networks for the distribution of centralized, hybrid and distributed applications because of its manageability, scalability and connectivity over dedicated lines to local Internet service providers and network service providers through dedicated points of presence.

We currently have direct connections in 17 countries with one or more local Internet service providers, providing customers with direct access to local markets worldwide. Currently, we purchase transit from AT&T, GTE, Sprint and MCI WorldCom in the United States and have established transport relationships in 16 other countries, giving us a total of 25 different direct points of connection to the Internet. Unlike traditional peering relationships, these network service providers carry the Internet traffic of our customers without any reciprocal transit agreement. While Digital Island pays a fee to the network service providers for this arrangement, it gives us access to thousands of Internet service providers without the obligation of carrying traffic originating outside of our network. Both the Santa Clara and New York data centers have direct

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connections through circuits with each of the four network service providers. In addition to the U.S., we have established private peering relationships in 16 other countries as listed below:

<TABLE>
<S> <C> <C>
Australia Israel South Korea
Brazil Japan Sweden
Canada Mexico Taiwan
China Netherlands United Kingdom
France Russia
Germany Singapore
</TABLE>

In China, we have connections in both Hong Kong and Beijing. With 25 different peering points to the Internet, we believe we offer our customers one of the most diverse, redundant and reliable networks for the deployment of e-business applications globally.

We currently have a state-of-the-art network operations center, headquartered in Honolulu, Hawaii, which provides real time end-to-end monitoring of our network 24 hours per day, seven days a week, 365 days per year. The network operations center helps us to ensure the efficient and reliable performance of our network, enabling us to identify, and often prevent, potential network disruptions and to respond immediately to actual disruptions. In addition, through traffic management and forecasting, line performance reporting and alarm monitoring, remote link restoration and coordination, and provisioning of network services, the network operations center enables us to schedule and conduct maintenance with minimal interferences to the network.

We currently lease lines or bandwidth from multiple telecommunications carriers. These carriers include MCI WorldCom, GTE and Sprint, as well as several international carriers such as Cable & Wireless, IDC, Telstra and Singapore Telecom. Leasing from multiple carriers assists us in achieving competitive pricing, provides us with diversity of routes and redundancy and provides access to multiple sources of bandwidth on different cable systems globally. Our lease contract term with a carrier is typically one year, which allows us to benefit from declining bandwidth costs over time. In some cases the term may extend to three years where we determine there is a significant cost advantage implicit in such arrangement or that the route served by such line is bandwidth constrained.

Services

We offer a family of services designed to allow companies to deploy their IP applications globally without developing or acquiring their own global network. Our services are especially suited to IP applications requiring a high performance end user experience which is consistent and reliable when downloading files (e.g., software, documentation and video clips), downloading graphic-intensive web content or engaging in real-time transactions (e.g., transaction clearing and video conferencing) across a range of access speeds. We work with each of our customers to optimize cost and performance requirements. Our content hosting, mirroring and caching services allow customer applications to be replicated throughout the network to lower costs and improve response times and our transport services guarantee bandwidth into local markets. Our network engineering team provides our customers with global IP networking expertise and consultation in the design and deployment of their applications on the Digital Island Global IP Applications Network. We also provide 24 hours per day, seven days per week, 365 days per year operations support and security experts to keep their applications up and running on a global basis.

We currently offer service level guarantees, customized billing, security services, network management and other application services designed to improve the performance of applications deployed on our network. We plan to continue to develop or acquire extensions to our application services to fuel ongoing product and service delivery. For example, we believe that our proprietary TraceWare technology, which is not yet commercially released, enables our customers to identify the source of IP requests as well as the destinations of Internet traffic. This technology will be predominantly used for targeted advertising and local language content delivery.

Application Hosting and Content Distribution Services

Our application hosting and content distribution services, including mirroring and caching, enable customers to gain the benefit of having their application (whether on a server on their site or on a server in one of our data centers) appear to be located in every country where we have a point of presence. Leveraging our network architecture, multi-cast technologies and distributed server arrays, our application hosting services provide end users globally with fast, reliable and seamless access to our customers' content. Each of our data centers has state-of-the-art power management, security, and fire suppression systems. Customers have access to our network operations center and our on-site personnel for ongoing maintenance services. Customers can choose from the following packages:

Server Management Package. This is an all-inclusive solution for customers seeking to outsource their day-to-day hardware and server administration. We operate two production-ready environments: Sun Solaris(TM) and Windows NT(TM) operating on Compaq servers. We host these servers, as well as servers provided by our customers, in our data centers and provide the network infrastructure as well as application monitoring, performance optimization, server administration and security services. This package provides a production-ready environment with maximum uptime.

Hardware Management Package. This enables our customers to outsource day-to-day hardware maintenance, while allowing our customers' IT staff unhindered access to perform any needed system administration functions. This package includes services from our data center personnel for hardware management and repair plus access to our network infrastructure. Our locally load balanced network architecture provides optimized routing, resulting in the uptime, performance, and reliability required by our customers.

Co-location Package. This allows our customers to house their own servers in one of our data centers, and provides a secure environment designed to deliver maximum uptime for the server plus access to our global IP application network.

Globeport. For customers choosing to maintain content at their own data centers, we will arrange dedicated connections from the client's site to our closest point of presence. This package includes network services enabling our customers to extend their reach globally.

Network Services

We offer a range of network services to be used with our Application Hosting and Content Distribution Services:

Open Bandwidth. Customers pay a minimum monthly fee for access to our network and are charged based on actual usage (per gigabit) above these minimum levels. Customers may also pay for services based on distance traveled. Customers can generate utilization reports which allow them to determine usage flows by country.

Reserved Bandwidth. Reserved Bandwidth is a network service that guarantees a minimum throughput level, expressed in kilobytes per second to a specified point of presence. Our customer is billed for a pre-specified minimum amount of data transfer to that specified point of presence. Unlike frame relay services, our network is engineered to accommodate peaks in traffic above the minimum guaranteed levels. Gigabytes in excess of the reserved monthly amount are billed at the applicable data transfer rate.

Managed Bandwidth. Managed Bandwidth is our premium network transport service offering. Using a web browser interface, IT professionals can readily allocate bandwidth by geographic region at any time from any location. Through this service, IT professionals can configure the Digital Island network to meet their organization's international throughput requirements.

Professional Services

We augment our primary product and service offerings with a range of professional service options for customers. Professional services include security audits, server/database optimization, application deployment consulting and application management and monitoring services.

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Customers

We primarily target leading customers in industries which are early adopters of Internet technologies, such as the financial services, technology, media and other Internet-centric sectors. Within our target markets, we have tailored our services to enhance the performance of our customers in electronic commerce, electronic services and electronic fulfillment, such as digital media distribution. Our customers use our services and proprietary technology to facilitate the deployment of commercial applications, including electronic

commerce, online customer service, software distribution, multimedia document distribution, sales force automation and distance learning. As of March 31, 1999, we had contracts with 62 customers including Autodesk, Cisco Systems, Diamond Multimedia Systems, E*TRADE, Mastercard International, National Semiconductor, Novell, and Platinum Technology.

The following examples, which are based on information furnished by the companies listed below, illustrate how certain customers use our global e-business network for deployment of business-critical applications:

Autodesk. Autodesk is a supplier of design software and multimedia tools that address several markets including architectural and mechanical design, filmmaking, videography and geographic information systems. Autodesk was seeking a mechanism to distribute their technical documentation and software to customers in over 150 countries. Using Digital Island's Server Management Package and Managed Bandwidth services, Autodesk customers experience consistent, reliable, secure and fast access to download documentation and software worldwide.

Cisco Systems. Cisco Systems is a leading provider of networking software and hardware for the Internet. Cisco sought a highly reliable and fast way for engineers to access the Cisco customer care online website in order to download Cisco software and to upgrade routers in the field. Using a combination of our Globeport, Hardware and Server Management Packages and our Open Bandwidth services and mirroring technology, Cisco was able to increase customer service by allowing the field engineers and customers to access critical information and download software while working at the client site.

E*TRADE. E*TRADE is an online financial services company that has engaged Digital Island to provide a broad range of network solutions to deliver mission-critical applications in 32 countries and provide their customers with consistent performance online. E*TRADE customers rely on the Internet for their trading and research requests, making the applications that provide these services mission-critical to E*TRADE's business. The applications serving these requests also require high levels of consistent bandwidth. By utilizing our Globeport Package and customized network services, E*TRADE provides its customers worldwide with a more consistent, fast and high quality online experience.

National Semiconductor. National Semiconductor is a multinational company that develops and manufactures semiconductor products for high growth markets in the electronics equipment industry. National Semiconductor needed a real-time global solution for distributing their technical documentation to customer engineers and technical information to their sales-force. Utilizing Digital Island's Co-location Package and network services, National Semiconductor is able to globally deploy technical documents to customers on a real-time basis, thereby greatly reducing documentation delivery times and costs. Digital Island's network also enables National Semiconductor to communicate with its global sales force on a real-time basis to assess demand and forecast

production levels.

Sales and Marketing

Our sales and marketing strategy is designed to target multinational businesses that depend on the Internet for mission-critical operations.

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To reach these enterprises, we utilize a multi-tiered channel approach. In North America, we primarily rely on direct sales and augment this effort with resellers, agents or co-marketing partners where appropriate. In Europe, Asia and Latin America, we are hiring direct sales personnel and developing agents and reseller channels. Our channel partners also provide services to us in the form of data center capacity, connectivity to local backbones or service providers and router installation/repair.

We are actively seeking to increase our sales and distribution capabilities globally. Currently, most of our sales are derived from the efforts of our direct sales force. We have begun developing an indirect sales channel targeting content developers (such as firms that develop Web sites), system integrators, consulting companies, suppliers and international Internet service providers. As of March 31, 1999, we had five channel partners in Europe and Asia.

Our marketing organization is responsible for product management, product marketing, public relations and marketing communications. Product management includes defining the product plan and bringing to market our products and services. These activities include product strategy and definition, pricing, competitive analysis, product launches, channel program development and product life cycle management. We stimulate product demand through a broad range of marketing communications and public relations activities. Primary marketing communications activities include public relations, collateral, advertising, direct response programs and management of our Web site. Our public relations focuses on cultivating industry analyst and media relationships with the goal of securing broad media coverage and recognition as a leader and innovator in global IP application deployment.

A key element of the our marketing strategy includes identifying and partnering with component suppliers, customers and other application service companies. We have a dedicated team focused on creating new, and expanding existing, relationships which will be critical to the ongoing success of future product developments.

Customer Support

We seek to provide superior customer service by understanding the technical requirements and business objectives of our customers and fulfilling their

needs proactively on an individual basis. By working closely with the customer, we seek to optimize the performance of our customers' Internet operations, avoid downtime, resolve quickly any problems that may arise and make adjustments in services as customer needs change over time.

Before sales are made, we provide technical advice to customers in order to help them understand their networking needs and how our products and services can provide solutions for particular needs. During the installation phase, we assign a support team led by our Customer Advocacy group which also retains support responsibility for the account after the customer's application is installed and operational, to assist the customer through the installation process. After commencing services, primary technical support is provided by our network operation center, which is operated 24 hours per day, seven days per week by highly trained technicians who respond to customer calls, monitor site and network operations and escalate problems to engineering to solve problems quickly and professionally. Our Customer Advocacy personnel are also available to assist with billing and business issues and to assist in planning for additional customer applications usage on the network.

Finally we employ network engineers who collaborate with customers to design and maintain their application across the network. Our network engineers are trained on Windows NT, Solaris and other UNIX platforms, as well as Cisco routers and switches, and they serve as the escalation path to resolve customer problems. We also employ a team of network backbone engineers that constantly monitor the network design and effectiveness to optimize performance for customers, rerouting and redesigning their applications as conditions require.

Competition

Our market is highly competitive. There are few substantial barriers to entry and we expect that we will face additional competition from existing competitors and new market entrants in the future. The principal competitive factors in this market include Internet system engineering expertise, customer service, network capability, reliability, quality of service and scalability, broad geographic presence, brand name recognition, technical expertise and functionality, the variety of services offered, the ability to maintain and expand distribution channels, price, the timing of introductions of new services, network security, financial resources and conformity with industry standards. We may not have the resources or expertise to compete successfully in the future.

Our current and potential competitors in the market include:

. information technology and Internet outsourcing firms;

. national and regional Internet service providers; and

. global, regional and local telecommunications companies.

Our competitors may operate in one or more of these areas and include companies such as AboveNet Communications, Inc., AT&T Corp., Exodus Communications, Inc., GTE Corporation, MCI WorldCom, Inc. and certain business units of Frontier GlobalCenter, Inc. In particular, Exodus and GlobalCenter provide services that are directly competitive with certain of the services that we provide.

Many of our competitors have substantially greater financial, technical and marketing resources, larger customer bases, longer operating histories, greater name recognition and more established relationships in the industry than we do. As a result, certain of these competitors may be able to develop and expand their network infrastructures and service offerings more quickly, adapt to new or emerging technologies and changes in customer requirements more quickly, take advantage of acquisition and other opportunities more readily, devote greater resources to the marketing and sale of their products and adopt more aggressive pricing policies than we can. In addition, these competitors have entered and will likely continue to enter into joint ventures or consortiums to provide additional services competitive with those that we provide.

Some of our competitors may be able to provide customers with additional benefits in connection with their Internet system and global applications network solutions, including reduced communications costs, which could reduce the overall costs of their services relative to the cost of our services. We may not be able to offset the effects of any such price reductions. In addition, we believe that the businesses in which we compete are likely to encounter consolidation in the near future, which could result in increased price and other competition that could cause our business and prospects to suffer.

Intellectual Property Rights

We rely on a combination of copyright, trademark, service mark and trade secret laws and contractual restrictions to establish and protect certain proprietary rights in our products and services. Although we have filed a patent application with respect to our TraceWare technology with the United States Patent and Trademark Office, or "PTO," such application is pending and we currently have no patented technology that would preclude or inhibit competitors from entering our market. In addition, we have registered the mark "Digital Island" with the PTO, and we have a pending trademark application for the mark "TraceWare" with the PTO. Our "Digital Island" mark is either registered or pending in several foreign countries. We have entered into confidentiality and invention assignment agreements with our employees, and nondisclosure agreements with our suppliers, distributors and appropriate customers in order to limit access to and disclosure of our proprietary information. These contractual arrangements or the other steps that we take to

protect our intellectual property may not be sufficient to prevent misappropriation of our

technology or to deter independent third-party development of similar technologies. The laws of certain foreign countries may not protect our products, services or intellectual property rights to the same extent as do the laws of the United States.

To date, we have not been notified that our products infringe the proprietary rights of third parties, but third parties may in the future claim that our current or future products infringe upon their proprietary rights. We expect that participants in our markets will be increasingly subject to infringement claims as the number of products and competitors in our industry segment grows. Any such claim, whether meritorious or not, could be time consuming, result in costly litigation, cause product installation delays or require us to enter into royalty or licensing agreements. Such royalty or licensing agreements might not be available on terms acceptable to us, or at all. As a result, any such claim could harm our business and prospects.

Government Regulation

Federal Regulation. The FCC does not currently regulate value-added network software or computer equipment-related services that transport data or voice messages on telecommunications facilities, except when provided by any of the Regional Bell Operating Companies. However, we provide value-added IP-based network services including transmitting data over public telephone lines, and those transmissions are governed to some extent by federal regulatory policies establishing charges and terms for wireline communications. Operators of those types of value-added networks that provide access to regulated transmission facilities only as part of a data services package currently are not subject to direct regulation as "telecommunications carriers" by the FCC or any other federal agency, other than regulations generally applicable to businesses.

The absence of direct FCC regulation reflects, in part, the status of Internet services as a relatively recent phenomenon. The federal legal and regulatory framework for such services is therefore in its nascent state of development.

The evolving state of federal law and regulation is reflected in the FCC's April 10, 1998 Report to Congress. In the April 1998 Report, the FCC discussed whether Internet service providers should be classified as telecommunications carriers, and, on that basis, be required to contribute to the Universal Service Fund, or "USF." The report concluded that Internet access service which the FCC defined as an offering combining computer processing, information storage, protocol conversion, and routing transmissions is an "information service" under the Telecommunications Act of 1996 and thus not subject to

regulation. In contrast, the FCC found that the provision of transmission capabilities to Internet service providers and other information service providers does constitute "telecommunications services" under the Telecommunications Act of 1996. Consequently, parties providing those latter services are presently subject to FCC regulation (and the corresponding USF obligations).

New federal laws and regulations may be adopted in the future that would subject the provision of our Internet services to government regulation. Legislative initiatives currently being considered in Congress, for example, may require taxation of Internet-related services like those that we offer or impose access charges on Internet service providers. Any new laws regarding the Internet, particularly those that impose regulatory or financial burdens, could cause our business and prospects to suffer. We cannot predict the impact, if any, that any future changes in law or regulation may have on our business.

Certain changes in federal law and regulations could cause our business and prospects to suffer. Changes of particular concern include those that directly or indirectly affect the regulatory status of Internet services, increase the cost telecommunications services (including the application of access charges or USF contribution obligations to Internet services), or increase the competition from the RBOCs and other telecommunications companies. We cannot predict the impact, if any, that such legislative or regulatory changes may have on our

business. For instance, the FCC could determine through any one of its ongoing or future proceedings that the Internet is subject to regulation. In that event, we could be required to comply with:

- FCC entry or exit regulations;
- tariff filing, reporting, fee, and record-keeping requirements;
- marketing restrictions;
- access charge obligations; and
- USF obligations.

Any one or more of those changes could have a material adverse impact on our ability to provide certain services, our results of operations and financial condition. The FCC could similarly conclude that providing Internet transport or telephony services over an IP-based network is subject to regulation. For example, the FCC currently has ongoing proceedings in which it is considering whether to regulate certain transmissions provided via the Internet, such as services functionally equivalent to traditional two-way voice telephony. Such

determination could cause our business and prospects to suffer.

Another major and unresolved regulatory issue concerns the obligation of information service providers, including Internet service providers, to pay access charges to Incumbent Local Exchange Carriers, or "ILECs". A proceeding initiated by the FCC in December 1996 that raises the issue whether ILECs can assess interstate access charges on information service providers, including Internet service providers. Unlike basic services, enhanced services, which the FCC has concluded are synonymous with information services and include Internet access services, are exempt from interstate access charges. The FCC has reaffirmed that information service providers are exempt from access charges, and a United States Court of Appeals has affirmed this decision by the FCC.

Another major regulatory issue concerns Internet-based telephony. In its April 1998 Report, the FCC observed that IP telephony appears to be a telecommunications service rather than an unregulated information service. The FCC explained that it would determine on a case-by-case basis whether to regulate the service and thereby require providers of IP telephony to contribute to the USF. The ultimate resolution of IP telephony issues could negatively impact the regulatory status, cost and other aspects of our service offerings.

Another major and unresolved regulatory proceeding that could affect the benefit and cost of our service offerings (to the extent we become involved in the exchange of communications traffic) involves reciprocal compensation. Reciprocal compensation relates to the fees paid by one carrier to terminate traffic on another carrier's network. In July 1997, the FCC was asked to determine whether Competitive Local Exchange, Carriers, or "CLECs," that serve Internet service providers are entitled to reciprocal compensation under the Telecommunications Act of 1996 for calls originated by customers of an ILEC to an Internet service provider served by a CLEC within the same local calling area. Prior to the time the FCC addressed the issue, every state that addressed the issue from an intrastate perspective (at least twenty-nine in number) determined that calls to Internet service providers are to be treated as local for purposes of reciprocal compensation. In February 1999, the FCC concluded that it would regulate in the future calls to Internet service providers as interstate traffic. The FCC sought comment on how this traffic should be compensated prospectively between carriers. The FCC's ultimate resolution of the compensation issue could increase Internet service provider costs in the future by increasing telephone charges if the FCC adopts a rule that precludes compensation for calls to Internet service providers or prescribes a rate that is substantially less than the reciprocal compensation rates that were paid in the past and are being paid under some existing inter-carrier agreements.

We could also be harmed by federal (as well as state) laws and regulations relating to the liability of on-line services companies and Internet access providers for information carried on or disseminated through their networks. Several private lawsuits seeking to impose such liability upon on-line services companies and Internet access providers are currently pending. In addition,

legislation has been enacted and new legislation has imposed liability for the transmission of, or prohibits the transmission of certain types of, information on the Internet, including sexually explicit and gambling information. The United States Supreme Court has

already held unconstitutional certain sections of the Communications Decency Act of 1996 that, among other provisions, proposed to impose criminal penalties on anyone distributing "indecent" material to minors over the Internet. Congress subsequently enacted legislation that imposes both criminal and civil penalties on persons who knowingly or intentionally make available materials through the Internet that are "harmful" to minors. However, the new law generally excludes from the definition of "person" Internet service providers that are not involved in the selection of content disseminated through their networks. Congress also enacted legislation recently that limits liability for online copyright infringement. That latter law includes exemptions which enable Internet service providers to avoid copyright infringement if they merely transmit material produced and requested by others. It is possible that other laws and regulations could be enacted in the future that would place copyright infringement liability more directly on Internet service providers. The imposition of potential liability on us and other Internet access providers for information carried on or disseminated through their systems could require us to implement measures to reduce our exposure to such liability, which may in turn require us to expend substantial resources or to discontinue certain service or product offerings. The increased attention to liability issues as a result of lawsuits and legislative action, could similarly impact the growth of Internet use. While we carry professional liability insurance, such insurance may not be adequate to compensate claimants or may not cover us in the event we become liable for information carried on or disseminated through our networks. Any costs not covered by insurance incurred as a result of such liability or asserted liability could cause our business and prospects to suffer.

State Regulation. The proliferation of Internet use in the past several years has prompted state legislators and regulators to consider the adoption of laws and regulations to govern Internet usage. Much of the legislation that has been proposed to date may, if enacted, handicap further growth in the use of the Internet. It is possible that state legislatures and regulators will attempt to regulate the Internet in the future, either by regulating transactions or by restricting the content of the available information and services. While state public utility commissions generally have declined to directly regulate enhanced or information services, some states have continued to regulate particular aspects of enhanced services in limited circumstances, such as where they are provided by local telecommunications carriers. Moreover, the public utility commissions of certain states continue to consider potential regulation of such service. Enactment of such legislation or adoption of such regulations could have a material adverse impact on us.

Another area of adverse potential state regulation concerns taxes. The United States Congress recently enacted a three-year moratorium on new state and local taxes on the Internet (those not generally imposed or actually enforced prior to October 1, 1998) as well as on taxes that discriminate against commerce through the Internet. Congress also established an advisory commission to study and make recommendations on the federal, state and local taxation of Internet-related commerce. These recommendations are due to Congress by April 2000 and could serve as the basis for additional legislation. Previous to the enactment of the tax moratorium a significant number of bills had been introduced in state legislatures that would have taxed commercial transactions on the Internet. Future laws or regulatory changes that lead to state taxation of Internet transactions could cause our business and prospects to suffer.

One issue of growing importance revolves around contract law. Although customer-level use of the Internet to conduct commercial transactions is still in its infancy, a growing number of corporate entities are engaging in Internet transactions. This Internet commerce has spawned a number of state legal and regulatory issues, such as whether and how certain provisions of the Uniform Commercial Code (adopted by 49 states) apply to transactions carried out on the Internet and how to decide which jurisdiction's laws are to be applied to a particular transaction. It is not possible to predict how state law will evolve to address new transactional circumstances created by Internet commerce or whether the evolution of such laws will cause our business and prospects to suffer.

State legislators and regulators have also sought to restrict the transition or limit access to certain materials on the Internet. For example, in the past several years, various state legislators have sought to limit or prohibit:

. certain communications between adults and minors;

. anonymous and pseudonymous use of the Internet;

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. on-line gambling; and

. the offering of securities on the Internet.

Enforcement of such limitations or prohibitions in some states could affect transmission in other states. State laws and regulations that restrict access to certain materials on the Internet could inadvertently block access to other permissible sites. We cannot predict the impact, if any, that any future laws or regulatory changes in this area may have on our business.

Some states have also sought to impose tort liability or criminal penalties on certain conduct involving the Internet, such as the use of "hate" speech,

invasion of privacy, and fraud. The adoption of such laws could adversely impact the transmission of non-offensive material on the Internet and, to that extent, could cause our business and prospects to suffer.

Local Regulation. Although local jurisdictions generally have not sought to regulate the Internet and related services, it is possible that such jurisdictions will seek to impose regulations in the future. In particular, local jurisdictions may attempt to tax various aspects of Internet access or services, such as transactions handled through the Internet or subscriber access, as a way of generating municipal revenue. The imposition of local taxes and other regulatory burdens by local jurisdictions could cause our business and prospects to suffer. Our networks may also be subject to numerous local regulations such as building codes and licensing. Such regulations vary on a city by city and county by county basis.

Foreign Regulation. As our services become available over the Internet in foreign countries, and as we facilitate sales by our customers to end users located in such foreign countries, such jurisdictions may claim that we are required to qualify to do business in the particular foreign country or to obtain certain permits or licenses to provide permits or licenses to provide value-added network services. Our failure to qualify as a foreign corporation in a jurisdiction where we are required to do so could subject us to taxes and penalties and could result in our inability to enforce contracts in such jurisdictions. It is possible that claims could be made against online service companies and Internet service providers under foreign law for defamation, negligence, copyright or trademark infringement, or other theories based on the nature and content of the materials disseminated through their networks. Any such new legislation or regulation, or the application of laws or regulations from jurisdictions whose laws do not currently apply to our business, could cause our business and prospects to suffer.

Employees

As of March 31, 1999, we had 146 employees, including 64 people in sales and marketing, 34 people in engineering, 32 people in operations and 16 people in finance and administration. We believe that our future success will depend in part on our continued ability to attract, hire and retain qualified personnel. The competition for such personnel is intense, and there can be no assurance that we will be able to identify, attract and retain such personnel in the future. None of our employees is represented by a labor union, and management believes that our employee relations are good.

Facilities

We currently have the following facilities: our corporate headquarters in San Francisco, and data centers in Honolulu, Santa Clara (California), New York City, and London. We intend to move our corporate headquarters to a new location in San Francisco in July 1999. We plan to open an additional data center in Hong Kong in September 1999. In addition, we have sales offices in

Boston, New York City, Minneapolis, Chicago, Philadelphia, Dallas, Houston, St. Louis, Japan, Malaysia, the Netherlands, Switzerland and the United Kingdom.

Legal Proceedings

We are not party to any material legal proceeding.

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MANAGEMENT

Officers, Directors and Senior Management

The following table sets forth the names and ages of our executive officers and directors and certain members of our senior management as of March 31, 1999.

<TABLE>
<CAPTION>

Name	Age	Position
<S>	<C>	<C>
Ron Higgins	41	Chairman of the Board of Directors
Ruann F. Ernst(1)(4)	52	Chief Executive Officer and President and Director
T.L. Thompson	52	Chief Financial Officer
Paul Evenson	38	Vice President of Operations
Sanne Higgins	49	Vice President of Corporate Communications
Allan Leinwand	32	Vice President of Engineering and Chief Technology Officer
Bruce Pinsky	35	Vice President of Solutions Engineering and Chief Information Officer
Michael T. Sullivan	48	Vice President of Finance
Rick Schultz	40	Vice President of North American Sales
Tim Wilson	39	Vice President of Marketing and International Sales
Charlie Bass(2)	57	Director

Christos Cotsakos(4)..... 50 Director

Marcelo A. Gumucio(2)(3)(4)..... 61 Director

Cliff Higgerson (1)(3)..... 57 Director

Shahan Soghikian(1)..... 40 Director

David Spreng..... 37 Director
</TABLE>
- ----------
(1) Member of Executive Committee

(2) Member of Compensation Committee

(3) Member of Audit Committee

(4) Member of Nominating Committee

Each director will hold office until the next annual meeting of stockholders and until such director's successor is elected and qualified or until such director's earlier resignation or removal. Each officer serves at the discretion of the Board of Directors of Digital Island.

Ron Higgins has served as Chairman of the Board of Directors since June 1998 and as a director since February 1994, when he founded Digital Island. Mr. Higgins served as President and Chief Executive Officer from February 1994 until June 1998 and as Chairman of the Board of Directors from February 1994 until January 1998. For the past 18 years, Mr. Higgins has been involved in developing high technology companies in the areas of networking, communications, desktop publishing and multimedia. Mr. Higgins holds a B.S. in Business Administration from the University of Southern California.

Ruann F. Ernst has served as President and Chief Executive Officer and as a director since June 1998. Prior to joining Digital Island, Ms. Ernst served with Hewlett Packard for over ten years, most recently as

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general manager of the Financial Services Business Unit. Ms. Ernst has also served as Director, Medical Computing Services Division and Assistant Professor, Medicine and Computer Science at The Ohio State University and as a Congressional Fellow in the Office of Technology Assessment. Ms. Ernst serves on the Board of Directors of The Institute for the Future, Phoenix International and Advanced Fibre Communications, Inc. Ms. Ernst holds a B.S. in Mathematics, a Masters Degree in Computer Science and a Ph.D. in Technology and Organizational Change from The Ohio State University.

T.L. Thompson has served as Chief Financial Officer since January 1999. Mr. Thompson served as Chief Financial Officer of Narrowline from October 1996 to November 1998. From 1989 to 1996 he served in various financial capacities at Ziff-Davis Publishing Company, most recently as Vice President of Business Development. Mr. Thompson holds a B.S. in Economics and an M.B.A. from Northwestern University.

Paul Evenson has served as Vice President of Operations since November 1998. From 1996 to 1998, Mr. Evenson served as Vice President of Sales and Operations at Westech Communications, Inc. From 1986 to 1996, Mr. Evenson served as Vice President of Information Technology at Montgomery Securities. Mr. Evenson studied Engineering at Oregon State University.

Sanne Higgins joined Digital Island in June 1996 and has served as Vice President of Corporate Communications since October 1997. From March 1990 to June 1996, Ms. Higgins served as an independent marketing consultant to companies with a broad range of products, including local area networking, hardware, computer displays, video and computer entertainment, software productivity tools, robotics and in-circuit test equipment. Ms. Higgins holds a B.A. from the California College of Arts & Crafts.

Allan Leinwand has served as Vice President of Engineering and Chief Technology Officer of Digital Island since January 1997 and as a director from January 1997 to February 1999. Prior to joining Digital Island, from August 1990 to February 1997, Mr. Leinwand served as Manager, Consulting Engineer at Cisco Systems, where he designed and deployed global internetworks for large corporations, governments and institutions. Mr. Leinwand also served as a network design and implementation engineer at Hewlett Packard from 1988 to 1990. Mr. Leinwand holds a B.S. in Computer Science from the University of Colorado, Boulder.

Bruce Pinsky has served as Vice President of Solutions Engineering and Chief Information Officer since March 1997. From August 1992 to March 1997, Mr. Pinsky worked in Customer Engineering and Global Support Engineering for Cisco Systems. Mr. Pinsky holds a B.S. in Computer Science from California State University, Hayward.

Michael T. Sullivan has served as Vice President of Finance since May 1997 and served as Chief Financial Officer from October 1997 to January 1999. From July 1993 to May 1996 Mr. Sullivan served as Vice President of Operations and Chief Financial Officer for Tut Systems. Mr. Sullivan holds a B.S. in Business Administration from the University of California, Berkeley.

Rick Schultz has served as Vice President of North American Sales since March 1999. From December 1995 to February 1999, Mr. Schultz served as Vice President of Sales at Pacific Bell Network Integration, a subsidiary of Pacific Bell. Mr. Schultz also held various senior management positions at AT&T from June 1980 to November 1995 in Sales, Product Management and Sales Management.

Mr. Schultz holds a B.S. in Commerce from De Paul University and an M.B.A. from the University of San Francisco.

Tim Wilson has served as Vice President of Marketing and International Sales since March 1998. From January 1996 to March 1998, Mr. Wilson served as general manager within the Business Communications Systems Division of Lucent Technologies. Mr. Wilson also served as Executive Director and General Manager of the Business Communications Systems Division of AT&T Australia from November 1993 to December 1995. From August 1983 to October 1993, Mr. Wilson held several management positions in engineering, sales and marketing at AT&T Corp. and AT&T Bell Laboratories. Mr. Wilson holds a B.A. in Physics from Bowdoin College and an M.B.A. from the Fuqua School of Business at Duke University.

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Charlie Bass has served as a director since March 1997. Dr. Bass is Trustee of The Bass Trust, General Partner of Bass Associates and a Consulting Professor of Electrical Engineering at Stanford University. He is also Chairman of the Board of Directors of Meridian Data, Inc., Socket Communications, Inc. and SoloPoint, Inc. and a member of the Board of Directors of several private communications companies. Prior to co-founding Ungermann-Bass in 1979, Dr. Bass was at Zilog, Inc., and prior to the formation of Zilog, Inc. in 1975, he was on the Electrical Engineering and Computer Sciences faculty at the University of California at Berkeley from 1972 to 1975. Dr. Bass holds a Ph.D. in Electrical Engineering from the University of Hawaii where he participated in the Aloha System research in radio frequency-based computer networks.

Christos Cotsakos has served as a director of Digital Island since July 1998. Mr. Cotsakos joined E*TRADE in March 1996 as the President and Chief Executive Officer and as a director. Before joining E*TRADE, he served as President, Chief Operating Officer, Co-Chief Executive Officer and a director of AC Nielsen Inc. Prior to joining AC Nielsen, Mr. Cotsakos spent 19 years with Federal Express Corporation, where he held a number of senior executive positions. Mr. Cotsakos serves on the Board of Directors of several technology companies, both publicly traded and private. A decorated Vietnam veteran, he received a B.A. from William Paterson College and an M.B.A. from Pepperdine University. Mr. Cotsakos is currently pursuing a Ph.D. degree in economics at the University of London.

Marcelo A. Gumucio has served as a director since January 1998, and served as Chairman of the Board of Directors from January 1998 until May 1998. He is the managing partner of Gumucio Burke & Associates, a private investment firm. In April 1996, Mr. Gumucio joined Micro Focus PLC as its Chief Executive Officer. He had served as a non-executive director of Micro Focus' Board of Directors since January 1996. Prior to joining Micro Focus, from 1992 to 1996, Mr. Gumucio was President, Chief Executive Officer and Chairman of the Board of Directors of Memorex Telex NV. Mr. Gumucio's professional experience in the computer and communications industry spans almost 30 years and includes senior

management positions at Cray Research, Inc., Northern Telecom Limited, Memorex Corporation and Hewlett-Packard Company. Mr. Gumucio is a member of the Board of Directors of BidCom Inc., E-Stamp Corporation and Burr Brown Corporation. Mr. Gumucio graduated cum laude with a B.S. in mathematics from the University of San Francisco in 1961. He received an M.S. in applied mathematics and operations research in 1963 from the University of Idaho, where he was named a National Science Fellow and graduated with honors. In 1982, he graduated from the Harvard Business School Advanced Management Program.

Cliff Higgerson has served as a director since March 1997. Mr. Higgerson has over 20 years experience with venture capital investments. Prior to forming Communications Ventures II in the summer of 1997, he was a General Partner of Vanguard Venture Partners, where he has been since 1993 and where he continues to manage several portfolio companies. His 25 years of involvement in the communications field include research, consulting, planning, investment banking, and venture capital. Mr. Higgerson serves on the Board of Directors of Advanced Fibre Communications, Inc., Ciena Corp. and Digital Microwave Corp., as well as several private companies. Mr. Higgerson holds a B.S. in electrical engineering and an M.B.A. from the Haas School of Business at the University of California at Berkeley.

Shahan Soghikian has served as a director since February 1999. Mr. Soghikian has over nine years experience with venture capital investments and is a General Partner of Chase Capital Partners, where he has been since 1990, and where he develops, executes and monitors investments in private companies. Mr. Soghikian serves on the Board of Directors of two private companies, Nextec Applications, Inc. and AFS Holdings. Mr. Soghikian graduated with a B.A. in Biology from Pitzer College and an M.B.A. from Anderson School of Business at the University of California at Los Angeles.

David Spreng has served as a director since July 1997. Mr. Spreng has over 10 years of venture capital investment experience, primarily in communications, and served as President of IAI Ventures, the private equity arm of Investment Advisers, Inc. from 1992 until September 1998, when Mr. Spreng became the

Managing Member of the General Partners of the successor in interest to IAI Ventures and IAI, the Crescendo Funds and its management company. Mr. Spreng serves on the Board of Directors of Tut Systems, Inc. and several private companies. Mr. Spreng graduated from the University of Minnesota with a B.S. in Accounting.

Director Compensation

Our directors do not currently receive compensation for their services as members of the Board of Directors. All directors are reimbursed for their reasonable out-of-pocket expenses in serving on the Board of Directors or any

committee thereof. Employee directors are eligible to participate in our 1998 Stock Option/Stock Issuance Plan and will also be eligible to receive equity incentives, in the form of stock option grants or direct stock issuances, under our 1999 Stock Incentive Plan.

Non-employee board members will receive option grants at periodic intervals under the Automatic Option Grant Program of the 1999 Stock Incentive Plan and will also be eligible to receive discretionary option grants under the Discretionary Option Grant Program of such plan. See "Executive Compensation and Other Information--Employee Benefit Plans."

Classified Board

Our certificate of incorporation provides for a classified Board of Directors consisting of three classes of directors, each serving staggered three-year terms. As a result, a portion of our Board of Directors will be elected each year. To implement the classified structure, prior to the consummation of the offering, two of the nominees to the board will be elected to one-year terms, three will be elected to two-year terms and three will be elected to three-year terms. Thereafter, directors will be elected for three-year terms. Ron Higgins and David Spreng have been designated Class I directors whose term expires at the 2000 annual meeting of stockholders. Charlie Bass, Cliff Higgerson and Shahan Soghikian have been designated Class II directors whose term expires at the 2001 annual meeting of stockholders. Christos Cotsakos, Ruann Ernst and Marcelo Gumucio have been designated Class III directors whose term expires at the 2002 annual meeting of stockholders. See "Description of Capital Stock--Antitakeover Effects of Provisions of Certain Charter Provisions, Bylaws and Delaware Law."

Officers are appointed by the Board of Directors on an annual basis and serve until their successors have been duly elected and qualified. Ron and Sanne Higgins are husband and wife. There are no other family relationships among any of the directors, officers or key employees of Digital Island.

Board Committees

The executive committee of the Board of Directors consists of Ruann Ernst, Cliff Higgerson and Shahan Soghikian. The executive committee, subject to the following limitations, acts upon all matters concerning our interests, and manages our business when the full Board of Directors is not in session. Our executive committee may not:

. Adopt, amend or repeal the bylaws;

. Elect directors to fill vacancies on the board;

. Fill vacancies on the executive committee, or change its membership;

. Elect to remove officers of Digital Island;

. Amend the corporate charter;

. Act on matters assigned to other committees of the board;

. Appoint standing committees of the board;

. Recommend to the stockholders any action requiring their approval; or

. Approve the acquisition or disposal of any capital asset or assets to be used by us or any subsidiary in an amount exceeding an aggregate $3,000,000 in any interim period between meetings of the board.

The audit committee of the Board of Directors consists of Marcelo Gumucio and Cliff Higgerson. The audit committee reviews our financial statements and accounting practices, makes recommendations to the Board of Directors regarding the selection of independent auditors and reviews the results and scope of our annual audit and other services provided by our independent auditors.

The compensation committee of the Board of Directors consists of Charlie Bass and Marcelo Gumucio. The compensation committee makes recommendations to the Board of Directors concerning salaries and incentive compensation for our officers and employees and administers our employee benefit plans.

The nominating committee of the Board of Directors consists of Christos Cotsakos, Ruann Ernst and Marcelo Gumucio. The nominating committee makes recommendations to the Board of Directors concerning candidates for directorships.

Compensation Committee Interlocks and Insider Participation

None of the members of the compensation committee of the Board of Directors was at any time since the formation of Digital Island an officer or employee of Digital Island. No executive officer of Digital Island serves as a member of the Board of Directors or compensation committee of any entity that has one or more executive officers serving on our Board of Directors or our compensation committee of the Board of Directors.

EXECUTIVE COMPENSATION AND OTHER INFORMATION

Summary of Cash and Certain Other Compensation

The following table sets forth the compensation earned by our Named

Executive Officers which include our Chief Executive Officer and our three other executive officers whose salary and bonus for services rendered in all capacities to Digital Island for the fiscal year ended September 30, 1998 exceeded $100,000. Since such date, certain of these executive officers have been succeeded by new persons and we have added additional officers. For a list of our current executive officers and certain members of senior management, see "Management."

Summary Compensation Table

<TABLE>
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		Annual Compensation		Long Term Compensation Awards	
Name and Principal Position(s)	Year	Salary	Bonus		Number of Securities Underlying Options(1)
<S>	<C>	<C>	<C>		<C>
Ruann F. Ernst(2)..... President and Chief Executive Officer	1998	$ 50,000	$ --		794,159
Allan Leinwand ..... Chief Technology Officer	1998	124,167	41,000		288,000
Michael T. Sullivan(3)..... Vice President of Finance	1998	136,250	25,750		100,000
Ron Higgins(4)..... Chairman of the Board of Directors	1998	130,615	20,000		400,000

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(1) The options listed in the table were originally granted under either our Stock Option and Incentive Plan or our 1998 Stock Option/Stock Issuance Plan. These options have been incorporated into the new 1999 Stock Incentive Plan, but will continue to be governed by their existing terms. See "Executive Compensation and Other Information--Employee Benefit Plans."

(2) Ms. Ernst has served as President and Chief Executive Officer of Digital Island since June 1998.

(3) Mr. Sullivan served as Chief Financial Officer of Digital Island in 1998 and was succeeded by T.L. Thompson in such position in January 1999.

(4) Mr. Higgins served as President and Chief Executive Officer of Digital Island from February 1994 until June 1998.

Stock Options and Stock Appreciation Rights

The following table sets forth information regarding option grants to each

of the Named Executive Officers during the fiscal year ended September 30, 1998. No stock appreciation rights were granted to the Named Executive Officers during the 1998 fiscal year.

Stock Option Grants in Fiscal Year 1998

<TABLE>
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Name	Number of Securities Underlying Options Granted (#)	Percentage of Total Options Granted to Employees in 1998	Exercise Price Per Share ($/Sh)	Expiration Date	Potential Realizable Value at Assumed Annual Rates of Stock Price Appreciation for Option Term 5%	10%
<S>	<C>	<C>	<C>	<C>	<C>	
Ruann F. Ernst.....	794,159	41.7%	$1.50	5/31/08	$ 1,940,402	$ 3,089,766
Allan Leinwand.....	48,000	2.5%	1.50	6/17/08	117,280	186,749
Michael T. Sullivan.....	--	--	--	--	--	--
Ron Higgins.....	--	--	--	--	--	--

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Each option has a maximum term of 10 years, subject to earlier termination upon the optionee's cessation of service with Digital Island. Ms. Ernst joined Digital Island as our President and Chief Executive Officer on June 1, 1998 and was granted an option for 794,159 shares with an exercise price of $1.50 per share, effective on her June 1, 1998 start date. The first 635,327 shares, subject to her options, will vest in a series of 50 successive equal monthly installments upon her completion of each month of service over the 50-month period measured from her hire date, and the remaining 158,832 shares will vest in a series of 50 successive equal monthly installments over the 50-month period measured from the first anniversary of her hire date. All the option shares will vest upon an involuntary termination of her employment (other than for cause) within 18 months following an acquisition of Digital Island by merger, sale of substantially all the assets or sale of more than 50% of our outstanding voting securities. Upon any other involuntary termination of her employment (other than for cause), the vesting of her option shares will be accelerated by six months. The option granted to Mr. Leinwand for 48,000 shares will begin to vest starting April 2, 2001 in 24 successive equal monthly installments.

The actual stock price appreciation over the 10-year option term may not be at the above 5% and 10% assumed annual rates of compounded stock price appreciation or at any other defined level. Unless the market price of common stock appreciates over the option term, no value will be realized from the

option grant made to the Named Executive Officer.

Aggregated Option/SAR Exercises and Fiscal Year-End Values

The following table sets forth information with respect to the Named Executive Officers concerning their exercise of stock options during the fiscal year ended September 30, 1998 and the number of shares subject to unexercised stock options held by them as of the close of such fiscal year. No stock appreciation rights were exercised during the fiscal year ended September 30, 1998, and no stock appreciation rights were outstanding at the close of such year.

Aggregated Option Exercises in 1998 and Year-End Values

<TABLE>
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	Shares Acquired on Exercise (#)	Value Realized ($)(1)	Number of Securities Underlying Unexercised Options at Year-End		Value of Unexercised In-the-Money Options at Year-End(2)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Ruann F. Ernst.....	100,000	0.00	443,492	250,667	$776,111	$438,667
Allan Leinwand.....	--	--	132,534	155,466	377,722	390,278
Michael T. Sullivan.....	--	--	32,000	68,000	91,200	193,800
Ron Higgins.....	--	--	158,333	241,667	451,249	688,751

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(1) Equal to the difference between the fair value of the shares at the time of exercise ($1.50 per share) and the exercise price paid for the shares ($1.50 per share).

(2) Based upon the fair value per share at the close of the 1998 fiscal year ($3.25) less the exercise price payable per share.

Employee Benefit Plans

1999 Stock Incentive Plan

Our 1999 Stock Incentive Plan is intended to serve as the successor equity incentive program to our 1998 Stock Option/Stock Issuance Plan which was the successor equity incentive program to our Stock Option and Incentive Plan. The 1999 Stock Incentive Plan was adopted by the board on April 21, 1999 and was subsequently approved by the stockholders on , 1999. The 1999 Stock Incentive Plan will become effective upon the effective date of the offering. All outstanding options under our predecessor plan will at that time be incorporated into the 1999 Stock Incentive Plan, and no further option grants will be made under that plan. The incorporated options will continue to be

governed by their existing terms, unless the plan

administrator elects to extend one or more features of the 1999 Incentive Plan to those options. Except as otherwise noted below, the incorporated options have substantially the same terms as will be in effect for grants made under the Discretionary Option Grant Program of the 1999 Stock Incentive Plan.

An initial reserve of 7,544,000 shares of common stock has been authorized for issuance under the 1999 Stock Incentive Plan. This share reserve consists of (i) the number of shares estimated to remain available for issuance under our predecessor plan, including the shares subject to outstanding options thereunder, plus (ii) an additional increase of approximately 2,500,000 shares. The number of shares of common stock reserved for issuance under the 1999 Stock Incentive Plan will automatically increase on the first trading day in January each calendar year, beginning in calendar year 2000, by an amount equal to four percent (4%) of the total number of shares of common stock outstanding on the last trading day in December in the preceding calendar year, but in no event will this annual increase exceed 2,000,000 shares. In addition, no participant in the 1999 Stock Incentive Plan may be granted stock options, separately exercisable stock appreciation rights and direct stock issuances for more than 750,000 shares of common stock in the aggregate per calendar year.

The 1999 Stock Incentive Plan is divided into five separate components:

- the Discretionary Option Grant Program, under which eligible individuals in our employ or service (including officers, non-employee board members and consultants) may, at the discretion of the plan administrator, be granted options to purchase shares of common stock at an exercise price not less than 100% of the fair market value of those shares on the grant date;

- the Stock Issuance Program under which eligible individuals may, in the plan administrator's discretion, be issued shares of common stock directly, upon the attainment of designated performance milestones or upon the completion of a specified service requirement or as a bonus for past services;

- the Salary Investment Option Grant Program, which may, at the plan administrator's sole discretion, be activated for one or more calendar years and, if so activated, will allow executive officers and other key executives selected by the plan administrator the opportunity to apply a portion of their base salary each year to the acquisition of special below-market stock option grants;

- the Automatic Option Grant Program, under which option grants will automatically be made at periodic intervals to eligible non-employee

board members to purchase shares of common stock at an exercise price equal to 100% of the fair market value of those shares on the grant date; and

- the Director Fee Option Grant Program, which may, in the plan administrator's sole discretion, be activated for one or more calendar years and, if so activated, will allow non-employee board members the opportunity to apply all or a portion of the annual retainer fee otherwise payable to them in cash each year to the acquisition of special below-market option grants.

The Discretionary Option Grant Program and the Stock Issuance Program will be administered by the compensation committee. The compensation committee as plan administrator will have complete discretion to determine which eligible individuals are to receive option grants or stock issuances under those programs, the time or times when the grants or issuances are to be made, the number of shares subject to each grant or issuance, the status of any granted option as either an incentive stock option or a non-statutory stock option under the Federal tax laws, the vesting schedule to be in effect for the option grant or stock issuance and the maximum term for which any granted option is to remain outstanding. However, the board acting by a disinterested majority will have the exclusive authority to make any discretionary option grants or stock issuances to members of the compensation committee. The compensation committee will also have the exclusive authority to select the executive officers and other highly compensated employees who may participate in the Salary Investment Option Grant Program in the event that program is activated for one or more calendar years. Neither the compensation committee nor the board will exercise any administrative discretion with respect to option grants under the Salary Investment Option Grant Program or under the Automatic Option Grant or

Director Fee Option Grant Program for the non-employee board members. All grants under those latter three programs will be made in strict compliance with the express provisions of each program.

The exercise price for the shares of common stock subject to option grants made under the 1999 Stock Incentive Plan may be paid in cash or in shares of common stock valued at fair market value on the exercise date. The option may also be exercised through a same-day sale program without any cash outlay by the optionee.

The plan administrator will have the authority to effect the cancellation of outstanding options under the Discretionary Option Grant Program (including options incorporated from our three predecessor plans) in return for the grant of new options for the same or different number of option shares with an exercise price per share based upon the fair market value of the common stock on the new grant date.

Stock appreciation rights are authorized for issuance under the Discretionary Option Grant Program. These rights will provide the holders with the election to surrender their outstanding options for an appreciation distribution from us equal to the excess of (i) the fair market value of the vested shares of common stock subject to the surrendered option over (ii) the aggregate exercise price payable for those shares. Such appreciation distribution may be made in cash or in shares of common stock. None of the incorporated options from our predecessor plan contain any stock appreciation rights.

In the event that we are acquired by merger or asset sale, each outstanding option under the Discretionary Option Grant Program which is not to be assumed by the successor corporation will automatically accelerate in full, and all unvested shares under the Discretionary Option Grant and Stock Issuance Programs will immediately vest, except to the extent our repurchase rights with respect to those shares are to be assigned to the successor corporation. The plan administrator will have complete discretion to grant one or more options under the Discretionary Option Grant Program which will vest and become exercisable for all the option shares in the event those options are assumed in the acquisition and the optionee's service with us or the acquiring entity is terminated within a designated period (not to exceed eighteen months) following that acquisition. The vesting of outstanding shares under the Stock Issuance Program may be accelerated upon similar terms and conditions.

The plan administrator is also authorized to grant options and structure repurchase rights so that the shares subject to those options or repurchase rights will immediately vest in connection with a change in ownership or control (whether by successful tender offer for more than fifty percent of our outstanding voting stock or by a change in the majority of our board through one or more contested elections for board membership). Such accelerated vesting may occur either at the time of such change or upon the subsequent termination of the individual's service within a designated period (not to exceed eighteen months) following the change.

The options to be incorporated from our predecessor plan will immediately vest and become exercisable for all the option shares if we are acquired by merger or asset sale, unless the options are assumed by the successor corporation and our repurchase rights with respect to the unvested shares subject to those options are concurrently assigned to the successor entity. The board also has the authority to provide for the cancellation of those options in return for a cash payment to the option holders in an amount per cancelled option share equal to the excess of the price to be paid per share of our common stock in the acquisition over the option exercise price payable per share under the cancelled option. Should the optionee's service be terminated within a designated period following an acquisition in which the outstanding options under our predecessor plan are assumed and our repurchase rights are assigned, then all of the optionee's outstanding options under that plan will vest at that time and become immediately exercisable for all the option shares

and all unvested shares held by such individual will also vest at that time. There are no other change in control provisions currently in effect for those options. However, the plan administrator will have the discretion to extend the acceleration provisions of the 1999 Stock Incentive Plan to any or all of the options outstanding under our three predecessor plans.

In the event the plan administrator elects to activate the Salary Investment Option Grant Program for one or more calendar years, each executive officer and other key employee selected for participation may elect, prior to the start of the calendar year, to reduce his or her base salary for that calendar year by a specified

dollar amount not less than $10,000 nor more than $50,000. Each selected individual who files this timely election will automatically be granted, on the first trading day in January of the calendar year for which that salary reduction is to be in effect, a non-statutory option to purchase that number of shares of common stock determined by dividing the salary reduction amount by two-thirds of the fair market value per share of common stock on the grant date. The option will be exercisable at a price per share equal to one-third of the fair market value of the option shares on the grant date. As a result, the total spread on the option shares at the time of grant (the fair market value of the option shares on the grant date less the aggregate exercise price payable for those shares) will be equal to the amount of salary invested in that option. The option will vest and become exercisable in a series of twelve equal monthly installments over the calendar year for which the salary reduction is to be in effect.

Under the Automatic Option Grant Program, eligible non-employee board members will receive a series of option grants over their period of board service. Each individual who first becomes a non-employee board member at any time at or after the effective date of this offering will receive an option grant for 15,000 shares of common stock on the date such individual joins the board, provided such individual has not been in our prior employ. In addition, on the date of each annual stockholders meeting held after the effective date of this offering, each non-employee board member who is to continue to serve as a non-employee board member (including the individuals who are currently serving as non-employee board members) will automatically be granted an option to purchase 5,000 shares of common stock, provided such individual has served on the board for at least six months. There will be no limit on the number of such 5,000 share option grants any one eligible non-employee Board member may receive over his or her period of continued board service, and non-employee board members who have previously been in our employ will be eligible to receive one or more such annual option grants over their period of board service.

Each automatic grant will have an exercise price per share equal to the fair

market value per share of common stock on the grant date and will have a term of 10 years, subject to earlier termination following the optionee's cessation of board service. Each automatic option will be immediately exercisable for all of the option shares; however, any unvested shares purchased under the 15,000-share option will be subject to repurchase by Digital Island, at the exercise price paid per share, should the optionee cease to serve on the board prior to vesting in those shares. However, the shares will immediately vest in full upon certain changes in control or ownership or upon the optionee's death or disability while a board member. The shares subject to each annual 5,000-share automatic grant will be fully-vested when granted. The shares subject to each initial 15,000-share automatic option grant will vest in a series of six successive equal semi-annual installments upon the optionee's completion of each month of board service over the 36 month period measured from the grant date. Following the optionee's cessation of board service for any reason, each option will remain exercisable for a 12-month period and may be exercised during that time for any or all shares in which the optionee is vested at the time of such cessation of service.

The Financial Accounting Standards Board recently issued an exposure draft of a proposed interpretation of the current accounting principles applicable to equity incentive plans. Under the proposed interpretation, option grants made to non-employee board members after December 15, 1998 will result in a direct charge to the company's reported earnings based upon the fair value of the option measured initially as of the grant date of that option and then subsequently on the vesting date of each installment of the underlying option shares. If the proposed interpretation is adopted, then the following changes will be made to our automatic stock option grant program:

- The 15,000-share option grant will not be made to a newly-elected or appointed non-employee board member until the first annual stockholders meeting held more than 12 months after the date of his or her initial election or appointment to the board. At that annual meeting, the board member will also receive an option grant for an additional 5,000 shares under the annual grant portion of the program.

- One-third of the shares subject to the 15,000-share option grant will be immediately vested at the time of the option grant, and the remaining shares will vest in a series of four successive equal

semi-annual installments upon the optionee's completion of each six-month period of board service over the twenty-four month period measured from the grant date. However, the shares will immediately vest in full upon certain changes in control or ownership or upon the optionee's death or disability while a board member.

If the Director Fee Option Grant Program is activated in the future, each non-employee board member will have the opportunity to apply all or a portion of any annual retainer fee otherwise payable in cash to the acquisition of a below-market option grant. The option grant will automatically be made on the first trading day in January in the year for which the retainer fee would otherwise be payable in cash. The option will have an exercise price per share equal to one-third of the fair market value of the option shares on the grant date, and the number of shares subject to the option will be determined by dividing the amount of the retainer fee applied to the program by two-thirds of the fair market value per share of common stock on the grant date. As a result, the total spread on the option (the fair market value of the option shares on the grant date less the aggregate exercise price payable for those shares) will be equal to the portion of the retainer fee invested in that option. The option will vest and become exercisable for the option shares in a series of twelve equal monthly installments over the calendar year for which the election is to be in effect. However, the option will become immediately exercisable and vested for all the option shares upon (i) certain changes in the ownership or control or (ii) the death or disability of the optionee while serving as a board member.

The shares subject to each option under the Salary Investment Option Grant, Automatic Option Grant and Director Fee Option Grant Programs will immediately vest upon (i) an acquisition of us by merger or asset sale or (ii) the successful completion of a tender offer for more than 50% of our outstanding voting stock or a change in the majority of our board effected through one or more contested elections for board membership.

Limited stock appreciation rights will automatically be included as part of each grant made under the Automatic Option Grant, Salary Investment Option Grant and Director Fee Option Grant Programs and may be granted to one or more officers as part of their option grants under the Discretionary Option Grant Program. Options with this limited stock appreciation right may be surrendered to us upon the successful completion of a hostile tender offer for more than 50% of our outstanding voting stock. In return for the surrendered option, the optionee will be entitled to a cash distribution from us in an amount per surrendered option share equal to the excess of (i) the highest price per share of common stock paid in connection with the tender offer over (ii) the exercise price payable for such share.

The board may amend or modify the 1999 Stock Incentive Plan at any time, subject to any required stockholder approval. The 1999 Stock Incentive Plan will terminate on the earliest of (i) April 15, 2009, (ii) the date on which all shares available for issuance under the 1999 Stock Incentive Plan have been issued as fully-vested shares or (iii) the termination of all outstanding options in connection with certain changes in control or ownership.

1999 Employee Stock Purchase Plan

Our 1999 Employee Stock Purchase Plan was adopted by the board on April 21,

1999 and approved by the stockholders on , 1999 and will become effective immediately upon the execution of the Underwriting Agreement for this offering. The plan is designed to allow our eligible employees and those of our participating subsidiaries to purchase shares of common stock, at semi-annual intervals, through their periodic payroll deductions under the plan. 300,000 shares of common stock will initially be reserved for issuance under the plan. The reserve will automatically increase on the first trading day in January each year, beginning in calendar year 2000, by an amount equal to one percent (1%) of the total number of outstanding shares of our common stock on the last trading day in December in the prior year. In no event will any such annual increase exceed 500,000 shares.

The plan will be implemented in a series of successive offering periods, each with a maximum duration of 24 months. However, the initial offering period will begin on the execution date of the Underwriting Agreement

and will end on the last business day in July 2001. The next offering period will commence on the first business day in August 2001, and subsequent offering periods will commence as designated by the plan administrator.

Individuals who are eligible employees (employees scheduled to work more than 20 hours per week for more than five calendar months per year) on the start date of any offering period may enter the plan on that start date or on any subsequent semi-annual entry date (the first business day of February or August each year). Individuals who become eligible employees after the start date of the offering period may join the plan on any subsequent semi-annual entry date within that offering period.

Payroll deductions may not exceed 15% of the participant's base salary, and the accumulated payroll deductions of each participant will be applied to the purchase of shares on his or her behalf on each semi-annual purchase date (the last business day in January and July each year) at a purchase price per share equal to 85% of the lower of (i) the fair market value of the common stock on the participant's entry date into the offering period or (ii) the fair market value on the semi-annual purchase date. In no event, however, may any participant purchase more than 1,200 shares on any semi-annual purchase date, nor may all participants in the aggregate purchase more than 200,000 shares on any semi-annual purchase date. The initial purchase date under the plan will occur on January 31, 2000.

If the fair market value per share of our common stock on any purchase date is less than the fair market value per share on the start date of the two-year offering period, then that offering period will automatically terminate, and a new two-year offering period will begin on the next business day, with all participants in the terminated offering to be automatically transferred to the new offering period.

Should we be acquired by merger, sale of substantially all our assets or sale of securities possessing more than fifty percent of the total combined voting power of our outstanding securities, then all outstanding purchase rights will automatically be exercised immediately prior to the effective date of an acquisition. The purchase price will be equal to 85% of the lower of (i) the fair market value per share of common stock on the participant's entry date into the offering period in which an acquisition occurs or (ii) the fair market value per share of common stock immediately prior to an acquisition. The limitation on the maximum number of shares purchasable in the aggregate on any one purchase date will not be in effect for any purchase date attributable to such an acquisition.

The plan will terminate on the earlier of (i) the last business day of July 2009, (ii) the date on which all shares available for issuance under the plan shall have been sold pursuant to purchase rights exercised thereunder or (iii) the date on which all purchase rights are exercised in connection with an acquisition of us by merger or asset sale.

The board may at any time alter, suspend or discontinue the plan. However, certain amendments may require stockholder approval.

401(k)Plan

We sponsor the Digital Island, Inc. 401(k) Plan (the "401(k) Plan"). Employees who complete three months of service with us are eligible to participate in the 401(k) Plan and may contribute up to 15% of their current compensation, but in no event may they contribute more than the maximum dollar amount allowable per calendar year under the federal tax laws. Each participant is fully vested in his or her salary reduction contributions. Participant contributions are held in trust and the individual participants may direct the trustee to invest their accounts in a number of investment alternatives. We may make contributions to the 401(k) Plan which match a percentage of each participant's contributions for the year, with the actual percentage match (if any) for one or more plan years to be determined by us in our discretion. In addition, we may make discretionary contributions for one or more plan years which would be allocated to participants on the basis of their compensation for the plan year. Any discretionary and matching contributions which we may make to the 401(k) Plan would be subject to a vesting schedule tied to the participant's years of service with us. To date, we have not made any matching or discretionary contributions to the 401(k) Plan. We may also make fully vested qualified non-elective contributions to the 401(k) Plan on behalf of participants who are not "highly compensated," but have not done so to date.

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Employment Contracts and Change of Control Arrangements

We have entered into employment agreements with Ms. Ernst, Mr. Leinwand, and Mr. Sullivan, each of whom are executive officers. All outstanding options held by the foregoing executive officers will automatically vest in full upon an acquisition of Digital Island by merger, sale of substantially all the assets or sale of more than 50% of our outstanding voting securities, unless those options are assumed or otherwise continued in effect by a successor entity or our repurchase rights for any unvested shares subject to those options are to remain in force following such acquisition.

Ruann F. Ernst. On May 20, 1998, Ruann F. Ernst, our Chief Executive Officer and President, entered into an employment agreement with us. This agreement provided for an annual salary of $150,000. Ms. Ernst is also entitled to incentive compensation in an amount not less than forty percent (40%) of her base salary upon the achievement of performance milestones mutually agreed upon with our Board of Directors. On March 1, 1999, Ms. Ernst's annual salary was increased to $200,000. In connection with her employment agreement we granted Ms. Ernst options to purchase up to 794,159 shares of our common stock at a per share exercise price of $1.50 per share.

Allan Leinwand. On February 3, 1997, Allan Leinwand, our Vice President of Engineering and Chief Technology Officer, entered into an employment agreement with us. This agreement provided for an annual salary of $105,000. Mr. Leinwand is also eligible for a discretionary quarterly bonus of up to $10,000. Should we terminate Mr. Leinwand for any lawful reason, we must pay Mr. Leinwand a severance payment equal to one hundred percent of his then current annual base salary. Currently, Mr. Leinwand's annual salary is $170,000, and he is eligible for a discretionary quarterly bonus of up to $12,500. In connection with his employment agreement, we granted to Mr. Leinwand options to purchase up to 240,000 shares of our common stock at a per share exercise price of $0.10 per share.

Michael T. Sullivan. On May 5, 1997, Michael T. Sullivan, our Vice President of Finance, entered into an employment agreement with us. This agreement provided for an annual salary of $120,000. Mr. Sullivan is also eligible for a discretionary quarterly bonus of up to $5,000. On March 16, 1998, Mr. Sullivan's annual salary was increased to $150,000 and his discretionary quarterly bonus was increased to $7,500. In connection with his employment agreement, we granted to Mr. Sullivan options to purchase up to 100,000 shares of our common stock at a per share exercise price of $0.40 per share.

Limitation of Liability and Indemnification

Our certificate of incorporation eliminates, to the fullest extent permitted by Delaware law, liability of a director to Digital Island or our stockholders for monetary damages for conduct as a director. Although liability for monetary damages has been eliminated, equitable remedies such as injunctive relief or rescission remain available. In addition, a director is not relieved of his or her responsibilities under any other law, including the federal securities laws.

Our certificate of incorporation requires us to indemnify our directors to the fullest extent permitted by Delaware law. We have also entered into indemnification agreements with each of our directors. We believe that the limitation of liability provisions in our certificate of incorporation and indemnification agreements may enhance our ability to attract and retain qualified individuals to serve as directors. See "Description of Capital Stock."

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CERTAIN TRANSACTIONS

Some of our directors, executive officers and affiliates have entered into transactions with us as follows:

Preferred Stock Financings

Since October 1, 1997 we have sold 4,283,181 shares of our Series C Preferred Stock at a price of $3.45 per share, 2,022,476 shares of our Series D Preferred Stock at a price of $5.25 per share and 11,764,706 shares of our Series E Preferred Stock at a price of $4.25 per share in a series of private financings. We sold these securities pursuant to preferred stock purchase agreements and an investors' rights agreement on substantially similar terms (except for terms relating to date and price), under which we made standard representations, warranties, and covenants, and pursuant to which we provided the purchasers thereunder with registration rights, information rights, and rights of first refusal, among other provisions standard in venture capital financings. The purchasers of the Preferred Stock included, among others, the following holders of 5% or more of our Common Stock, directors, and entities associated with directors:

<TABLE>
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	Shares of Preferred Stock Purchased(1)		
Name	Series C	Series D	Series E
<S>	<C>	<C>	<C>
Bass Trust U/D/T dated April 29, 1988(2)	39,420	34,095	27,765
Chase Venture Capital Associates, L.P.(3)	--	--	2,823,529
The Cotsakos Revocable Trust dated 9/3/87(4)	--	28,571	--
Crescendo II, L.P.(5)	289,855(6)	143,429(6)	463,294(6)
Crosspoint Venture Partners	289,855	--	926,824

E*TRADE Group, Inc.(7)..... -- 1,333,334 562,588
FW Ventures III, LP..... -- -- 1,822,353
Marcelo Gumucio..... 29,000 -- --
Merrill Lynch KECALP..... -- -- 1,482,824
Tudor Global Trading, Inc..... 1,015,000 190,476 744,470
Vanguard V, L.P.(8)..... 260,870 142,857 --
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(1) Each share of our preferred stock will automatically convert into one share of our common stock upon the completion of the offering, except that each share of Series D Preferred Stock will automatically convert into 1.088084 shares of our common stock after giving effect to an antidilution adjustment resulting from the sale of the Series E Preferred Stock.

(2) Charlie Bass, a director of Digital Island, is the Trustee of the Bass Trust U/D/T dated April 29, 1998.

(3) Shahan Soghikian, a director of Digital Island, is a General Partner of Chase Venture Capital Associates, L.P.

(4) Christos Cotsakos, a director of Digital Island, is the Trustee of The Cotsakos Revocable Trust dated 9/3/87.

(5) David Spreng, a director of Digital Island, is the Managing Member of Crescendo Ventures II, LLC, the general partner of Crescendo II, L.P.

(6) Includes shares held by Eagle Ventures II, LLC pursuant to a parallel investment agreement with Crescendo.

(7) Mr. Cotsakos, a director of Digital Island, is Chairman of the Board of E*TRADE.

(8) Cliff Higgerson, a director of Digital Island, is the General Partner of Vanguard V, L.P.

Investors' Rights Agreement

Pursuant to the terms of the Amended and Restated Investors' Rights Agreement dated February 19, 1999, as amended, by and among Digital Island and the holders of our preferred stock, the investors acquired certain registration rights with respect to their capital stock of Digital Island. At any time after the earlier of (i) February 19, 2001, or (ii) one year after our initial public offering, holders of more than two-thirds of the currently outstanding preferred stock may require us to effect registration under the Securities Act covering the lesser of 50% of the outstanding Registrable Securities (as defined in the Investors' Rights Agreement) or a

number of shares of common stock yielding gross aggregate proceeds in excess of $15.0 million, subject in either case to the board of directors' right if such registration would harm Digital Island to defer such registration for a period up to 60 days. In addition, if we propose to issue equity securities under the Securities Act for our own account in an underwritten public offering, then any of the investors has a right (subject to quantity limitations determined by the underwriters) to request that Digital Island register such investor's Registrable Securities. All registration expenses incurred in connection with the first two demand registrations described above and all piggyback registrations will be borne by Digital Island. The participating investors will pay for underwriting discounts and commissions incurred in connection with any such registrations. We have agreed to indemnify the investors against certain liabilities in connection with any registration effected pursuant to the foregoing Investors' Rights Agreement, including Securities Act liabilities.

Co-Sale Agreement

Pursuant to the terms of a Co-Sale Agreement dated February 19, 1999 by and among Digital Island, Mr. Higgins and the investors, the investors acquired certain co-sale rights with respect to their shares of preferred stock. Subject to certain customary exceptions, in the event that Mr. Higgins proposes to sell shares of common stock, each investor may elect to participate pro-rata in such sale on the same terms and conditions as Mr. Higgins. These co-sale rights will terminate upon completion of this offering.

Employment and Indemnification Agreements

We have entered into employment agreements with Ms. Ernst, Mr. Leinwand and Mr. Sullivan, who are Named Executive Officers. We have also entered into indemnification agreements with each of our other directors and officers. See "Executive Compensation and Other Information--Employment Contracts and Change of Control Arrangements," and "--Limitation of Liability and Indemnification." On January 1, 1997, Sanne Higgins, our Vice President of Corporate Communications, and the spouse of Ron Higgins our Chairman of the Board of Directors, entered into an employment agreement with us. This agreement provided for an annual salary of $100,000 and has been increased to $125,000. Ms. Higgins is also eligible for a discretionary annual bonus of up to $40,000. In connection with her employment agreement, we granted to Ms. Higgins options to purchase up to 75,000 shares of our common stock at a per share exercise price of $0.40 per share.

Director Arrangements and Stockholder Notes

In February 1998, Digital Island granted a nonstatutory option to purchase a total of 183,000 shares of our common stock to Marcelo Gumucio, then the Chairman of the Board of Directors and now a director of Digital Island. These options were immediately exercisable and subject to repurchase by Digital Island, with the right to repurchase expiring in 16 equal quarterly

installments. At the time of the option grant, Mr. Gumucio exercised the option to purchase the entire 183,000 shares of common stock, in exchange for a $109,800 note. Under the terms of the note, interest accrues on outstanding amounts at 5.61% per annum. Interest is to be repaid in four equal annual installments commencing February 24, 1999. The entire principal amount is due and payable in one lump sum on February 24, 2002. As of March 31, 1999, the outstanding unpaid principal balance of the shareholder note was $109,800. Mr. Gumucio also received an aggregate of $60,000 in 1998 in connection with his services to us as Chairman of our Board of Directors.

Officer Loans

On April 21, 1999, Ms. Ernst, our President and Chief Executive Officer, and Mr. Higgins, our Chairman of the Board, each delivered a promissory note to us in payment of the exercise price of certain outstanding stock options they hold under our 1998 Stock Option/Stock Issuance Plan. Ms. Ernst delivered a full-recourse promissory note in the principal amount of $179,999 in payment of the exercise price for 119,999 shares of our common stock, and Mr. Higgins delivered a full-recourse promissory note in the amount of $86,400 in payment of the exercise price for 216,000 shares of our common stock. Each note bears interest at the rate of 7.75% per annum, compounded semi-annually, and is secured by the purchased shares. Accrued interest is due and

payable at successive quarterly intervals over the four-year term of the note, and the principal balance will become due and payable in one lump sum at the end of such four-year term. However, the entire unpaid balance of the note will become due and payable upon termination of employment or failure to pay any installment of interest when due. None of the shares serving as security for the note may be sold unless the principal portion of the note attributable to those shares, together with the accrued interest on that principal portion, is paid to us.

E*TRADE Agreements

We have entered into a global data distribution agreement with E*TRADE dated August 1, 1997 where we provide network connectivity for E*TRADE. Mr. Costakos, a member of our Board of Directors, is President, Chief Executive Officer and a director of E*TRADE.

We believe that all of the transactions set forth above were made on terms no less favorable to us than could have been obtained from unaffiliated third parties. We intend that all future transactions, including loans, between us and our officers, directors, principal stockholders and their affiliates will be approved by a majority of the Board of Directors, and be on terms no less favorable to us than could be obtained from unaffiliated third parties.

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PRINCIPAL STOCKHOLDERS

The following table sets forth certain information as of March 31, 1999 (except as indicated in the footnotes below) with respect to the beneficial ownership of our common stock by:

- each person known by us to own beneficially more than 5%, in the aggregate, of the outstanding shares of our common stock,
- the directors and Named Executive Officers of Digital Island who hold securities of Digital Island, and
- all executive officers and directors as a group.

Unless otherwise indicated, the address for each shareholder is c/o Digital Island, 353 Sacramento Street, Suite 1520, San Francisco, CA 94111.

<TABLE>
<CAPTION>

	Beneficial Ownership of Shares Before the Offering(2)(3)		Beneficial Ownership of Shares After the Offering(4)	
Name of Beneficial Owner(1)	Number	Percent	Number	Percent
<S>	<C>	<C>	<C>	<C>
Crosspoint Venture Partners(5)	3,246,679	11.7%	3,246,679	
Chase Venture Capital Associates, L.P.(6)	2,823,529	10.1%	2,823,529	
Vanguard V, L.P(7)	2,561,310	9.2%	2,561,310	
Crescendo Venture Management, LLC(8)	2,109,212	7.6%	2,109,212	
E*TRADE Group, Inc.(9)	2,013,367	7.2%	2,013,367	
Tudor Global Trading, Inc.(10)	1,966,724	7.1%	1,966,724	
FW Ventures III, LP(11)	1,882,353	6.8%	1,882,353	
Merrill Lynch KECALP(12)	1,482,824	5.3%	1,482,824	
Ron Higgins(13)	2,075,000	7.4%	2,075,000	
Ruann F. Ernst(14)	836,159	2.9%	836,159	
T. L. Thompson(15)	251,000	*	251,000	
Paul Evenson(16)	200,000	*	200,000	
Allan Leinwand(17)	195,267	*	195,267	
Rick Schultz(18)	200,000	*	200,000	
Michael T. Sullivan(19)	83,000	*	83,000	
Tim Wilson(20)	179,200	*	179,200	
Charlie Bass(21)	419,283	1.5%	419,283	
Marcelo A. Gumucio(22)	212,000	*	212,000	

Christos Cotsakos(23).....	36,644	*	36,644		
Cliff Higgerson(24).....	--	--	--	--	
Shahan Soghikian(25).....	--	--	--	--	
David Spreng(26).....	--	--	--	--	
All directors and executive officers as a group (14 people)(27).....	4,687,553	16.2%	4,687,553		

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* Less than 1%.

(1) Except as indicated by footnote, we understand that the persons named in the table above have sole voting and investment power with respect to all shares shown as beneficially owned by them, subject to community property laws where applicable.

(2) Shares of common stock subject to options, which are currently exercisable or exercisable within 60 days of March 31, 1999, are deemed outstanding for computing the percentages of the person holding such options but are not deemed outstanding for computing the percentages of any other person.

(3) The number of shares reflects the number of shares of common stock in the aggregate assuming the conversion of the preferred stock. Each share of preferred stock is currently convertible into one share of common stock, with the exception of the Series D Preferred Stock, each share of which currently

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converts into 1.088084 shares of common stock. Percentage ownership is based on 27,870,736 shares of common stock and preferred stock, as converted, outstanding as of March 31, 1999. See "Description of Capital Stock--Preferred Stock."

(4) "Beneficial Ownership of Shares Before Offering" reflects the beneficial ownership of the common stock, assuming the conversion of the preferred stock. "Beneficial Ownership of Shares After Offering" reflects the beneficial ownership of the common stock, assuming the conversion of the preferred stock and after giving effect to the Offering.

(5) Stock consists of 1,450,000 shares of Series A Preferred Stock held directly by Crosspoint Venture Partners, 580,000 shares of Series B Preferred Stock and 289,855 shares of Series C Preferred Stock held directly by Crosspoint Venture Partners 1996 and 926,824 shares of Series E Preferred Stock held directly by Crosspoint Venture Partners LS 1997 (collectively, with Crosspoint Venture Partners 1996 and Crosspoint Venture Partners, the "Crosspoint Entities"). The address for the Crosspoint Entities is 2925 Woodside Road, Woodside, California 94062.

(6) Stock consists of 2,823,529 shares of Series E Preferred Stock. Mr. Soghikian, a director of Digital Island, is the General Partner of Chase Capital Partners, the General Partner of Chase Venture Capital Associates, L.P. The address for Chase Venture Capital Associates, L.P. is 50 California Street, Suite 2940, San Francisco, CA 94111.

(7) Stock includes 95,000 shares subject to warrants exercisable for common stock, 1,450,000 shares of Series A Preferred Stock, 600,000 shares of Series B Preferred Stock, 260,870 shares of Series C Preferred Stock and 142,857 shares of Series D Preferred Stock. Mr. Higgerson, a director of Digital Island, is the General Partner of Vanguard V, L.P. The address of Vanguard V, L.P. is 505 Hamilton Avenue, Suite 305, Palo Alto, California 94301.

(8) Stock consists of an aggregate of 1,200,000 shares of Series B Preferred Stock, 289,855 shares of Series C Preferred Stock, 143,429 shares of Series D Preferred Stock and 463,294 shares of Series E Preferred Stock held directly by Eagle Ventures II, LLC and Crescendo II, L.P. (collectively, the "Crescendo Entities"). Mr. Spreng, a director of Digital Island, is the President of Eagle Ventures II, LLC and the Managing Member of Crescendo Ventures II, LLC, the General Partner of Crescendo II, LP. The address for the Crescendo Entities is 505 Hamilton Avenue, Suite 315, Palo Alto, CA 94301.

(9) Stock consists of 1,333,334 shares of Series D Preferred Stock and 562,588 shares of Series E Preferred Stock. Mr. Cotsakos, a director of Digital Island, is Chairman of the Board and Chief Executive Officer of E*TRADE Group, Inc. The address of E*TRADE Group, Inc. is Four Embarcadero Place, 2400 Geng Road, Palo Alto, California 94303.

(10) Stock consists of an aggregate of 1,015,000 shares of Series C Preferred Stock, 190,476 shares of Series D Preferred Stock and 744,470 shares of Series E Preferred Stock held directly by Raptor Global Fund L.P., Raptor Global Fund Ltd. and Tudor Private Equity Fund L.P. (collectively, the "Tudor Entities"). The address for the Tudor Entities is Tudor Global Trading, Inc., 40 Rowes Wharf, Second Floor, Boston, Massachusetts 02110.

(11) Stock consists of 1,882,353 shares of Series E Preferred Stock. The address of FW Ventures III, LP is 2775 Sand Hill Road, Menlo Park, CA 94025.

(12) Stock consists of 1,482,824 shares of Series E Preferred Stock held directly by KECALP, Inc., KECALP Inc., as Nominee for Merrill Lynch KECALP International L.P. 1997 and Merrill Lynch KECALP L.P. (collectively, the "Merrill Lynch KECALP Entities"). The address for the Merrill Lynch KECALP Entities is Word Financial Center, North Tower, New York, NY 10281.

(13) Stock consists of 1,575,000 shares of common stock held directly by Mr.

Higgins, 225,000 shares of common stock subject to options exercisable within 60 days of March 31, 1999, of which 216,000 shares

were exercised by Mr. Higgins on April 20, 1999, 100,000 shares of common stock held directly by the Ron and Sanne Higgins 1998 Irrevocable Trust Agreement f/b/o Dana Espinoza (the "Espinoza Trust"), 100,000 shares of common stock held directly by the Ron and Sanne Higgins 1998 Irrevocable Trust Agreement f/b/o Nina Higgins (the "Higgins Trust") and 75,000 shares held by the Ron and Sanne Higgins 1998 Irrevocable Grandchildren's Trust Agreement (the "Grandchildren's Trust"). Mr. Higgins is a Trustee of the Espinoza Trust, the Higgins Trust and the Grandchildren's Trust.

(14) Stock consists of 100,000 shares of common stock held directly by Ms. Ernst and 736,159 shares of common stock subject to options exercisable within 60 days of March 31, 1999, of which 119,999 shares were exercised by Ms. Ernst on April 20, 1999.

(15) Stock consists of common stock subject to options exercisable within 60 days of March 31, 1999.

(16) Stock consists of common stock subject to options exercisable within 60 days of March 31, 1999.

(17) Stock consists of common stock subject to options exercisable within 60 days of March 31, 1999, of which 125,000 shares were exercised by Mr. Leinwand on April 9, 1999.

(18) Stock consists of common stock subject to options exercisable within 60 days of March 31, 1999.

(19) Stock consists of 25,000 shares of common stock held directly by Mr. Sullivan and 58,000 shares of common stock subject to options exercisable within 60 days of March 31, 1999, of which 46,000 shares were exercised by Mr. Sullivan on April 21, 1999.

(20) Stock consists of common stock subject to options exercisable within 60 days of March 31, 1999, of which 41,400 shares were exercised by Mr. Wilson on April 20, 1999.

(21) Stock consists of 225,000 shares of Series A Preferred Stock, 90,000 shares of Series B Preferred Stock, 39,420 shares of Series C Preferred Stock, 34,095 shares of Series D Preferred Stock and 27,765 shares of Series E Preferred Stock held directly by the Bass Trust U/D/T dated April 29, 1988 (the "Bass Trust"). Mr. Bass, a director of Digital Island, is the Trustee of the Bass Trust.

(22) Stock consists of 183,000 shares of common stock and 29,000 shares of Series C Preferred Stock.

(23) Stock consists of 5,556 shares of common stock subject to options exercisable within 60 days of March 31, 1999 and 28,571 shares of Series D Preferred Stock held directly by The Cotsakos Revocable Trust dated September 3, 1987. Excludes 2,013,367 shares of preferred stock, as converted, held by E*TRADE Group, Inc. Mr. Cotsakos, a director of Digital Island, is the Trustee of the Cotsakos Trust and Chairman of the Board and Chief Executive Officer of E*TRADE Group, Inc. Mr. Cotsakos disclaims beneficial ownership of the shares of preferred stock held by E*TRADE Group, Inc. except to the extent of his pecuniary interest therein. See footnote 9 above.

(24) Excludes an aggregate of 2,561,310 shares comprised of warrants exercisable for common stock and preferred stock, as converted, held by Vanguard V, L.P. Mr. Higgerson, a director of Digital Island, is the General Partner of Vanguard V, L.P. Mr. Higgerson disclaims beneficial ownership of warrants exercisable for common stock and preferred stock held by Vanguard V, L.P. except to the extent of his pecuniary interest therein. See footnote 7 above.

(25) Excludes 2,823,529 shares of preferred stock, as converted, held by Chase Venture Capital Associates, L.P. Mr. Soghikian, a director of Digital Island, is the General Partner of Chase Capital Partners, the General Partner of Chase Venture Capital Associates, L.P. Mr. Soghikian disclaims beneficial ownership of the shares of preferred stock held by Chase Venture Capital Associates, L.P. except to the extent of his pecuniary interest therein. See footnote 6 above.

(26) Excludes an aggregate 2,109,212 shares of preferred stock, as converted, held by the Crescendo Entities. Mr. Spreng, a director of Digital Island, is the President of Eagle Ventures II, LLC and the Managing Member of Crescendo Ventures II, LLC, the General Partner of Crescendo. Mr. Spreng disclaims beneficial ownership of the shares of preferred stock held by the Crescendo Entities, except to the extent of his pecuniary interest therein. See footnote 8 above.

(27) See footnotes 13 through 26 above. Includes options exercisable for 2,050,182 shares of common stock within 60 days of March 31, 1999 under the 1998 Stock Option/Stock Issuance Plan.

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DESCRIPTION OF CAPITAL STOCK

Upon the closing of this offering, the authorized capital stock of Digital Island will consist of 100,000,000 shares of common stock, $0.001 par value per

share, and 10,000,000 shares of preferred stock, $0.001 par value per share.

Common Stock

As of March 31, 1999, 2,622,225 shares of our common stock were outstanding and held of record by 35 stockholders. After this offering, shares will be outstanding. Concurrently with the completion of this offering, each outstanding share of our preferred stock will be exchanged for and converted into one share of our common stock, except that each share of our Series D Preferred Stock will convert into 1.088084 shares of our common stock to reflect a price based antidilution adjustment. The following description of rights assumes this conversion.

Holders of common stock are entitled to receive dividends as may from time to time be declared by our Board of Directors out of funds legally available therefor. See "Dividend Policy." Holders of common stock are entitled to one vote per share on all matters on which the holders of common stock are entitled to vote and do not have any cumulative voting rights. Holders of common stock have no preemptive, conversion, redemption or sinking fund rights. In the event of a liquidation, dissolution or winding up of Digital Island, holders of common stock are entitled to share equally and ratably in the assets of the Digital Island, if any, remaining after the payment of all our liabilities and the liquidation preference of any then outstanding class or series of preferred stock. The outstanding shares of common stock are, and the shares of common stock offered by us in this offering when issued will be, fully paid and nonassessable. The rights, preferences and privileges of holders of common stock are subject to any series of preferred stock that we may issue in the future, as described below.

Preferred Stock

Our Board of Directors has the authority to issue preferred stock in one or more series and to fix the number of shares constituting any such series and the preferences, limitations and relative rights, including dividend rights, dividend rate, voting rights, terms of redemption, redemption price or prices, conversion rights and liquidation preferences of the shares constituting any series, without any further vote or action by our stockholders. The issuance of preferred stock by our Board of Directors could adversely affect the rights of holders of common stock.

The potential issuance of preferred stock may have the effect of delaying or preventing a change in control of Digital Island, may discourage bids for our common stock at a premium over the market price of the common stock and may adversely affect the market price of, and the voting and other rights of the holders of, common stock. Immediately after this offering there will be no shares of preferred stock outstanding and we have no current plans to issue shares of preferred stock.

Certain Anti-Takeover, Limited Liability and Indemnification Provisions

Effect of Delaware Anti-takeover Statute. We are subject to Section 203 of the Delaware General Corporation Law, as amended ("Section 203"), which, subject to certain exceptions, prohibits a Delaware corporation from engaging in any business combination with any interested stockholder for a period of three years following the date that such stockholder became an interested stockholder, unless:

- prior to such date, the board of directors of the corporation approved either the business combination or the transaction that resulted in the stockholder becoming an interested stockholder;

- upon consummation of the transaction that resulted in the stockholder becoming an interested stockholder, the interested stockholder owned at least 85% of the voting stock of the corporation outstanding at the time the transaction commenced, excluding for purposes of determining the number of shares outstanding those shares owned (1) by persons who are directors and also officers and (2) by employee stock plans in which employee participants do not have the right to determine confidentially whether shares held subject to the plan will be tendered in a tender or exchange offer; or

- on or subsequent to such date, the business combination is approved by the board of directors and authorized at an annual or special meeting of stockholders, and not by written consent, by the affirmative vote of at least 66 2/3% of the outstanding voting stock that is not owned by the interested stockholder.

Section 203 defines business combinations to include:

- any merger or consolidation involving the corporation or any majority-owned subsidiary of the corporation and any other person or entity;

- subject to certain exceptions, any sale, transfer, pledge or other disposition of 10% or more of the assets of the corporation or any majority-owned subsidiary of the corporation involving the interested stockholder;

- subject to certain exceptions, any transaction that results in the issuance or transfer by the corporation or any majority-owned subsidiary of the corporation of any stock of the corporation to the interested stockholder;

- any transaction involving the corporation or any majority-owned

subsidiary of the corporation that has the effect of increasing the proportionate share of the stock of any class or series of the corporation or any majority-owned subsidiary of the corporation beneficially owned by the interested stockholder; or

. the receipt by the interested stockholder of the benefit of any loans, advances, guarantees, pledges or other financial benefits provided by or through the corporation or any majority-owned subsidiary of the corporation.

In general, Section 203 defines an interested stockholder as any entity or person beneficially owning 15% or more or the outstanding voting stock of the corporation and any entity or person affiliated with or controlling or controlled by such entity or person.

Certificate of Incorporation and Bylaw Provisions. Our certificate of incorporation and bylaws include provisions that may have the effect of discouraging, delaying or preventing a change in control of Digital Island or an unsolicited acquisition proposal that a stockholder might consider favorable, including a proposal that might result in the payment of a premium over the market price for the shares held by stockholders. These provisions are summarized in the following paragraphs.

Classified Board of Directors. Our certificate of incorporation and bylaws provide for our board to be divided into three classes of directors serving staggered, three year terms. The classification of the board has the effect of requiring at least two annual stockholder meetings, instead of one, to replace a majority of the members of the Board of Directors.

Supermajority Voting. Our certificate of incorporation requires the approval of the holders of at least 66 2/3% of our combined voting power to effect certain amendments to the certificate of incorporation or to effect any business combination (as defined in Section 203) relating to us. Our bylaws may be amended by either a majority of the Board of Directors, or the holders of a majority of our voting stock, provided that certain amendments approved by stockholders require the approval of at least 66 2/3% of our combined voting power.

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Authorized but Unissued or Undesignated Capital Stock. Our authorized capital stock consists of 100,000,000 shares of common stock and 10,000,000 shares of preferred stock. No preferred stock will be designated upon consummation of this offering. After this offering, we will have outstanding shares of common stock. The authorized but unissued (and in the case of preferred stock, undesignated) stock may be issued by the Board of Directors in one or more transactions. In this regard, our certificate of incorporation grants the Board of Directors broad power to establish the rights and

preferences of authorized and unissued preferred stock. The issuance of shares of preferred stock pursuant to the Board of Director's authority described above could decrease the amount of earnings and assets available for distribution to holders of common stock and adversely affect the rights and powers, including voting rights, of such holders and may have the effect of delaying, deferring or preventing a change in control of Digital Island. The Board of Directors does not currently intend to seek stockholder approval prior to any issuance of preferred stock, unless otherwise required by law or the rules of any exchange on which our securities are then traded.

Special Meetings of Stockholders. Our bylaws provide that special meetings of stockholders of Digital Island may be called only by the Board of Directors, or by our Chairman of the Board of Directors or President.

No Stockholder Action by Written Consent. Our certificate of incorporation and bylaws provide that an action required or permitted to be taken at any annual or special meeting of the stockholders of Digital Island may only be taken at a duly called annual or special meeting of stockholders. This provision prevents stockholders from initiating or effecting any action by written consent.

Notice Procedures. Our bylaws establish advance notice procedures with regard to all stockholder proposals to be brought before meetings of stockholders of Digital Island, including proposals relating to the nomination of candidates for election as directors, the removal of directors and amendments to our certificate of incorporation or bylaws. These procedures provide that notice of such stockholder proposals must be timely given in writing to the Secretary of Digital Island prior to the meeting. Generally, to be timely, notice must be received by our Secretary not less than 120 days prior to the meeting. The notice must contain certain information specified in the bylaws.

Other Anti-Takeover Provisions. See "Executive Compensation and Other Information--Employee Benefit Plans" for a discussion of certain provisions of the 1999 Stock Incentive Plan which may have the effect of discouraging, delaying or preventing a change in control of Digital Island or unsolicited acquisition proposals.

Limitation of Director Liability. Our certificate of incorporation limits the liability of our directors (in their capacity as directors but not in their capacity as officers) to Digital Island or our stockholders to the fullest extent permitted by Delaware law. Specifically, directors of Digital Island will not be personally liable for monetary damages for breach of a director's fiduciary duty as a director, except for liability:

- for any breach of the director's duty of loyalty to Digital Island or our stockholders;

- for acts or omissions not in good faith or which involve intentional

misconduct or a knowing violation of law;

- under Section 174 of the Delaware General Corporation Law, which relates to unlawful payments of dividends or unlawful stock repurchases or redemptions; or

- for any transaction from which the director derived an improper personal benefit.

Indemnification Arrangements. Our bylaws provide that the directors and officers of Digital Island shall be indemnified and provide for the advancement to them of expenses in connection with actual or threatened proceedings and claims arising out of their status as such to the fullest extent permitted by the Delaware General Corporation Law. Prior to consummation of this offering, we will enter into indemnification

agreements with each of our directors and executives officers that will provide them with rights to indemnification and expense advancement to the fullest extent permitted under the Delaware General Corporation Law.

Transfer Agent and Registrar

The transfer agent and registrar for the common stock is BankBoston, N.A.

SHARES ELIGIBLE FOR FUTURE SALE

Prior to this offering, there has not been any public market for our common stock. Future sales of substantial amounts of common stock in the public market, or the prospect of such sales, could adversely affect prevailing market prices.

Upon completion of this offering, shares of common stock will be outstanding. Of these shares, all of the shares sold in this offering will be freely tradeable without restriction under the Securities Act, unless purchased by an "affiliate" of Digital Island, as that term is defined in Rule 144. The remaining shares outstanding after completion of this offering are "restricted securities" as defined in Rule 144 and may be sold in the public market only if registered under the Securities Act or if they qualify for an exemption from registration, including an exemption pursuant to Rule 144.

All holders of our outstanding common stock as of the date hereof have agreed that, subject to certain exceptions and consents, during the period beginning from the date of this prospectus, and continuing to and including the

date 180 days after the date of this prospectus, they will not offer, sell, contract to sell or otherwise dispose of any securities of Digital Island. Upon expiration of these agreements, shares will be eligible for immediate resale in the public market subject to the volume and other limitations of Rule 144, and shares will be eligible for immediate resale pursuant to Rule 144(k) without such limitations, unless they are held by affiliates of Digital Island. Of such shares, approximately will be eligible for immediate resale in the public market pursuant to Rule 144 subject to the volume and manner of sale limitations in Rule 144 and shares will be eligible for resale without such volume limitations.

In general under Rule 144, a person, including an "affiliate" of Digital Island, who has beneficially owned restricted shares for at least one year is entitled to sell within any three-month period a number of shares that does not exceed the greater of 1% of the then outstanding shares of common stock (approximately shares immediately following this offering) or the average weekly trading volume of the common stock during the four calendar weeks preceding such sale. Sales under Rule 144 are subject to certain manner of sale limitations, notice requirements and the availability of current public information about Digital Island. Rule 144(k) provides that a person who is not an "affiliate" of the issuer at any time during the three months preceding a sale and who has beneficially owned shares for at least two years is entitled to sell those shares at any time without compliance with the public information, volume limitation, manner of sale and notice provisions of Rule 144.

As of March 31, 1999, options to purchase 4,218,839 shares of common stock were outstanding under the 1998 Stock Option/Stock Issuance Plan. We intend to file as soon as practicable following completion of this offering a registration statement on Form S-8 under the Securities Act covering shares of common stock reserved for issuance under the 1999 Stock Incentive Plan. Based on the number of options expected to be outstanding upon completion of this offering and shares reserved for issuance under the 1999 Stock Incentive Plan, the S-8 registration statement would cover shares. See "Executive Compensation and Other Information--Employee Benefit Plans". The S-8 registration statement will become effective immediately upon filing, whereupon, subject to the satisfaction of applicable exercisability periods, Rule 144 volume limitations applicable to affiliates and, in certain cases, the agreements with the underwriters referred to above, shares of Common Stock to be issued upon exercise of outstanding options granted pursuant to the 1999 Stock Incentive Plan (to the extent that such shares were held by affiliates) will be available for immediate resale in the open market.

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UNDERWRITING

The underwriters of this offering named below, for whom Bear, Stearns & Co.

Inc., Lehman Brothers Inc., and Thomas Weisel Partners LLC are acting as representatives, have severally agreed with Digital Island, subject to the terms and conditions of the Underwriting Agreement (the form of which has been filed as an exhibit to the Registration Statement on Form S-1 of which this prospectus is a part), to purchase from Digital Island the aggregate number of shares of common stock set forth opposite their respective names below:

<TABLE>
<CAPTION>

Underwriter	Number of Shares
<S>	<C>
Bear, Stearns & Co. Inc.	
Lehman Brothers Inc.	
Thomas Weisel Partners LLC.....	
Total.....	

</TABLE>

The nature of the respective obligations of the underwriters is such that all of the shares of common stock (other than shares of common stock covered by the over-allotment option described below) must be purchased if any are purchased. Those obligations are subject, however, to various conditions, including the approval of certain matters by counsel. Digital Island has agreed to indemnify the underwriters against certain liabilities, including liabilities under the Securities Act, and, where such indemnification is unavailable, to contribute to payments that the underwriters may be required to make in respect of such liabilities.

The Company has been advised that the underwriters propose to offer the shares of common stock directly to the public initially at the public offering price set forth on the cover page of this Prospectus and to certain selected dealers at such price less a concession not to exceed $ per share, that the underwriters may allow, and such selected dealers may reallow, a concession to certain other dealers not to exceed $ per share and that after the commencement of this offering, the public offering price and the concessions may be changed.

Digital Island has granted to the underwriters an option to purchase in the aggregate up to additional shares of common stock to be sold in this offering solely to cover over-allotments, if any. The option may be exercised in whole or in part at any time within 30 days after the date of this prospectus. To the extent the option is exercised, the underwriters will be severally committed, subject to certain conditions, including the approval of certain matters by counsel, to purchase the additional shares of common stock in proportion to their respective purchase commitments as indicated in the preceding table.

The underwriters have reserved for sale at the initial public offering price up to 5% of the number of shares of common stock offered hereby for sale to certain directors, officers, other employees, business affiliates and related persons of Digital Island who have expressed an interest in purchasing shares. The number of shares available for sale to the general public will be reduced to the extent any reserved shares are purchased. Any reserved shares not so purchased will be offered by the underwriters on the same basis as the other shares offered hereby.

Digital Island and our executive officers, directors and the majority of our current stockholders have agreed that, subject to certain limited exceptions, for a period of 180 days after the date of this prospectus, without the prior written consent of Bear, Stearns & Co. Inc., they will not, directly or indirectly, issue, sell, offer or agree to sell or otherwise dispose of any shares of common stock (or securities convertible into, exchangeable for or evidencing the right to purchase shares of common stock).

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Prior to this offering, there has been no public market for the common stock. Consequently, the initial public offering price will be determined through negotiations among Digital Island and the representatives of the underwriters. Among the factors considered in making such determination were Digital Island's financial and operating history and condition, market valuations of other companies engaged in activities similar to ours, our prospects and prospects for the industry in which we do business in general, the management of Digital Island, prevailing equity market conditions and the demand for securities considered comparable to those of Digital Island.

In order to facilitate this offering, certain persons participating in this offering may engage in transactions that stabilize, maintain or otherwise affect the price of the common stock during and after this offering. Specifically, the underwriters may over-allot or otherwise create a short position in the common stock for their own account by selling more shares of common stock, than have been sold to them by Digital Island. The underwriters may elect to cover any such short position by purchasing shares of common stock in the open market or by exercising the over-allotment option granted to the underwriters. In addition, the underwriters may stabilize or maintain the price of the common stock by bidding for or purchasing shares of common stock in the open market and may impose penalty bids, under which selling concessions allowed to syndicate members or other broker-dealers participating in this offering are reclaimed if shares of common stock previously distributed in this offering are repurchased in connection with stabilization transactions or otherwise. The effect of these transactions may be to stabilize or maintain the market price of the common stock at a level above that which might otherwise prevail in the open market. The imposition of a penalty bid may also affect the price of the common stock to the extent that it discourages resales thereof. No

representation is made as to the magnitude or effect of any such stabilization or other transactions. Such transactions may be effected on the Nasdaq National Market or otherwise and, if commenced, may be discontinued at any time.

Thomas Weisel Partners LLC, one of the representatives of the underwriters, was organized and registered as a broker-dealer in December 1998. Since December 1998, Thomas Weisel Partners LLC has co-managed public offerings of equity securities and has acted as an underwriter in an additional public offerings of equity securities. Thomas Weisel Partners LLC does not have any material relationship with us or any of our officers, directors or controlling persons, except with respect to its contractual relationship with us pursuant to the underwriting agreement entered into in connection with this offering.

LEGAL MATTERS

The validity of the issuance of the common stock offered in this offering will be passed upon for us by Brobeck, Phleger & Harrison LLP, Palo Alto, California. Certain legal matters in connection with this offering will be passed upon for the underwriters by Skadden, Arps, Slate, Meagher & Flom LLP, Palo Alto, California.

EXPERTS

The Financial Statements of Digital Island as of September 30, 1998 and 1997 and for each of the years in the three-year period then ended included in this prospectus have been audited by PricewaterhouseCoopers LLP, independent auditors, as stated in their report appearing herein.

ADDITIONAL INFORMATION

Digital Island has filed with the Securities and Exchange Commission, Washington, D.C. 20549, a Registration Statement on Form S-1 under the Securities Act with respect to the common stock offered in this offering. This prospectus omits certain information set forth in the Registration Statement and the exhibits and schedules thereto. For further information with respect to Digital Island and the common stock offered in this offering, reference is made to such Registration Statement, exhibits and schedules. Statements contained in this prospectus as to the contents of any contract or other document referred to are not necessarily complete, and in each instance reference is made to the copy of such contract or other document filed as an exhibit to the Registration Statement, each such statement being qualified in all respects by such reference. After consummation of this offering we will be subject to the informational requirements of the Securities Exchange Act of 1934, as amended, and in accordance therewith, will be required to file annual and quarterly reports, proxy statements and other information with the Commission. The

Registration Statement, including the exhibits and schedules filed therewith, as well as such reports and other information filed by us may be inspected without charge at the public reference facilities maintained by the Securities and Exchange Commission at Room 1024, 450 Fifth Street, N.W., Washington, D.C. 20549 and at the regional offices of the Securities and Exchange Commission located at Seven World Trade Center, Suite 1300, New York, New York 10048 and Citicorp Center, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661. Copies of such materials may be obtained from the Public Reference Section of the Securities and Exchange Commission, Room 1024, 450 Fifth Street, N.W., Washington, D.C. 20549 at prescribed rates and from the Commission's Internet Web site at http://www.sec.gov.

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DIGITAL ISLAND, INC.

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REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and Stockholders of
Digital Island, Inc.:

In our opinion, the accompanying balance sheets and the related statements of operations, stockholders' equity and cash flows present fairly, in all material respects, the financial position of Digital Island, Inc. (the Company) at September 30, 1998 and 1997, and the results of its operations and its cash flows for each of the three years in the period ended September 30, 1998, in conformity with generally accepted accounting principles. These financial statements are the responsibility of the Company's management; our

responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

/s/ PricewaterhouseCoopers LLP

San Francisco, California
February 19, 1999

The foregoing report is in the form that will be signed upon the completion of the reincorporation of the Company in Delaware and the related exchange of common and preferred shares as described in Note 16 to the Consolidated Financial Statements.

San Francisco, California
April 23, 1999

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DIGITAL ISLAND, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

<TABLE>
<CAPTION>

	September 30,		March 31,	
			1999	
	1997	1998	1999	pro forma
			(unaudited)	(unaudited)
<S>	<C>	<C>	<C>	<C>
ASSETS				
Current assets:				
Cash and cash equivalents	$4,583,771	$ 5,710,937	$ 29,750,924	$ 29,760,424
Investments	1,982,664	10,122,631	20,915,423	
Accounts receivable, net of allowance of $0, $55,000, and $168,655 respectively	73,558	662,491	2,707,374	

Restricted cash.....	383,862	263,082	263,082	
Loan receivable.....	--	531,553	--	
Deferred offering costs.....	--	132,119	--	
Prepaid expenses and other.....	53,539	151,819	1,364,409	
Total current assets....	7,077,394	17,574,632	55,001,212	55,010,712
Property and equipment, net.....	2,109,485	4,937,717	7,039,207	
Other assets.....	36,007	104,455	318,948	
Total assets.....	$9,222,886	$ 22,616,804	$ 62,359,367	$ 62,368,867
LIABILITIES AND SHAREHOLDERS' EQUITY				
Current liabilities:				
Bank borrowings.....	$ 211,393	$ 800,579	$ 800,579	
Capital lease obligations.....	--	756,091	1,019,000	
Accounts payable.....	1,922,101	2,407,828	4,774,686	
Accrued liabilities.....	322,132	716,133	3,943,669	
Deferred revenue.....	8,742	11,000	453,395	
Total current liabilities.....	2,464,368	4,691,631	10,991,329	
Bank borrowings, less current portion.....	493,361	884,282	599,192	
Capital lease obligations, less current portion.....	--	1,550,648	1,619,730	
Total liabilities.....	2,957,729	7,126,561	13,210,251	
Commitments (Note 8).				
Stockholders' equity:				
Series A through E convertible preferred stock, $0.001 par value:				
Authorized: 7,000,000 shares in 1997, 14,000,000 shares in 1998 and 30,000,000 shares at March 31, 1999 (unaudited); issued and outstanding: 7,000,000 shares in				

1997, 13,305,657 shares in 1998, and 25,070,363 shares at March 31, 1999 (unaudited); (liquidation value: $86,894,973 at March 31, 1999); pro forma-- no shares authorized, issued, and outstanding.....	7,000	13,305	25,070	$ --
Common stock, $0.001 par value: Authorized: 13,000,000 shares in 1997, 30,000,000 shares in 1998, and 40,000,000 shares at March 31, 1999 (unaudited); issued and outstanding: 2,215,875 shares in 1997, 2,519,835 shares in 1998 and 2,622,225 shares at March 31,1999 (unaudited); pro forma--70,000,000 shares authorized and 27,965,736 shares issued and outstanding.....	2,216	2,520	2,622	27,787
Additional paid-in capital.....	11,586,366	37,192,110	90,168,185	90,206,692
Deferred compensation...	--	--	(4,969,246)	(4,969,246)
Shareholder note receivable.....	--	(109,800)	(109,800)	(109,800)
Common stock warrants...	29,102	29,102	29,102	--
Accumulated deficit.....	(5,359,527)	(21,636,994)	(35,996,817)	(35,996,817)
Total stockholders' equity.....	6,265,157	15,490,243	49,149,116	49,158,616
Total liabilities and stockholders' equity..	$9,222,886	$ 22,616,804	$ 62,359,367	$ 62,368,867

</TABLE>

The accompanying notes are an integral part of these consolidated financial statements

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DIGITAL ISLAND, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

<TABLE>
<CAPTION>

	Years Ended September 30,			Six Months Ended March 31,	
	1996	1997	1998	1998	1999
				(unaudited)	(unaudited)
<S>	<C>	<C>	<C>	<C>	<C>
Revenue	$ --	$ 218,186	$ 2,342,759	$ 691,183	$ 3,795,487
Costs and expenses:					
Cost of revenue	--	2,508,351	9,038,678	4,025,661	7,749,903
Sales and marketing	--	1,205,448	4,846,722	1,786,816	5,170,560
Product development	--	378,241	1,693,962	571,030	2,010,387
General and administrative	25,669	1,501,659	3,392,135	1,163,693	2,962,877
Stock compensation expense	--	--	--	--	516,264
Total costs and expenses	25,669	5,593,699	18,971,497	7,547,200	18,409,991
Loss from operations	(25,669)	(5,375,513)	(16,628,738)	(6,856,017)	(14,614,504)
Interest income (expense), net	(578)	87,349	353,340	64,000	256,572
Loss before income taxes	(26,247)	(5,288,164)	(16,275,398)	(6,792,017)	(14,357,932)
Provision for income taxes	800	800	2,069	1,269	1,891
Net loss	$(27,047)	$(5,288,964)	$(16,277,467)	$(6,793,286)	$(14,359,823)
Basic and diluted net loss per share	$ (0.10)	$ (3.53)	$ (7.28)	$ (3.07)	$ (6.07)
Weighted average shares outstanding used in per share calculation	275,000	1,497,711	2,236,452	2,215,875	2,366,951
Pro forma basic and					

diluted net loss per share.....	$ (1.35)	$ (0.78)
Weighted average shares outstanding used in pro forma per share calculation.....	12,042,539	18,353,258

</TABLE>

The accompanying notes are an integral part of these consolidated financial statements

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DIGITAL ISLAND, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

<TABLE>
<CAPTION>

	Convertible Preferred Stock		Common Stock		Additional Paid-in	Deferred	Stockholder Note	Common Stock	Accumulated
	Shares	Amount	Shares	Amount	Capital	Compensation	Receivable	Warrants	Deficit
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Balances, September 30, 1995.....	2,000,000	$ 2,000	275,000	$ 275	$ 129,025	$ --	$ --	$ --	$ (43,516)
Warrants issued in connection with convertible note	--	--	--	--	--	--	--	22,975	--
Net loss.....	--	--	--	--	--	--	--	--	(27,047)
Balances, September 30, 1996.....	2,000,000	2,000	275,000	275	129,025	--	--	22,975	(70,563)
Common stock issued for professional services.....	--	--	70,875	71	28,279	--	--	--	--
Conversion of preferred stock into common stock.....	(2,000,000)	(2,000)	2,000,000	2,000	--	--	--	--	--

Repurchase of common stock....	--	--	(130,000)	(130)	(1,170)	--	--	--	--	
Series A preferred stock issued for cash, net of issuance costs of $16,569.....	3,341,546	3,342	--	--	3,321,635	--	--	--	--	
Series B preferred stock issued for cash, net of issuance costs of $46,199.....	3,000,000	3,000	--	--	7,450,801	--	--	--	--	
Warrants issued in connection with convertible note	--	--	--	--	--	--	--	6,127	--	
Conversion of notes payable into Series A preferred stock.....	658,454	658	--	--	657,796	--	--	--	--	
Net loss.....	--	--	--	--	--	--	--	--	(5,288,964)	
Balances, September 30, 1997.....	7,000,000	7,000	2,215,875	2,216	11,586,366	--	--	29,102	(5,359,527)	
Series C preferred stock issued for cash, net of issuance costs of $34,011.....	4,283,181	4,283	--	--	14,738,680	--	--	--	--	
Series D preferred stock issued for cash, net of issuance costs of $33,293.....	2,022,476	2,022	--	--	10,582,684	--	--	--	--	
Issuance of shareholder note in exchange for common stock....	--	--	183,000	183	109,617	--	(109,800)	--	--	
Common stock issued for professional services.....	--	--	6,000	6	18,894	--	--	--	--	
Common stock										

issued for cash upon exercise of options.....	--	--	114,960	115	155,869	--	--	--	--		
Net loss.....	--	--	--	--	--	--	--	--	(16,277,467)		
Balances, September 30, 1998.....	13,305,657	13,305	2,519,835	2,520	37,192,110	--	(109,800)	29,102	(21,636,994)		
Series E preferred stock issued for cash, net of issuance costs of $2,538,580.....	11,764,706	11,765	--	--	47,449,655	--	--	--	--		
Common stock issued for cash upon exercise of options.....	--	--	102,390	102	40,910	--	--	--	--		
Deferred compensation in connection with issuance of stock options...	--	--	--	--	5,485,510	(5,485,510)	--	--	--		
Amortization of deferred compensation....	--	--	--	--	--	516,264	--	--	--		
Net loss.....	--	--	--	--			--	--	(14,359,823)		
Balances, March 31, 1999 (unaudited).....	25,070,363	$25,070	2,622,225	$2,622	$90,168,185	$(4,969,246)	$(109,800)	$29,102	$(35,996,817)		

<CAPTION>

	Total Stockholders' Equity
<S>	<C>
Balances, September 30, 1995.....	$ 87,784
Warrants issued in connection with convertible note	22,975
Net loss.....	(27,047)

Balances, September 30, 1996.....	83,712
Common stock issued for professional services.....	28,350
Conversion of preferred stock into common stock.....	--
Repurchase of common stock....	(1,300)
Series A preferred stock issued for cash, net of issuance costs of $16,569.....	3,324,977
Series B preferred stock issued for cash, net of issuance costs of $46,199.....	7,453,801
Warrants issued in connection with convertible note	6,127
Conversion of notes payable into Series A preferred stock.....	658,454
Net loss.....	(5,288,964)
Balances, September 30, 1997.....	6,265,157
Series C preferred stock issued for cash, net of issuance costs of $34,011.....	14,742,963
Series D preferred stock issued for cash,	

net of issuance costs of $33,293..... 10,584,706
Issuance of shareholder note in exchange for common stock.... --
Common stock issued for professional services..... 18,900
Common stock issued for cash upon exercise of options..... 155,984
Net loss..... (16,277,467)

Balances, September 30, 1998..... 15,490,243
Series E preferred stock issued for cash, net of issuance costs of $2,538,580..... 47,461,420
Common stock issued for cash upon exercise of options..... 41,012
Deferred compensation in connection with issuance of stock options... --
Amortization of deferred compensation.... 516,264
Net loss..... (14,359,823)

Balances, March 31, 1999 (unaudited)..... $49,149,116
==========
</TABLE>

The accompanying notes are an integral part of these consolidated financial statements

<PAGE>

DIGITAL ISLAND, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

<TABLE>
<CAPTION>

	Years Ended September 30,			For the Six Months Ended March 31,	
	1996	1997	1998	1998	1999
				(unaudited)	(unaudited)
<S>	<C>	<C>	<C>	<C>	<C>
Cash flows from operating activities:					
Net loss.....	$(27,047)	$(5,288,964)	$(16,277,467)	$(6,793,286)	$(14,359,823)
Adjustments to reconcile net loss to net cash used in operating activities:					
Depreciation and amortization.....	--	158,247	547,376	285,283	435,275
Amortization of capital lease obligations.....	--	--	263,433	7,705	488,402
Stock compensation expense.....	--	--	--	--	516,264
Non-cash revenue in connection with barter agreement.....	--	(131,912)	--	--	--
Debt discount in conjunction with convertible notes.....	--	29,102	--	--	--
Amortization of discounts on investments.....	--	(23,908)	(227,280)	(30,249)	(170,668)
Professional services in exchange for common stock.....	--	28,350	18,900	--	--
Loss on disposal of property and equipment.....	--	--	1,373	--	--
Change in operating assets and liabilities:					
Accounts receivable...	--	(73,558)	(588,933)	(239,983)	(2,044,883)

Prepaids expenses and other.....	1,949	27,137	(98,280)	(238,586)	(1,212,590)
Deferred offering costs.....	--	--	(132,119)	--	132,119
Accounts payable.....	14,372	1,901,036	485,727	(136,994)	2,366,858
Accrued liabilities...	--	322,132	394,001	41,378	3,227,536
Deferred revenue.....	--	8,742	2,258	(8,742)	442,395
Other assets.....	--	(36,007)	(68,448)	24,582	(216,093)
Net cash used in operating activities.....	(10,726)	(3,079,603)	(15,679,459)	(7,088,892)	(10,395,208)
Cash flows from investing activities:					
Purchases of property and equipment.....	(2,327)	(2,128,376)	(1,234,005)	(160,417)	(2,283,814)
Proceeds from maturities of short-term investments.....	--	1,000,000	5,600,000	2,000,000	12,200,000
Decrease (increase) in restricted cash.....	--	(383,862)	120,780	61,983	--
Purchases of short-term investments.....	--	(2,958,756)	(13,512,687)	(4,684,688)	(22,822,124)
Net cash used in investing activities.....	(2,327)	(4,470,994)	(9,025,912)	(2,783,122)	(12,905,938)
Cash flows from financing activities:					
Proceeds from issuance of preferred stock, net.....	--	10,778,778	25,327,669	11,000,100	47,461,420
Proceeds from issuance of common stock.....	--	--	155,984	--	41,012
Proceeds from issuance of notes payable.....	350,000	308,454	--	--	--
Proceeds from bank borrowings.....	--	704,754	647,378	527,417	531,553
Repayments of bank borrowings.....	--	--	(198,824)	(42,712)	(285,090)
Repayments of capital lease obligations.....	--	--	(99,670)	(16,015)	(407,762)
Repurchase of common stock.....	--	(1,300)	--	--	--
Net cash provided by financing					

activities.....	350,000	11,790,686	25,832,537	11,468,790	47,341,133
Net increase in cash and cash equivalents.....	336,947	4,240,089	1,127,166	1,596,776	24,039,987
Cash and cash equivalents, beginning of period.....	6,735	343,682	4,583,771	4,583,771	5,710,937
Cash and cash equivalents, end of period.....	$343,682	$ 4,583,771	$ 5,710,937	$ 6,180,547	$ 29,750,924
Supplemental disclosures of cash flow information:					
Cash paid for interest.....	$ 1,814	$ 27,219	$ 128,850	$ 45,213	$ 167,604
Cash paid for income taxes.....	$ --	$ 1,600	$ 2,069	$ 1,269	$ 1,891
Supplemental schedule of noncash investing and financing activities:					
Common stock issued for professional services..	$ --	$ 28,350	$ 18,900	$ --	$ --
Receivable on bank borrowings.....	$ --	$ --	$ 531,553	$ --	$ --
Notes payable converted into preferred stock...	$ --	$ 658,454	$ --	$ --	$ --
Conversion of preferred stock into common stock.....	$ --	$ 21,300	$ --	$ --	$ --
Note receivable issued in exchange for common stock.....	$ --	$ --	$ 109,800	$ 109,800	$ --
Capital lease obligations for equipment.....	$ --	$ --	$ 2,406,409	$ 251,443	$ 739,753

</TABLE>

The accompanying notes are an integral part of these consolidated financial statements

DIGITAL ISLAND, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Information as of and relating to the six months ended March 31, 1999 and 1998 is unaudited)

1. The Company:

Digital Island, Inc. (the Company) offers a global internet protocol applications network designed to deploy business-critical applications worldwide. The Company also offers services such as network management and application services to customers deployed on its network. The Company was incorporated in February 1994 under the name Smartvision, Inc. Together, these services provide a product offering that enables multinational corporations to reach end users in worldwide local markets.

2. Summary of Significant Accounting Policies:

Initial Public Offering and Unaudited Pro Forma Balance Sheet (unaudited)

In April 1999, the Board of Directors of the Company authorized the filing of a registration statement with the Securities and Exchange Commission (the SEC) that would permit the Company to sell shares of the Company's common stock in connection with a proposed initial public offering (IPO). If the offering is consummated under the terms presently anticipated, all the outstanding shares of the Company's convertible preferred stock will automatically convert into shares of common stock upon the closing of the proposed IPO and the exercise of outstanding warrants to purchase 95,000 shares of common stock at an exercise price of $0.10 per share. These warrants expire upon an IPO. The conversion of the convertible preferred stock and the exercise of the warrants has been reflected in the accompanying unaudited pro forma balance sheet as if it had occurred on March 31, 1999.

Principles of Consolidation:

The accompanying interim consolidated financial statements of the Company include the accounts of Digital Island, Inc. and its wholly-owned subsidiaries, Digital Island B.V.i.o. and Digital Island Ltd., which were established in December 1998 and March 1999, respectively. All significant intercompany accounts and transactions are eliminated in consolidation.

Use of Estimates:

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

Unaudited Interim Financial Information:

The accompanying interim consolidated financial statements as of and for the six months ended March 31, 1998 and 1999, together with the related notes are unaudited but include all adjustments, consisting of only normal recurring adjustments, which the Company considers necessary to present fairly, in all material respects, the consolidated financial position, and consolidated results of operations and cash flows for the six month periods ended March 31, 1998 and 1999. Results for the six months ended March 31, 1999 are not necessarily indicative of results for the entire year.

Revenue Recognition:

Revenues are comprised primarily of global connectivity fees, bandwidth charges, equipment co-location and storage fees, and one-time fees for installation. Bandwidth charges are billed and recognized monthly based on customer usage. All other revenues are based on flat-rate monthly charges. Installation fees are typically recognized at the time that installation occurs. To date, such revenues have not significantly exceeded the direct costs of installation.

Computation of Historical Net Loss Per Share and Pro Forma Net Loss Per Share:

The Company has adopted Statement of Financial Accounting Standards No. 128, (SFAS 128) "Earnings Per Share." In accordance with SFAS 128, basic earnings per share is computed using the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of common and dilutive common equivalent shares outstanding during the period, using either the as if converted method for convertible preferred stock or the treasury stock method for options and

warrants. Pursuant to SEC Staff Accounting Bulletin No. 98, common stock and convertible preferred stock issued for nominal consideration, prior to the anticipated effective date of an IPO, are included in the calculation of basic and diluted net loss per share, as if they were outstanding for all periods presented. To date, the Company has not had any issuances for nominal consideration.

Diluted net loss per share for the years ended September 30, 1996, 1997 and 1998, and the six months ended March 31, 1998 and 1999 does not include the effect of 0, 0, 639, 0 and 0 stock options, respectively, and 0, 67,420, 71,250, 71,250, and 71,250 common stock warrants, respectively, or 2,000,000, 7,000,000, 13,305,657, 11,283,181, and 25,070,363 shares of convertible preferred stock on an "as if converted" basis, respectively, as the effect of their inclusion is antidilutive during each period.

Pro forma basic and diluted net loss per share is presented to reflect per share data assuming the conversion of all outstanding shares of convertible preferred stock into common stock as if the conversion had taken place at the beginning of fiscal 1998 or at the date of issuance, if later. This data is unaudited.

Cash and Cash Equivalents:

Cash and cash equivalents are stated at cost, which approximates fair value. The Company includes in cash equivalents all highly liquid investments which mature within three months of their purchase date.

Fair Value of Financial Instruments:

The carrying amounts of certain of the Company's financial instruments including cash and cash equivalents, accounts receivable, notes payable, accounts payable and accrued liabilities approximate fair value due to their short maturities.

Investments:

At September 30, 1997 and 1998, and March 31, 1999 the Company's investments consisted of commercial paper. Remaining maturities at the time of purchase are generally less than one year.

Investments are accounted for in accordance with Statement of Financial Accounting Standards No. 115 (SFAS 115) "Accounting for Certain Investments in Debt and Equity Securities." This statement requires that securities be classified as "held to maturity," "available for sale" or "trading," and the securities in each

classification be accounted for at either amortized cost or fair market value, depending upon their classification. The Company has the intent and the ability to hold investments until maturity. Therefore, all such investments are classified as held to maturity investments and carried at amortized cost in the accompanying consolidated financial statements.

The Company's investments consist of the following:

<TABLE>
<CAPTION>

	September 30, 1997		September 30, 1998		March 31, 1999 (unaudited)	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Commercial paper.....	$1,982,664	$1,982,000	$10,122,631	$10,124,557	$20,915,423	$20,798,002

</TABLE>

Restricted Cash:

Restricted cash consists of irrevocable standby letters of credit issued by the Company's banks. Funds are generally held in certificates of deposit at the Company's bank, and have been established in favor of a third party beneficiary. The funds are released to the beneficiary in the event that the Company fails to comply with certain specified contractual obligations. Provided the Company meets these contractual obligations, the letter of credit is discharged and the Company is no longer restricted from use of the cash.

Property and Equipment:

Property and equipment are recorded at cost and depreciated using the straight-line method over their useful lives. Equipment recorded under capital leases is amortized using the straight-line method over the shorter of the respective lease term or the estimated useful life of the asset. Network and communications equipment is depreciated over five years, computer equipment and software is depreciated over three years, and furniture and fixtures are depreciated over seven years. Maintenance and repairs are charged to expense as incurred, and improvements and betterments are capitalized. When assets are retired or otherwise disposed of, the cost and accumulated depreciation are removed from the accounts and any resulting gain or loss is reflected in

operations in the period realized.

Long-lived Assets:

The Company evaluates the recoverability of its long-lived assets in accordance with Statement of Financial Accounting Standards No. 121, (SFAS 121) "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of." SFAS 121 requires recognition of impairment of long-lived assets in the event the net book value of such assets exceeds the future undiscounted cash flows attributable to such assets. No such impairments have been identified to date. The Company assesses the impairment of long-lived assets when events or changes in circumstances indicate that the carrying value of an asset may not be recoverable.

Income Taxes:

The Company accounts for income taxes in accordance with Statement of Financial Accounting Standards No. 109, (SFAS 109) "Accounting for Income Taxes." Under SFAS 109, deferred tax liabilities and assets are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. Valuation allowances

are established when necessary to reduce deferred tax assets to the amounts expected to be realized. Income tax expense represents the tax payable for the current period and the change during the period in the deferred tax assets and liabilities.

Software Development Costs:

Software development costs have been accounted for in accordance with Statement of Financial Accounting Standards No. 86, (SFAS 86) "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed." Under the standard, capitalization of software development costs begins upon the establishment of technological feasibility. To date, all such amounts have been insignificant, and accordingly, the Company has charged all such costs to research and development expenses.

Deferred Revenues:

Deferred revenues primarily represent advanced billings to customers, or prepayments by customers prior to completion of installation or prior to provision of contractual bandwidth usage.

Concentration of Credit Risk:

Financial instruments which potentially subject the Company to concentrations of credit risk consist primarily of temporary cash investments and accounts receivable. The Company places its temporary investments with one major financial institution.

The Company performs ongoing credit evaluations, does not require collateral, and maintains reserves for potential credit losses on customer accounts when deemed necessary. For the year ended September 30, 1997, three customers accounted for approximately 56%, 20%, and 10%, respectively, of all revenue generated by the Company, and 0%, 57%, and 31% of accounts receivable at September 30, 1997, respectively. For the year ended September 30, 1998, the same customers accounted for approximately 13%, 20%, and 4%, respectively, of all revenue generated by the Company, and 19%, 5%, and 0% of accounts receivable at September 30, 1998, respectively. In addition, a fourth customer accounted for 12% of all revenues generated by the Company for the year ended September 30, 1998, and 14% of accounts receivable at September 30, 1998. For the six months ended March 31, 1998, the same four customers accounted for approximately 15%, 31%, 9%, and 16%, respectively, of all revenues generated by the Company. For the six months ended March 31, 1999, the same customers accounted for 5%, 16%, 1%, and 7%, respectively, of all revenues generated by the Company, and 3%, 35%, 0%, and 6%, respectively, of accounts receivable at March 31, 1999.

Risks and Uncertainties:

Factors that may materially and adversely affect the Company's future operating results include: demand for and market acceptance of the Company's products and services; introductions of products and services or enhancements by the Company and its competitors; competitive factors that affect our pricing; capacity utilization of the Digital Island Global IP applications network; reliable continuity of service and network availability; the ability and cost of bandwidth and our ability to increase bandwidth as necessary; the timing of customer installations; the mix of products and services sold by the Company; customer retention; the timing and success of marketing efforts and product and service introductions by the Company; the timing and magnitude of capital expenditures, including costs relating to the expansion of operations; the timely expansion of its network infrastructure; fluctuations in bandwidth used by customers; the retention of key personnel; conditions specific to the Internet industry and other general economic factors; and new government legislation and regulation.

<PAGE>

DIGITAL ISLAND, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

(Information as of and relating to the six months ended March 31, 1999 and 1998 is unaudited)

Comprehensive Income:

The Company has adopted the accounting treatment prescribed by Financial Accounting Statement No. 130, "Comprehensive Income." The adoption of this statement had no impact on the Company's financial statements for the periods presented.

Recently Issued Accounting Pronouncements:

On March 4, 1998, the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants (AICPA) issued Statement of Position No. 98-1 (SOP 98-1), "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." SOP 98-1 requires computer software costs related to internal software that are incurred in the preliminary project stage should be expensed as incurred. Once the capitalization criteria of SOP 98-1 have been met, external direct costs of materials and services consumed in developing or obtaining internal-use computer software; payroll and payroll-related costs for employees who are directly associated with and who devote time to the internal-use computer software project (to the extent of the time spent directly on the project); and interest costs incurred when developing computer software for internal use should be capitalized. SOP 98-1 is effective for financial statements for fiscal years beginning after December 15, 1998. Accordingly, the Company will adopt SOP 98-1 in its consolidated financial statements for the year ending September 30, 2000.

On April 3, 1998, the Accounting Standards Executive Committee of the AICPA issued Statement of Position No. 98-5 (SOP 98-5), "Reporting on the Costs of Start-Up Activities," which provides guidance on the financial reporting of start-up costs and organization costs. SOP 98-5 requires costs of start-up activities and organization costs to be expensed as incurred. SOP 98-5 is effective for financial statements for fiscal years beginning after December 15, 1998. As the Company has not capitalized such costs, the adoption of SOP 98-5 is not expected to have an impact on the consolidated financial statements of the Company.

In June 1998, the FASB issued Statement of Financial Accounting Standards No. 133 (SFAS 133), "Accounting for Derivative Instruments and Hedging Activities." SFAS 133 establishes accounting and reporting standards for derivative instruments and for hedging activities. SFAS 133 is effective for

fiscal years beginning after June 15, 1999. The Company does not believe the adoption of SFAS 133 will have a material effect on the Company's consolidated results of operations or financial condition.

3. Property and Equipment:

Property and equipment consists of the following:

<TABLE>
<CAPTION>

	September 30,		March 31,
	1997	1998	1999
			(unaudited)
<S>	<C>	<C>	<C>
Network equipment	$1,503,352	$2,299,279	$4,129,370
Communications equipment	167,571	194,106	197,378
Computer equipment and software	301,980	514,651	816,119
Furniture, fixtures, and leasehold improvements	294,829	491,388	640,371
Equipment and fixtures under capital leases	--	2,406,409	3,146,162
	2,267,732	5,905,833	8,929,400
Less accumulated depreciation and amortization	158,247	968,116	1,890,193
Total property and equipment, net	$2,109,485	$4,937,717	$7,039,207

</TABLE>

<PAGE>

4. Income Taxes:

For the years ended September 30, 1996, 1997, and 1998, the provision for income taxes consists of state taxes.

The primary components of the net deferred tax asset are as follows:

<TABLE>
<CAPTION>

	September 30,	
	1997	1998
<S>	<C>	<C>
Net operating loss carryforwards, federal and state	$2,140,000	$8,440,000
Accrued employee benefits	41,000	61,000
Sales tax	11,000	1,000
Accounts receivable allowance	--	22,000
Property and equipment	(49,000)	(358,000)
	2,143,000	8,166,000
Less valuation allowance	(2,143,000)	(8,166,000)
	$ --	$ --

</TABLE>

Due to the uncertainty surrounding the realization of the favorable tax attributes in future tax returns, the Company has placed a valuation allowance against its otherwise recognizable net deferred tax assets. The valuation allowance increased by $2,121,000 and $6,023,000 for the years ended September 30, 1997 and 1998, respectively. The effective income tax rate differs from the statutory federal income tax rate primarily due to the inability to recognize the benefit of net operating losses.

At September 30, 1998, the Company had NOL carryforwards of approximately $21,100,000 and $21,097,000 for federal and state income tax purposes, respectively. These carryforwards expire beginning 2009 and 2002, respectively.

Pursuant to the provisions of Section 382 of the Internal Revenue Code, utilization of the NOLs are subject to annual limitations through 2013 due to a greater than 50% change in the ownership of the Company which occurred during fiscal 1998.

5. Bank Borrowings:

Bank borrowings consist of:

<TABLE>
<CAPTION>

	September 30,		
	1997	1998	March 31, 1999
			(unaudited)
<S>	<C>	<C>	<C>

Line of credit	$ --	$ 230,400	$ 230,400
Revolving credit facility	704,754	579,150	451,013
Equipment term facility	--	875,311	718,358
	704,754	1,684,861	1,399,771
Current maturities	(211,393)	(800,579)	(800,579)
Long-term bank borrowings	$ 493,361	$ 884,282	$ 599,192

</TABLE>

<PAGE>

On November 21, 1996, the Company entered into a revolving credit agreement (the Revolving Agreement) with a commercial lender. The aggregate credit under the Revolving Agreement was originally $250,000, and was increased to $750,000 on April 18, 1997. Interest under the Revolving Agreement is 0.75% over the "Prime Rate" as announced from time to time by the lender. At both September 30, 1997 and 1998, and March 31, 1999, the effective interest rate was 9.25%, 9.25%, and 8.50%, respectively. The weighted average interest rates for the years ended September 30, 1997 and 1998, and the six months ended March 31, 1999 were 9.24%, 9.25%, and 8.55%, respectively. Under the terms of the Revolving Agreement, advances could be made for the purchase of equipment until October 18, 1997. At that date, the unpaid principal balance of equipment advances plus interest became payable over 36 months in equal installments. Outstanding borrowings under the Revolving Agreement at September 30, 1997 and 1998, and March 31, 1999 were $704,754, $579,150, and $451,013, respectively. All amounts outstanding related to advances for equipment purchases.

On November 19, 1997, the Company entered into a loan agreement (the Loan Agreement) with the same commercial lender associated with the Revolving Agreement. Under the terms of the Loan Agreement, the Company was extended a $5,000,000 line of credit, as well as an equipment loan term facility for $2,500,000. Any borrowings under this line of credit are collateralized by substantially all assets of the Company. Certain of the Loan Agreement's provisions restrict the ability of the Company to declare or pay any dividends while the credit agreement is in effect.

Advances under the line of credit are limited to a percentage of the Company's recurring contract revenues, as defined in the Loan Agreement. The

Loan Agreement contains certain standard covenants. At September 30, 1998 and March 31, 1999, $230,400 and $230,400, respectively, was outstanding under the line of credit. Interest on borrowings are charged at the lender's prime rate plus 0.25%, which was 8.75% and 8.00% at September 30, 1998 and March 31, 1999, respectively. The weighted average interest rate for the year ended September 30, 1998 and the six months ended March 31, 1999, was 8.75% and 8.04%, respectively. Advances under the line of credit can be repaid and reborrowed at any time until the maturity date of May 31, 1999.

Under the terms of the equipment loan term facility, the Company had the ability to borrow up to $1,250,000 for equipment purchases from November 19, 1997 to May 19, 1998 (Equipment Line A), as well as borrow an additional $1,250,000 from February 1, 1998 to September 30, 1998 (Equipment Line B). At September 30, 1998 and March 31, 1999, $223,796 and $181,835, respectively was outstanding related to advances made under Equipment Line A, and $651,515 and $536,523, respectively, was outstanding related to advances made under Equipment Line B. Interest on these borrowings are charged at the lender's prime rate plus 0.75%, which was 9.25% and 8.50% at September 30, 1998 and March 31, 1999, respectively. The weighted average interest rate for the year ended September 30, 1998 and the six months ended March 31, 1999 was 9.25% and 8.55%, respectively. Repayments of advances on Equipment Line A commenced on June 19, 1998, with the unpaid principal balance as of May 19, 1998, plus interest, being repaid in 36 equal monthly installments. Repayments of advances on Equipment Line B commenced on October 19, 1998 in 34 monthly installments of principal and interest.

The Loan Agreement was due to mature on November 19, 1998. On November 18, 1998, the Loan Agreement was modified to extend the maturity date to February 15, 1999. On February 15, 1999 the Loan Agreement was modified again to extend the maturity date to May 31, 1999.

The Company did not comply with certain financial covenants as of September 30, 1997 and at various points during fiscal 1998, and accordingly, received an amendment and waiver dated October 6, 1998 from its lender, which waived covenant violations for periods prior to September 30, 1998 and eliminated one financial covenant with respect to a minimum profitability threshold. Subsequent to September 30, 1998, the Company did not comply with certain financial covenants. The Company obtained waivers for all covenant violations

from October 1, 1998 to January 31, 1999. Through April 22, 1999 the Company has been in compliance with all covenants.

Interest expense for the years ended September 30, 1997 and 1998, and the six months ended March 31, 1998 and 1999 was $35,673, $94,400, $42,602, and $65,738, respectively.

Principal maturities of bank borrowings are as follows:

<TABLE>
<CAPTION>

Year ending September 30,	
<S>	<C>
1999	$ 800,579
2000	570,181
2001	314,101
	$1,684,861

</TABLE>

6. Notes Payable:

Between September 27, 1996 and January 31, 1997, the Company issued three convertible notes totalling $600,000 to a commercial lender. These notes had a simple interest rate of 6%. In March 1997, all three notes plus accrued interest of $8,454 were converted into 608,454 shares of Series A preferred stock.

Prior to October 1, 1996, the Company had issued a $50,000 convertible note to a related party. In March 1997, this note was converted into 50,000 shares of Series A preferred stock.

7. Accrued Liabilities:

Accrued liabilities consist of the following:

<TABLE>
<CAPTION>

	September 30,		March 31,
	1997	1998	1999
			(unaudited)
<S>	<C>	<C>	<C>
Employee compensation	$209,275	$595,975	$1,146,930
Accrued sales tax	38,851	2,346	32,637
Travel and entertainment	47,505	52,000	365,500

Series E preferred stock financing costs.....	--	--	2,200,000
Other accrued liabilities.....	26,501	65,812	198,602
Total.....	$322,132	$716,133	$3,943,669

</TABLE>

8. Commitments:

Leases:

The Company leases office space under noncancelable operating leases expiring through May 2002. Rent expense for the years ended September 30, 1996, 1997, and 1998, and the six months ended March 31, 1998 and 1999 was $0, $136,678, $715,115, $189,617, and $335,646, respectively.

<PAGE>

The Company also leases network equipment under capital leases agreements. These capital leases are governed by master lease agreements with two separate lessors. The total credit extended to the Company under these master lease agreements totalled $3,500,000 and $4,423,169 at September 30, 1998 and March 31, 1999, respectively, of which $2,306,739 and $2,638,730, respectively, had been borrowed and was outstanding.

The Company's future minimum lease payments under noncancelable operating leases having an initial or remaining term of more than one year, and capital leases are as follows:

<TABLE>
<CAPTION>

Year ending September 30,	Operating	Capital
<S>	<C>	<C>
1999.....	$ 649,204	$ 896,061
2000.....	660,380	896,061
2001.....	558,708	751,944
2002.....	257,718	--
Total minimum lease payments.....	$2,126,010	2,544,066

Less amounts representing interest.....	(237,327)
Present value of minimum lease payments.....	2,306,739
Less current portion of capital lease obligations....	(756,091)
Long-term portion of capital lease obligations.....	$1,550,648

</TABLE>

Carrier Line Agreements:

The Company has entered into various bandwidth capacity agreements with domestic and foreign carriers. These agreements are generally cancellable and provide for termination fees if cancelled by the Company prior to expiration.

9. Earnings Per Share:

The following is a reconciliation of the numerator and denominator of basic and diluted earnings per share (EPS):

<TABLE>
<CAPTION>

	Years Ended September 30,			Six Months Ended March 31,	
	1996	1997	1998	1998	1999
				(unaudited)	(unaudited)
<S>	<C>	<C>	<C>	<C>	<C>
Numerator--Basic and Diluted EPS					
Net Loss.....	$(27,047)	$(5,288,964)	$(16,277,467)	$(6,793,286)	$(14,359,823)
Denominator--Basic and Diluted EPS					
Weighted average Common Stock outstanding.....	275,000	1,497,711	2,361,010	2,250,062	2,586,201
Common Stock subject to repurchase.....	--	--	(124,558)	(34,187)	(219,250)
Total weighted average Common Stock outstanding.....	275,000	1,497,711	2,236,452	2,215,875	2,366,951
Basic and diluted loss per share.....	$ (0.10)	$ (3.53)	$ (7.28)	$ (3.07)	$ (6.07)
Pro forma:					

Denominator--Basic and Diluted EPS		
Weighted Average Common Stock.....	2,361,010	2,586,201
Conversion of Preferred Stock.....	9,711,087	15,891,307
Conversion of Warrants.....	95,000	95,000
Common Stock subject to repurchase.....	(124,558)	(219,250)
Total weighted average Common Stock outstanding pro forma.....	12,042,539	18,353,258
Basic and diluted pro forma loss per share...	$ (1.35)	$ (0.78)

</TABLE>

<PAGE>

10. Shareholders' Equity:

Convertible Preferred Stock:

As of March 31, 1999, the Company had five series of preferred stock authorized and outstanding. The holders of the various series of preferred stock generally have the same rights unless specified.

Liquidation Preference:

In the event of any liquidation, dissolution, or winding up of the Company, either voluntary or involuntary and including a sale, merger, or reorganization, the holders of preferred stock retain liquidation preference over common shareholders. If consideration received in the event of liquidation of the Company is in the form of cash and/or publicly traded securities with a fair value of at least $3.00, $7.50, $10.35, $15.75, and $12.75 per share of Series A, Series B, Series C, Series D, and Series E, respectively, then the

consideration paid in such a transaction shall be distributed among the holders of all common and preferred stock on a pro rata basis based on the number of common stock equivalent shares owned by the holder. In the event of a liquidation in which the fair value of the consideration received is less than $3.00, $7.50, $10.35, $15.75, and $12.75 per share of Series A, Series B, Series C, Series D, and Series E, respectively, the holders of Series A, Series B, Series C, Series D, and Series E preferred stock are entitled to a distribution of $1.00, $2.50, $3.45, $5.25, and $4.25 per share, respectively. In the event that the consideration is inadequate to cover the preferential amounts of $1.00, $2.50, $3.45, $5.25, and $4.25 per share of Series A, B, C, D, and E, respectively, then the consideration is distributed rateably to all preferred stockholders. If the consideration received is in excess of these preferential amounts, then the excess is distributed among the holders of all common and preferred stock on a pro rata basis based on the number of common stock equivalent shares owned by the holder.

Voting Rights:

Holders of Series A, Series B, Series C, Series D, and Series E preferred stock are entitled to vote together with holders of common stock. The number of votes equal the number of full shares of common stock into which Series A, Series B, Series C, Series D, and Series E preferred stock could be converted into.

Conversion:

At the option of the holder, preferred shares are convertible at any time into shares of common stock at a ratio of the conversion price divided by the initial purchase price. The conversion price is $1.00 per share for Series A, $2.50 per share for Series B, $3.45 per share for Series C, and $4.25 per share for Series E. Series D shares were originally convertible at a price of $5.25 per share. Pursuant to anti-dilution provisions triggered by the issuance of Series E, Series D shares are now convertible at a price of $4.82 per share. The conversion price of each series of preferred stock is subject to adjustment as described in the Company's Articles of Incorporation. All Series A, Series B, Series C, Series D, and Series E preferred shares will automatically be converted into shares of common stock upon (1) the election of holders of at least two-thirds of the outstanding shares of preferred stock, or (2) upon the closing of an underwritten public offering pursuant to an effective registration statement under the Securities Act of 1933 at an offering price of not less than $7.00 per share (adjusted to reflect stock splits, reverse stock splits, or stock dividends), and $25,000,000 in the aggregate. In the event the Company proposes to undertake a dilutive issuance, holders of preferred stock who do not agree to become participating investors in the dilutive issuance are deemed non-participating investors. Additionally, in the event that shares of preferred stock (New Series) are issued for a consideration per share that is less than the conversion price per share with respect to any previously issued series of preferred stock (Previous Series),

<PAGE>

DIGITAL ISLAND, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

(Information as of and relating to the six months ended March 31, 1999 and 1998 is unaudited)

then the conversion price per share shall be reduced for the Previous Series concurrent with the issuance of the New Series. The Company has reserved 30,000,000 shares of common stock for the conversion of the outstanding shares of preferred stock.

Dividends:

Each fiscal year, holders of preferred stock are entitled to receive, when and if declared by the board of directors, out of any funds legally available, a preferential non-cumulative dividend of $0.07, $0.18, $0.24, $0.37, and $0.2975 per share for Series A, Series B, Series C, Series D, and Series E, respectively. In addition, preferred shareholders are entitled to participate in cash dividends paid to common shareholders in an amount per share as would be payable on the number of shares of common stock into which each share of preferred stock could be converted. As of March 31, 1999 and in accordance with the Loan Agreement, the board of directors had not declared any dividends.

Convertible preferred stock issued and outstanding as of March 31, 1999 was as follows:

<TABLE>
<CAPTION>

Series	Shares Designated	Issued and Outstanding	Liquidation Value
<S>	<C>	<C>	<C>
A.....	4,000,000	4,000,000	$ 4,000,000
B.....	3,000,000	3,000,000	$ 7,500,000
C.....	4,300,000	4,283,181	$14,776,974
D.....	2,700,000	2,022,476	$10,617,999
E.....	11,764,706	11,764,706	$50,000,000
	25,764,706	25,070,363	$86,894,973

</TABLE>

11. Stock Option and Stock Issuance Plan:

In January 1997, the Company established the Stock Option and Incentive Plan

(the 1997 Plan) and reserved up to 1,689,125 shares of common stock issuable upon exercise of options granted to certain employees, directors, and consultants. In May 1998, the Company adopted the 1998 Stock Option/Stock Issuance Plan (the 1998 Plan). The 1998 Plan was designed to serve as the successor to the 1997 Plan. Upon adoption of the 1998 Plan the existing share reserve under the 1997 Plan was transferred to the 1998 Plan, and all outstanding options under the 1997 Plan were incorporated into the 1998 Plan. The Company increased the maximum number of shares issuable to a total of 3,833,284. In November 1998, the Company increased the stock option pool by another 600,000 shares, bringing the total to 4,433,284. This number of shares has been reserved for issuance under the 1998 Plan.

Under the terms of the 1998 Plan, the Company has the ability to grant incentive and nonstatutory stock options, as well as issue vested and unvested shares of the Company's common stock. Exercise prices of stock options are generally not less than 100% and 85% of the fair value of the common stock on the date of grant of incentive stock options and nonstatutory stock options, respectively, and have a term of up to ten years. Options generally vest rateably over a period of up to fifty months after the grant date, subject to accelerated vesting in connection with certain changes in control or ownership of the Company. In certain instances employees have been granted the right to exercise options prior to vesting. Upon termination of an employee's employment with the Company for any reason, the Company has the right to repurchase all or any portion of the unvested shares acquired by the employee upon exercise of options, within 90 days following the date of termination. At March 31, 1999, 219,250 shares of common stock were subject to repurchase by the

Company. In addition, the Company has a thirty day right of first refusal if an optionee intends to sell shares acquired pursuant to options.

A summary of the activity under the 1997 Plan and the 1998 Plan is as follows:

<TABLE>
<CAPTION>

	Shares	Exercise Price Per Share	Aggregate Exercise Price	Weighted Average Exercise Price

<S>	<C>	<C>	<C>	<C>
Outstanding at September 30, 1996	--	--	--	--
Granted	1,688,500	$0.40	$ 675,400	$0.40
Terminated	(105,000)	$0.40	(42,000)	0.40
Outstanding at September 30, 1997	1,583,500	$0.40	633,400	0.40
Granted	1,903,009	$0.40--$3.35	3,283,649	1.73
Exercised	(297,960)	$0.40--$1.50	(265,784)	0.89
Terminated	(194,784)	$0.40--$3.25	(91,564)	0.47
Outstanding at September 30, 1998	2,993,765	$0.40--$3.35	3,559,701	1.19
Granted	1,503,900	$3.35--$4.25	5,987,675	3.98
Exercised	(102,390)	$0.40--$0.60	(41,012)	0.40
Terminated	(176,436)	$0.40--$3.75	(510,699)	2.89
Outstanding at March 31, 1999 (unaudited)	4,218,839	$0.40--$4.25	$8,995,665	$2.13

</TABLE>

For financial reporting purposes, the Company has determined that the deemed fair value on the date of grant of employee stock options granted after September 30, 1998 was in excess of the exercise price of the options. Consequently, the Company has recorded deferred compensation of $5,485,510 for the six-month period ended March 31, 1999. Of the total deferred compensation, $516,264 was amortized during the six months ended March 31, 1999.

At March 31, 1999 options to purchase 2,960,863 shares of common stock were exercisable.

At September 30, 1998 and March 31, 1999, options to purchase 541,559 and 815,095 shares of common stock, respectively, remain available for issuance.

The following summarizes information with respect to stock options outstanding at September 30, 1998:

<TABLE>
<CAPTION>

Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Prices	Number Exercisable	Weighted Average Exercise Prices

$0.40--$0.60	1,587,356	8.54	$0.42	518,978	$0.40
$0.90--$1.50	951,659	9.67	$1.50	427,492	$1.50
$2.50--$3.35	454,750	9.93	$3.23	124,519	$3.15

The following information concerning the Company's 1998 Plan is provided in accordance with Statement of Financial Accounting Standards No. 123 (SFAS 123), "Accounting for Stock-Based Compensation." The Company accounts for the 1998 Plan in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations.

The fair value of each option grant has been estimated on the date of grant using the minimum value method with the following weighted average assumptions used for grants in the years ended September 30, 1997 and 1998:

	September 30, 1997	September 30, 1998
Risk-free interest rates	5.85%--6.86%	4.23%--6.08%
Expected life	5 years	5 years
Expected dividend yield	--	--
Expected volatility	--	--

The weighted average fair value for options granted was $0.10 and $0.36 for the years ended September 30, 1997 and 1998, respectively.

The pro forma net loss for the Company for the years ended September 30, 1997 and 1998 following the provisions of SFAS 123, was $5,312,228 and $16,353,107, respectively. The pro forma basic and diluted net loss per share for the years ended September 30, 1997 and 1998 was $3.55 and $6.93, respectively.

12. Shareholder Note Receivable:

On February 25, 1998, the Company granted a nonstatutory option to purchase a total of 183,000 shares of the Company's common stock to the then chairman of the board of directors (the Optionee). These options were immediately exercisable and the shares purchased thereunder are subject to repurchase by the Company, with the right to repurchase expiring in 16 equal quarterly installments. At the time of the option grant, the Optionee exercised the option to purchase the entire 183,000 shares of common stock, in exchange for a $109,800 note. The note is secured by the 183,000 shares of common stock and by other assets of the Optionee. Under the terms of the note, interest is accrued at 5.61% per annum. Interest is to be repaid in four equal annual installments commencing February 24, 1999. The entire principal amount is due and payable in one lump sum on February 24, 2002. At March 31, 1999, the Company had not elected to repurchase any of these shares.

13. Warrants:

In connection with the issuance of certain convertible notes (see Note 6), the Company issued warrants to purchase shares of the Company's common stock to the note holders. Warrants to purchase 75,000 and 20,000 shares of the Company's common stock were granted in September 1996 and January 1997, respectively. The exercise price of the warrants is equal to $0.10 per share. The warrants expire upon the earlier of i) five years from the date of grant, ii) the closing of a underwritten public offering of the Company's common stock for not less than $2.50 per share and gross proceeds of at least $10,000,000, or iii) the closing of a consolidation or merger of the Company. At March 31, 1999, none of the warrants had as yet been exercised. The fair value of the warrants was determined using the Black-Scholes model and was accounted for as interest expense over the time period the notes were outstanding.

<PAGE>

14. Related Party Transactions:

One of the parties who has extended credit to the Company under the terms of a master lease agreement (see Note 8), also is a significant customer of the Company. For the years ended September 30, 1997 and 1998, and the six month periods ended March 31, 1998 and 1999, the Company earned $122,000, $309,943,

$104,849, and $207,428, respectively, in revenue from sales to this customer, and had $138,593 and $75,540 in total receivables at September 30, 1998 and March 31, 1999, respectively. The Company owed this customer $991,522 and $1,173,493 at September 30, 1998 and March 31, 1999, respectively, under terms of the master lease agreement, and also owed another $93,841 and $239,300, respectively, in other trade-related payables.

An investor, who participated in the Company's Series D and Series E preferred stock offerings, is also a customer of the Company. For the years ended September 30, 1997 and 1998, and the six month periods ended March 31, 1998 and 1999, the Company earned $43,000, $457,513, $217,714, and $604,472, respectively, in revenue from sales to this customer, and had $38,565 and $957,516 in total receivables at September 30, 1998 and March 31, 1999, respectively. In addition, $443,395 of the deferred revenue balance at March 31, 1999 related to this customer.

15. Retirement Savings Plan:

On November 1, 1997, the Company established the Digital Island Retirement Savings Plan (Retirement Plan), a defined contribution plan, covering all eligible employees. Employees may elect to contribute from 1%-15% of their annual compensation to the Retirement Plan. Matching contributions by the Company are discretionary. The Company has made no contributions during the year ended September 30, 1998, or the six month period ended March 31, 1999.

16. Subsequent Events:

On April 20, 1999, executive officers of the Company exercised stock options to purchase 335,999 shares of common stock in exchange for full-recourse notes. The total principal amount of these notes is $266,399. The notes bear interest at the rate of 7.75% per annum, compounded semiannually. Accrued interest is due and payable at successive quarterly intervals over the four-year term of the note, and the principal balance will become due and payable in one lump sum at the end of the four year term. None of the shares purchased with the notes may be sold unless the principal portion of the note attributable to those shares, together with the accrued interest on that principal portion, is paid in full.

On April 21, 1999, the Board of Directors approved the reincorporation of the Company in the state of Delaware. Pursuant to the reincorporation, each share of common and preferred stock of the Company's California predecessor entity is exchanged for one share of common and preferred stock of the newly formed Delaware entity. Pursuant to the reincorporation, the number of authorized shares of common stock will increase to 100,000,000 with a par value of $0.001 per share. Additionally, 10,000,000 shares of undesignated preferred stock were authorized with a par value of $0.001 per share. These consolidated financial statements have been restated for the reincorporation of the Company in Delaware.

Also, on April 21, 1999, the Board of Directors adopted the 1999 Stock Incentive Plan (the 1999 Plan). The 1999 Plan is to serve as the successor to the 1998 Plan. Upon the initial public offering of the Company's common stock, all outstanding options under the 1998 Plan, together with the remaining share reserved under that plan, are to be incorporated into the 1999 Plan, with no further grants of common stock options to be made under the 1998 Plan. Upon implementation of the 1999 Plan, an additional 2,500,000 shares of common stock will be reserved for issuance.

<PAGE>

Additionally, on April 21, 1999, the Board of Directors adopted the 1999 Employee Stock Purchase Plan (1999 ESPP). Under the 1999 ESPP, eligible employees are allowed to have salary withholdings of up to a certain specified percentage of their base compensation to purchase shares of common stock at a price equal to 85% of the lower of the market value of the stock at the beginning or end of defined purchase periods. The initial purchase period commences upon the execution and final pricing of the underwriting agreement for the initial public offering of the Company's common stock. The 1999 ESPP will become effective upon the initial public offering of the Company's common stock. A total of 300,000 shares will be reserved for issuance under the 1999 ESPP.

On April 21, 1999, options to purchase 99,500 shares of common stock were granted at an exercise price of $7.50. Deferred compensation associated with these shares is $238,800.

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Prospective investors may rely only on the information contained in this prospectus. Neither Digital Island, Inc. nor any underwriter has authorized anyone to provide prospective investors with different or additional information. This prospectus is not an offer to sell nor is it seeking an offer to buy these securities in any jurisdiction where the offer or sale is not permitted. The information contained in this prospectus is correct only as of the date of this prospectus, regardless of the time of the delivery of this

prospectus or any sale of these securities.

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<TABLE>
<CAPTION>

</TABLE>

Until , 1999 (25 days after the date of this prospectus), all dealers that effect transactions in these securities, whether or not participating in this offering, may be required to deliver a prospectus. This is in addition to the dealers' obligation to deliver a prospectus when acting as underwriters and with respect to their unsold allotments or subscriptions.

- ---
- ---
- ---
- ---

Shares

[LOGO]

Digital Island, Inc.

Common Stock

PRELIMINARY PROSPECTUS

Bear, Stearns & Co. Inc.

Lehman Brothers

Thomas Weisel Partners LLC

, 1999

- ---
- ---

<PAGE>

PART II

INFORMATION NOT REQUIRED IN PROSPECTUS

Item 13. Other Expenses of Issuance and Distribution

The following table sets forth the costs and expenses, other than underwriting discounts, payable by the Registrant in connection with the offer and sale of the Common Stock being registered. All amounts are estimates except the registration fee, the NASD filing fee and the Nasdaq National Market entry and application fee.

<TABLE>

<S>	<C>
Registration fee	$20,850
NASD filing fee	8,000
Blue Sky/NASD fees and expenses (including legal fees)	*
Nasdaq National Market entry and application fee	*
Accounting fees and expenses	150,000
Other legal fees and expenses	300,000
Transfer agent and registrar fee	*
Printing and engraving	140,000

Miscellaneous.....	*
Total.....	$ *

</TABLE>

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* To be supplied by amendment.

Item 14. Indemnification of Directors and Officers

Section 145 of the Delaware General Corporation Law authorizes a court to award or a corporation's Board of Directors to grant indemnification to directors and officers in terms sufficiently broad to permit such indemnification under certain circumstances for liabilities (including reimbursement for expenses incurred) arising under the Securities Act of 1933, as amended (the "Securities Act"). Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers and controlling persons of the Registrant pursuant to the foregoing provisions, the Registrant has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Securities Act and is, therefore, unenforceable. Article VII, Section 6, of the Registrant's Bylaws provides for mandatory indemnification of its directors and officers and permissible indemnification of employees and other agents to the maximum extent permitted by the Delaware General Corporation Law. The Registrant's Amended and Restated Certificate of Incorporation (the "Certificate of Incorporation") provides that, pursuant to Delaware law, its directors shall not be liable for monetary damages for breach of the directors' fiduciary duty as directors to the Company or its stockholders. This provision in the Certificate of Incorporation does not eliminate the directors' fiduciary duty, and in appropriate circumstances equitable remedies such as injunctive or other forms of non-monetary relief will remain available under Delaware law. In addition, each director will continue to be subject to liability for breach of the director's duty of loyalty to the Company for acts or omissions not in good faith or involving intentional misconduct, for knowing violations of law, for actions leading to improper personal benefit to the director, and for payment of dividends or approval of stock repurchases or redemptions that are unlawful under Delaware law. The provision also does not affect a director's responsibilities under any other law, such as the federal securities laws or state or federal environmental laws. The Registrant has entered into Indemnity Agreements with its officers and directors, a form of which is attached as Exhibit 10.4 hereto and incorporated herein by reference. The Indemnification Agreements provide the Registrant's officers and directors with further indemnification to the maximum extent permitted by the Delaware General Corporation Law. The Registrant maintains directors and officers liabilities insurance. Reference is made to Section 8 of the Underwriting Agreement contained in Exhibit 1.1 hereto, indemnifying officers and directors of the Registrant against certain liabilities.

Item 15. Recent Sales of Unregistered Securities

Since April 1, 1996, we have issued and sold the following securities:

(a) The Registrant issued and sold 406,350 shares of its common stock to employees and consultants for an aggregate purchase price of $280,512 pursuant to direct stock issuances and the exercise of options under its 1998 Stock Option/Stock Issuance Plan.

(b) In September 1996, the Registrant issued a warrant to purchase up to 75,000 shares of its common stock, at an exercise price of $0.10 per share (subject to adjustment), to Vanguard V, L.P.

(c) In November 1996, the Registrant issued and sold 50,000 shares of its common stock to two individuals for an aggregate purchase price of $20,000.

(d) In January 1997, the Registrant issued a warrant to purchase up to 20,000 shares of its common stock, at an exercise price of $0.10 per share (subject to adjustment), to Vanguard V, L.P.

(e) In February 1997, the Registrant issued 2,005,875 shares of its common stock to several investors. Of such shares, 5,875 were sold for an aggregate consideration of $2,350, and 2,000,000 shares were converted from outstanding preferred stock.

(f) In March 1997, the Registrant issued and sold an aggregate of 4,000,000 shares of Series A Preferred Stock to several investors for an aggregate of purchase price of $4,000,000.

(g) In April 1997, the Registrant issued 15,000 shares of its common stock to one corporation in consideration for services rendered with an aggregate fair value of $6,000.

(h) In July 1997, the Registrant issued and sold an aggregate of 3,000,000 shares of Series B Preferred Stock to several investors for an aggregate of purchase price of $7,000,000.

(i) In March 1998 and May 1998, the Registrant issued and sold an aggregate of 4,283,181 shares of Series C Preferred Stock to several investors for an aggregate of purchase price of $14,776,974.

(j) In July 1998 and August 1998, the Registrant issued and sold an aggregate of 2,022,476 shares of Series D Preferred Stock to several investors for an aggregate of purchase price of $10,617,999.00.

(k) In February 1999, the Registrant issued and sold an aggregate of 11,764,706 shares of Series E Preferred Stock to several investors for an

aggregate of purchase price of $50,000,000.05

None of the foregoing transactions involved any underwriters, underwriting discounts or commissions, or any public offering, and the Registrant believes that each transaction was exempt from the registration requirements of the Securities Act by virtue of Section 4(2) thereof, Regulation D promulgated thereunder or Rule 701 pursuant to compensatory benefit plans and contracts relating to compensation as provided under such Rule 701. The recipients 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 appropriate legends were affixed to the share certificates and instruments issued in such transactions. All recipients had adequate access, through their relationships with the Registrant, to information about the Registrant.

<PAGE>

Item 16. Exhibits and Financial Statement Schedules

(a) Exhibits

<TABLE>
<C> <S>
1.1* Form of Underwriting Agreement
3.1* Amended and Restated Certificate of Incorporation
3.2* Bylaws, as amended to date
4.1 Reference is made to Exhibit 3.1
4.2 Reference is made to Exhibit 3.2
4.3* Specimen Common Stock Certificate
4.4 Amended and Restated Investors' Rights Agreement, among the Registrant and the parties listed on the signature pages thereto dated February 19, 1999
5.1* Opinion of Brobeck, Phleger & Harrison LLP
10.1* 1998 Stock Option/Stock Issuance Plan
10.2* Form of 1999 Stock Incentive Plan
10.3* Form of 1999 Employee Stock Purchase Plan
10.4 Form of Indemnification Agreement for Officers and Directors
10.5 Employment Agreement between the Registrant and Ruann Ernst
10.6 Employment Agreement between the Registrant and Allan Leinwand
10.7 Employment Agreement between the Registrant and Michael Sullivan
10.8 Office Lease Agreement, between the Registrant and John Hancock Mutual Life Insurance Co., dated as of April 8, 1997
21.1 Subsidiaries of the Registrant
23.1 Consent of PricewaterhouseCoopers LLP, Independent Auditors
23.2* Consent of Brobeck, Phleger & Harrison LLP (included in Exhibit 5.1)
24.1 Power of Attorney (included on signature page)
27.1 Financial Data Schedule
</TABLE>

- ----------
* To be filed by amendment.

<TABLE>
<S> <C>
(b) Financial Statement Schedules
Schedule II--Valuation and Qualifying Accounts S-2
</TABLE>

Financial Statement Schedules not listed above have been omitted because the information required to be set forth therein is not applicable or is shown in the financial statements or notes thereto.

Item 17. Undertakings

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers and controlling persons of the Registrant pursuant to the provisions described in Item 14, or otherwise, the Registrant has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Securities Act and is, therefore, unenforceable. In the event that a claim for indemnification against such liabilities (other than the payment by the Registrant of expenses incurred or paid by a director, officer or controlling person of the Registrant in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, the Registrant will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question of whether such indemnification by it is against public policy as expressed in the Securities Act and will be governed by the final adjudication of such issue. The undersigned Registrant hereby undertakes to provide to the Underwriters at the closing specified in the Underwriting Agreement certificates in such denominations and registered in such names as required by the Underwriters to permit prompt delivery to each purchaser. The undersigned Registrant hereby undertakes that: (1) For purposes of determining any liability under the Securities Act, the information omitted from the form of Prospectus filed as part of this Registration Statement in reliance upon Rule 430A and contained in a form of Prospectus filed by the Registrant pursuant to Rule 424(b)(1) or (4) or 497(h) under the Securities Act shall be deemed to be part of this Registration Statement as of the time it was declared effective and (2) For the purpose of determining any liability under the Securities Act, each post-effective amendment that contains a form of prospectus shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof.

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SIGNATURES

Pursuant to the requirements of the Securities Act of 1933, as amended, the Registrant certifies that it has reasonable grounds to believe that it meets all the requirements for filing on Form S-1 and has duly caused this Registration Statement to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of San Francisco, State of California, on this 26th day of April, 1999.

Digital Island, Inc.

/s/ Ruann Ernst
By: _____
Ruann Ernst
Chief Executive Officer and
President

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints, jointly and severally, Ruann Ernst and T. L. Thompson, and each one of them, his true and lawful attorneys-in-fact and agents, each with full power of substitution, for him and in his name, place and stead, in any and all capacities, to sign any and all amendments (including post-effective amendments) to this Registration Statement, and to sign any registration statement for the same offering covered by this Registration Statement that is to be effective upon filing pursuant to Rule 462(b) promulgated under the Securities Act of 1933, as amended, and all post-effective amendments thereto, and to file the same, with all exhibits thereto and all documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming that each of said attorneys-in-fact and agents or any of them, or his or their substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

IN WITNESS WHEREOF, each of the undersigned has executed this Power of Attorney as of the date indicated.

Pursuant to the requirements of the Securities Act of 1933, as amended, this Registration Statement has been signed by the persons whose signatures appear below, which persons have signed such Registration Statement in the capacities and on the dates indicated:

<TABLE>
<CAPTION>
Signature	Title	Date

| --- | --- | --- |

<C> <S> <C>

/s/ Ron Higgins _____ Ron Higgins	Chairman of the Board of Directors	April 26, 1999
/s/ Ruann Ernst _____ Ruann Ernst	Chief Executive Officer, President and Director (Principal Executive Officer	April 26, 1999
/s/ T. L. Thompson _____ T. L. Thompson	Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	April 26, 1999

</TABLE>

<PAGE>

<TABLE>
<CAPTION>

Signature	Title	Date

<C> <S> <C>

/s/ Charlie Bass _____ Charlie Bass	Director	April 26, 1999
/s/ Christos Cotsakos _____ Christos Cotsakos	Director	April 26, 1999
/s/ Marcelo A. Gumucio _____ Marcelo A. Gumucio	Director	April 26, 1999
/s/ Cliff Higgerson _____ Cliff Higgerson	Director	April 26, 1999
/s/ David Spreng _____ David Spreng	Director	April 26, 1999
/s/ Shahan Soghikian _____	Director	April 26, 1999

Shahan Soghikian
</TABLE>

<PAGE>

REPORT OF INDEPENDENT ACCOUNTANTS ON FINANCIAL STATEMENT SCHEDULE

Board of Directors and Stockholders of Digital Island, Inc.

We have audited the financial statements of Digital Island, Inc. as of September 30, 1998 and 1997, and for each of the three years in the period ended September 30, 1998, and have issued our report thereon dated February 19, 1999. Our audits also included the financial statement schedule listed in Item 16(b) of this Registration Statement. This schedule is the responsibility of the Company's management. Our responsibility is to express an opinion based on our audits.

In our opinion, the financial statement schedule referred to above, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information required to be included therein.

/s/ PricewaterhouseCoopers LLP

San Francisco, California
February 19, 1999

<PAGE>

SCHEDULE II--VALUATION AND QUALIFYING ACCOUNTS

Digital Island, Inc.

<TABLE>
<CAPTION>

Description	Balance at Beginning of Period	Charged to Costs and Expenses	Deductions	Balance at End of Period
<S>	<C>	<C>	<C>	<C>
Year ended September 30, 1996:				
Deferred tax valuation allowance...	$ --	$ 22,000	$ --	$ 22,000
Total.....	$ --	$ 22,000	$ --	$ 22,000
Year ended September 30, 1997:				
Deferred tax valuation allowance...	$ 22,000	$2,121,000	$ --	$2,143,000

Total.....	$ 22,000	$2,121,000	$ --	$2,143,000
Year ended September 30, 1998:				
Allowance for doubtful accounts....	$ --	$ 111,104	$56,104	$ 55,000
Deferred tax valuation allowance...	2,143,000	6,023,000	--	8,166,000
Total.....	$2,143,000	$6,134,104	$56,104	$8,221,000

</TABLE>

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EXHIBIT INDEX

<TABLE>

<C>	<S>
1.1*	Form of Underwriting Agreement
3.1*	Amended and Restated Certificate of Incorporation
3.2*	Bylaws, as amended to date
4.1	Reference is made to Exhibit 3.1
4.2	Reference is made to Exhibit 3.2
4.3*	Specimen Common Stock Certificate
4.4	Amended and Restated Investors' Rights Agreement, among the Registrant and the parties listed on the signature pages thereto dated February 19, 1999
5.1*	Opinion of Brobeck, Phleger & Harrison LLP
10.1*	1998 Stock Option/Stock Issuance Plan
10.2*	Form of 1999 Stock Incentive Plan
10.3*	Form of 1999 Employee Stock Purchase Plan
10.4	Form of Indemnification Agreement for Officers and Directors
10.5	Employment Agreement between the Registrant and Ruann Ernst
10.6	Employment Agreement between the Registrant and Allan Leinwand
10.7	Employment Agreement between the Registrant and Michael Sullivan
10.8	Office Lease Agreement, between the Registrant and John Hancock Mutual Life Insurance Co., dated as of April 8, 1997
21.1	Subsidiaries of the Registrant
23.1	Consent of PricewaterhouseCoopers LLP, Independent Auditors
23.2*	Consent of Brobeck, Phleger & Harrison LLP (included in Exhibit 5.1)
24.1	Power of Attorney (included on signature page)
27.1	Financial Data Schedule

</TABLE>

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* To be filed by amendment.

</TEXT>

</DOCUMENT>

<DOCUMENT>

<TYPE>EX-4.4

<SEQUENCE>2
<DESCRIPTION>AMENDED AND RESTATED INVESTORS' RIGHTS AGREEMENT
<TEXT>

<PAGE>

EXHIBIT 4.4

DIGITAL ISLAND, INC.

AMENDED AND RESTATED

INVESTORS' RIGHTS AGREEMENT

February 19, 1999

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DIGITAL ISLAND, INC.

AMENDED AND RESTATED
INVESTORS' RIGHTS AGREEMENT

THIS AMENDED AND RESTATED INVESTORS' RIGHTS AGREEMENT (the "Agreement") is entered into as of February 19, 1999, by and among DIGITAL ISLAND, INC., a California corporation (the "Company"), and the individuals or entities listed on the signature pages hereof (each a "Holder" and collectively, the "Holders").

RECITALS

A. Certain of the Holders have purchased or will purchase shares of

the Company's Series E Preferred Stock (the "Series E Preferred") pursuant to the terms of a Series E Preferred Stock Purchase Agreement dated as of even date herewith among the Company and such Holders (the "Purchase Agreement").

B. The execution of this Agreement is a condition to the closing of the transactions contemplated by the Purchase Agreement.

C. The Company desires to enter into this Agreement and grant the Holders the rights contained herein in order to fulfill such condition.

D. The Company and those Holders who hold shares of the Company's Series A Preferred Stock (the "Series A Preferred"), Series B Preferred Stock (the "Series B Preferred"), Series C Preferred Stock (the "Series C Preferred") and Series D Preferred Stock (the "Series D Preferred"), are parties to an Amended and Restated Rights Agreement dated as of July 13, 1998 (the "Existing Rights Agreement"), and wish to amend and restate the Existing Rights Agreement, upon the terms and conditions set forth herein.

NOW, THEREFORE, in consideration of the mutual promises and covenants hereinafter set forth, the parties agree as follows:

Section 1
Certain Definitions

Certain Definitions. As used in this Agreement, the following terms shall have the following respective meanings:

1.1 "SEC" shall mean the Securities and Exchange Commission or any other federal agency at the time administering the Securities Act.
<PAGE>

1.2 "Exchange Act" shall mean the Securities Exchange Act of 1934, as amended, and the rules and regulations of the SEC promulgated thereunder, as the same shall be in effect from time to time.

1.3 "Initial Public Offering" or "IPO" means the Company's sale of its Common Stock in a bona fide, firm commitment underwriting pursuant to a registration statement under the Securities Act yielding gross proceeds to the Company of at least $25,000,000.00 and a per share offering price of at least $7.00 (as adjusted for stock splits and the like).

1.4 The terms "register", "registered" and "registration" refer to a registration effected by preparing and filing a registration statement in compliance with the Securities Act (as defined below), and the declaration or ordering of the effectiveness of such registration statement.

1.5 "Registrable Securities" means (i) the shares of Common Stock of

the Company issuable or issued upon conversion of the Series A Preferred, Series B Preferred, Series C Preferred, Series D Preferred or Series E Preferred of the Company (such shares of Common Stock, the "Stock"), and (ii) any other shares of the Company's Common Stock issued as (or issuable upon conversion or exercise of any warrant, right or other security which is issued as) a dividend or other distribution with respect to or in exchange for or replacement of the Series A Preferred, Series B Preferred, Series C Preferred, Series D Preferred or Series E Preferred of the Company or the Stock, excluding in all cases, however, any Registrable Securities sold by a person in a transaction in which a Holder's rights under this Agreement are not assigned; provided, however, that Registrable Securities shall only be treated as Registrable Securities if and so long as, they have not been (A) sold to or through a broker or dealer or underwriter in a public distribution or a public securities transaction or (B) sold in a transaction exempt from the registration and prospectus delivery requirements of the Securities Act under Section 4(1) thereof so that all transfer restrictions and restrictive legends with respect thereto are removed upon the consummation of such sale.

1.6 "Securities Act" shall mean the Securities Act of 1933, as amended, and the rules and regulations of the SEC promulgated thereunder, as the same shall be in effect from time to time.

1.7 An "Affiliate" of an entity referenced herein shall mean (i) any entity who controls, is controlled by, or is under common control with such entity, (ii) any constituent partner or shareholder of such entity, (iii) all mutual funds or other pooled investment vehicles or entities under the control or management of such entity, or the general partner or investment advisor of such entity, or any Affiliate of such mutual funds, pooled investment vehicles, general partner or investment advisor, or (iv) with respect to an individual, such individual's spouse, siblings, ancestors and descendants (whether natural or adopted), any spouses of such siblings, ancestors and descendants, any siblings of such ancestors and descendants, and any trust established solely for the benefit of one or more of such individual's spouse, siblings, ancestors and/or descendants.

Section 2
PIGGYBACK RIGHTS

2.1 Notice of Registration. If at any time or from time to time, the Company shall determine to register any of its equity securities for its own account in an underwritten public offering, the Company will:

(i) promptly give to the Holders written notice thereof; and

(ii) include in such registration (and any related qualification under blue sky laws or other compliance), and underwriting, all the Registrable Securities (subject to cutback as set forth in Section 2.2) specified in a written request or requests made within thirty (30) days after receipt of such written notice from the Company by any Holder.

2.2 Underwriting. The right of any Holder to registration pursuant
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to this Section 2 shall be conditioned upon such Holder's participation in such underwriting and the inclusion of Registrable Securities in the underwriting to the extent provided herein. If any Holder proposes to distribute its securities through such underwriting, such Holder shall (together with the Company and any other shareholders distributing their securities through such underwriting) enter into an underwriting agreement in customary form with the managing underwriter selected for such underwriting by the Company. Notwithstanding any other provision of this Section 2, if the managing underwriter determines that marketing factors require a limitation of the number of shares to be underwritten, the managing underwriter may limit the Registrable Securities to be included in such registration. The Company shall so advise the Holder and the other shareholders distributing their securities through such underwriting pursuant to piggyback registration rights similar to this Section 2, and the number of shares of Registrable Securities and other securities that may be included in the registration and underwriting shall be allocated among the Holder and any other participating shareholders in proportion, as nearly as practicable, to the respective amounts of Registrable Securities held by such Holder and other securities held by other shareholders and entitled to registration rights at the time of filing the registration statement, provided that the aggregate amount of Registrable Securities held by selling Holders included in the offering shall not be reduced below twenty percent (20%) of the total amount of securities included in that offering unless the offering is the Initial Public Offering of the Company's securities, in which case all Registrable Securities held by Holders may be excluded. In the event the managing underwriter does determine that marketing factors require a limitation of the number of shares to be underwritten (the "Cutback"), such Cutback shall be applied first to any participating shareholders other than Holders of Registrable Securities before it shall be applied to Holders of Registrable Securities, subject to the above mentioned twenty percent (20%) reduction limit, if at all. To facilitate the allocation of shares in accordance with the above provisions, the Company or the underwriters may round the number of shares allocated to each Holder or other shareholder to the nearest 100 shares. If any Holder or other shareholder disapproves of the terms of any such underwriting, he or she may elect to withdraw therefrom by written notice to the Company and the managing underwriter. Any securities excluded or withdrawn from such underwriting shall be withdrawn from such registration, and shall not be transferred in a public distribution prior to one-hundred eighty (180) days after the effective date of the registration statement relating thereto.

2.3 Right to Terminate Registration. The Company shall have the
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right to terminate or withdraw any registration initiated by it under this Section 2 prior to the effectiveness of such registration, whether or not any Holder has elected to include securities in such registration.

2.4 Definition of Holder. Solely for purposes of this Section 2 and
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for so long as he remains employed by the Company, Ron Higgins shall be deemed to be a "Holder" and all shares of the Company's capital stock held by him shall be deemed to be "Registrable Securities."

Section 3

Demand Registration

3.1 Demand Registration. Beginning on the earlier of (i) February 19,
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2001, or (ii) one year after the Company's Initial Public Offering, if Holders of more than 66-2/3% of the Registrable Securities request that the Company file a registration statement for the lesser of 50% of the outstanding Registrable Securities or a number of shares yielding gross aggregate proceeds in excess of $15,000,000, then the Company will (x) promptly give written notice of the proposed registration to all other Holders, and (y) use its reasonable best efforts to cause such shares to be registered (together with any Registrable Securities of any Holder or Holders joining in such request as are specified in a written request received by the Company within twenty (20) days after receipt of such written notice from the Company); provided, however, that (a) the Company shall not be required to effect any such registration within one-hundred eighty (180) days prior to its good faith estimate of the date of the filing of, and one-hundred eighty (180) days following the effective date of, a registration statement pertaining to an underwritten public offering of the Company's securities, (b) such registration obligation shall be deferred for not more than sixty days if the Company furnishes the requesting holders with a certificate of the President of the Company stating that in the good faith judgment of the Board of Directors it would be detrimental to the Company or its shareholders for a registration statement to be filed in the near future, but the Company shall not be entitled to such deferral more than twice in any 12-month period and (c) the Company shall not be obligated to effect more than a total of two such demand registrations. Any such registration shall be firmly underwritten by an underwriter of nationally recognized standing which shall be mutually agreeable to the Company and a majority in interest of the Holders requesting the registration. If any Holder disapproves of the terms of the underwriting, such person may elect to withdraw therefrom by written notice to the Company, the managing underwriter and the Holders making the request. The Registrable Securities so withdrawn shall also be withdrawn from registration, and such Registrable Securities shall not be transferred in a public

distribution prior to ninety (90) days after the effective date of such registration; provided, however, that, if by the withdrawal of such Registrable Securities, a greater number of Registrable Securities held by other Holders may be included in such registration (up to the maximum of any limitation imposed by the underwriters), then the Company shall offer to all Holders who have included Registrable Securities in the registration the right to include additional Registrable Securities. Holders shall be so entitled to include additional Registrable Securities in the registration upon written notice within 10 days of such offer being made.

3.2 Underwritten Public Offering. The Company shall enter into an underwriting agreement with an investment banking firm or firms containing representations,

warranties, indemnities and agreements then customarily included by an issuer in underwriting agreements with respect to secondary distributions. The Company shall not cause the registration under the Securities Act of any other shares of its Common Stock to become effective (other than registration of an employee stock plan, or registration in connection with any Rule 145 or similar transaction) during the effectiveness of a registration requested hereunder for an underwritten public offering if, in the judgment of the underwriter or underwriters, marketing factors would adversely affect the price of the Registrable Securities subject to such underwritten registration.

3.3 Limitations. Notwithstanding the foregoing, if at the time of any request to register Registrable Securities pursuant to this Section 3, the Company is engaged, or has fixed plans to engage within one-hundred eighty (180) days of the request, in a registered public offering or any other activity that, in the good faith determination of the Board of Directors of the Company, would be adversely affected by the requested registration to the material detriment of the Company, then the Company may, at its option, direct that such request be delayed for a period not in excess of one-hundred eighty (180) days from the effective date of such offering, or the date of commencement of such other material activity, as the case may be. Such rights to delay a request to be exercised by the Company may not be exercised more than once in any twelve month period.

Section 4
FORM S-3 REGISTRATION

4.1 Registrations on Form S-3. Holders shall be entitled to request (an "S-3 Registration Request") an unlimited number of registrations of

Registrable Securities then owned by such requesting Holders on a Form S-3 registration statement or any successor form under the Securities Act (an "S-3 Registration"). The S-3 Registration Request must be made in writing and the S-3 Registration Request shall: (i) specify the number of shares intended to be offered and sold; (ii) express the present intention of the requesting Holders to offer or cause the offering of such shares for distribution; and (iii) contain the undertaking of the requesting Holders to provide all such information and materials and take all such action as may be required in order to permit the Company to comply with all applicable requirements of the SEC and to obtain any desired acceleration of the effective date of such registration statement. The Company shall, as soon as practicable, (a) promptly give written notice of the proposed registration to all other Holders, and (b) file an S-3 Registration and use its reasonable best efforts to obtain all such qualifications and compliance as may be so requested and as would permit or facilitate the sale and distribution of all or such portion of the requesting Holders' Registrable Securities as are specified in the S-3 Registration Request (together with any Registrable Securities of any Holder or Holders joining in such request as are specified in a written request received by the Company within twenty (20) days after receipt of such written notice from the Company), within 45 days after receipt of such written notice by the Company; provided,

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however, that the Company shall not be obligated to effect any such

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registration, qualification or compliance, pursuant to this Section 4 if: (i) Form S-3 is not available for such offering by the requesting Holders; (ii) the requesting Holders, together with the holders of any other securities of the Company entitled to inclusion in such registration, propose to sell Registrable Securities and such other securities (if any) at an aggregate gross price to the public of less than $1,000,000; or (iii) the Company has, within the twelve (12) month period preceding

the date of such request, already effected two registrations on Form S-3 for any Holder pursuant to this Section 4.

4.2 Limitations. Notwithstanding the foregoing, if at the time of

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any request to register Registrable Securities pursuant to this Section 4, the Company is engaged, or has fixed plans to engage in any activity that, in the good faith determination of the Board of Directors, would be adversely affected by the requested registration to the material detriment of the Company, then the Company may, at its option, direct that such request be delayed for a period not in excess of forty-five (45) days from the effective date of such material activity. Such rights to delay a request to be exercised by the Company may not be exercised more than once in any twelve month period.

Section 5

OBLIGATIONS OF COMPANY

Whenever the Company is required by the provisions of this Agreement to use its reasonable best efforts to effect the registration of the Registrable Securities, the Company shall: (i) prepare and, as soon as possible, file with the SEC a registration statement with respect to the Registrable Securities, and use its reasonable best efforts to cause such registration statement to become effective and to remain effective until the earlier of the sale of the Registrable Securities so registered or one hundred twenty (120) days subsequent to the effective date of such registration provided, however, that if the

Holders requesting a demand registration pursuant to an S-3 Registration pursuant to Section 4 state in their request that they desire a shelf registration pursuant to Rule 415 under the Securities Act (a "Shelf Registration"), then the Company shall, solely in the first such instance, cause such registration statement to be a Shelf Registration and shall cause such registration statement to become effective and to remain effective until the earlier of the date of the sale of the Registerable Securities so registered or nine (9) months subsequent to the effective date of such registration statement; (ii) prepare and file with the SEC such amendments and supplements to such registration statement and the prospectus used in connection therewith as may be necessary to make and to keep such registration statement effective and to comply with the provisions of the Securities Act with respect to the sale or other disposition of all securities proposed to be registered in such registration statement until the earlier of the sale of the Registrable Securities so registered or one hundred twenty (120) days subsequent to the effective date of such registration statement, or, in the case of a Shelf Registration, until the earlier of the sale of the Registerable Securities so registered or nine (9) months subsequent to the effective date of such registration statement; (iii) furnish to any Holder such number of copies of any prospectus (including any preliminary prospectus and any amended or supplemented prospectus), in conformity with the requirements of the Securities Act, as such Holder may reasonably request in order to effect the offering and sale of the Registrable Securities to be offered and sold, but only while the Company shall be required under the provisions hereof to cause the registration statement to remain current; (iv) use its reasonable best efforts to register or qualify the Registrable Securities covered by such registration statement under the securities or blue sky laws of such states as Holder shall reasonably request, maintain any such registration or qualification current until the earlier of the sale of the Registrable Securities so registered or one hundred twenty (120) days subsequent to the effective date of the registration statement, or, in the case of a Shelf Registration, until the earlier of the sale of the Registrable Securities so registered or nine (9) months subsequent to the effective date

of such registration statement and, take any and all other actions either

necessary or reasonably advisable to enable Holders to consummate the public sale or other disposition of the Registrable Securities in jurisdictions where such Holders desire to effect such sales or other disposition; (v) cause all Registrable Securities registered pursuant hereunder to be listed on each securities exchange on which the same class of securities of the Company are then listed; and (vi) take all such other actions either necessary or reasonably desirable to permit the Registrable Securities held by a Holder to be registered and disposed of in accordance with the method of disposition described herein, including causing the Company's senior management to use their commercially reasonable efforts in the marketing of any securities pursuant to any underwritten public offering so registered. Notwithstanding the foregoing, the Company shall not be required to register or to qualify an offering of the Registrable Securities under the laws of a state if as a condition to so doing the Company is required to qualify to do business or to file a general consent to service of process in any such state or jurisdiction, unless the Company is already subject to service in such jurisdiction.

Section 6
EXPENSES OF REGISTRATION

Except with respect to the Demand Registrations and the S-3 Registrations set forth in Sections 3 and 4 hereof for which the Company shall pay for only the first two Demand Registrations and the first two S-3 Registrations initiated pursuant to this Agreement, the Company shall pay all of the fees and expenses incurred in connection with any registration statement that is initiated pursuant to this Agreement, including, without limitation, all SEC and blue sky registration and filing fees, printing expenses, transfer agent and registrar fees, the fees and disbursements of the Company's outside counsel, the reasonable fees and disbursements of one counsel to the Holders and independent accountants (the "Registration Expenses"). If a registration proceeding is begun upon the request of Holders pursuant to Section 3 or 4 but such request is subsequently withdrawn, then the Holders of Registrable Securities to have been registered may either: (i) bear all Registration Expenses of such proceeding, pro rata on the basis of the number of shares to have been registered, in which case the Company shall be deemed not to have effected a registration pursuant to Section 3 or 4, as applicable, of this Agreement; or (ii) require the Company to bear all Registration Expenses of such proceeding, in which case the Company shall be deemed to have effected a registration pursuant to Section 3 or 4, as applicable, of this Agreement. Notwithstanding the foregoing, however, if at the time of the withdrawal, the Holders have learned of a material adverse change in the condition, business or prospects of the Company from that known to the Holders at the time of their request, then the Holders shall be required to pay one-half (1/2) of any of said Registration Expenses, unless the Company shall have failed to perform any of its obligations with respect to such registration proceeding in which case the holders shall bear none of the Registration Expenses. In such case, the Company shall be deemed not to have effected a registration pursuant to Section 3 or 4, as applicable, of this Agreement. The Holders shall pay all of the fees and

expenses incurred in connection with any Demand Registration or S-3 Registration initiated pursuant to this Agreement after the filing of the first two Demand Registrations and the first two S-3 Registrations. In addition, any underwriting discounts, fees and disbursements of any additional counsel to the Holders, selling commissions and stock transfer or other taxes applicable to the Registrable Securities registered on behalf of Holders shall be borne by the Holders of the Registrable Securities included in such registration.

Section 7
INDEMNIFICATION

7.1 The Company. To the extent permitted by law, the Company will indemnify Holders and each person controlling Holders within the meaning of Section 15 of the Securities Act, and each underwriter if any, of the Company's securities, with respect to any registration, qualification or compliance which has been effected pursuant to this Agreement, against all expenses, claims, losses, damages or liabilities (or actions in respect thereof), including any of the foregoing incurred in settlement of any litigation, commenced or threatened, arising out of or based on any untrue statement (or alleged untrue statement) of a material fact contained in any registration statement, prospectus, offering circular or other document, or any amendment or supplement thereto, incident to any such registration, qualification or compliance, or based on any omission (or alleged omission) to state therein a material fact required to be stated therein or necessary to make the statements therein, in light of the circumstances in which they were made, not misleading, or any violation by the Company of any rule or regulation promulgated under the Securities Act applicable to the Company in connection with any such registration, qualification or compliance, and the Company will reimburse Holders and each person controlling Holders, and each underwriter, if any, for any legal and any other expenses reasonably incurred in connection with investigating, preparing or defending any such claim, loss, damage, liability or action, provided that the Company will not be liable in any such case to the extent that any such claim, loss, damage, liability or expense arises out of or is based on any untrue statement or omission or alleged untrue statement or omission, made in reliance upon and in conformity with written information furnished to the Company by such Holder or controlling person or underwriter seeking indemnification expressly for use therein; and provided further, that the indemnity provided in this Section 7.1 with respect to any losses, claims, damages, liabilities or actions, arising from a sale of Registrable Securities pursuant to a registration hereunder, based upon any untrue statement or alleged untrue statement of material fact or omission or alleged omission to state a material fact in any preliminary or final prospectus (or amendment or supplement thereto) of the Company shall not inure to the benefit of or be available to the Holders or any other person if a copy of the prospectus, as further amended or supplemented, in which such untrue

statement or alleged untrue statement or omission or alleged omission was corrected is sent or given to those persons asserting such losses, claims, damages, liabilities or actions within the time required by the Act and the Rules and Regulations thereto.

7.2 Holders. To the extent permitted by law, each Holder will, if
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Registrable Securities held by such Holder are included in the securities as to which such registration, qualification or compliance is being effected (the "Indemnifying Holder"), indemnify the Company, each of its directors and officers and each person who controls the Company within the meaning of Section 15 of the Securities Act, and each underwriter, if any, of the Company's securities with respect to any registration, qualification or compliance which has been effected pursuant to this Agreement, against all expenses, claims, losses, damages and liabilities (or actions in respect thereof), arising out of or based on any untrue statement (or alleged untrue statement) of a material fact contained in any such registration statement, prospectus, offering circular or other document, or any amendment or supplement thereto, incident to any such registration, qualification or compliance, or based on any omission (or alleged omission) to state therein a material fact required to be stated therein or necessary to make the statements therein not misleading, or any violation by such Indemnifying Holder of any rule or regulation

promulgated under the Securities Act applicable to such Indemnifying Holder in connection with any such registration, qualification or compliance, and the Indemnifying Holder will reimburse the Company, such directors and officers and each person controlling Company and each underwriter, if any, for any legal or any other expenses reasonably incurred in connection with investigating, preparing or defending any such claim, loss, damage, liability or action, in each case to the extent, but only to the extent, that such untrue statement (or alleged untrue statement) or omission (or alleged omission) is made in such registration statement, prospectus, offering circular or other document, or any amendment or supplement thereto, incident to any such registration, qualification or compliance, in reliance upon and in conformity with written information furnished to the Company by such Indemnifying Holder expressly for use therein, provided that in no event shall any indemnity under this Section 7.2 exceed the gross proceeds of the offering received by such Indemnifying Holder; and provided further, that the indemnity provided in this Section 7.2 with respect to any losses, claims, damages, liabilities or actions, arising from a sale of Registrable Securities pursuant to a registration hereunder, based upon any untrue statement or alleged untrue statement of material fact or omission or alleged omission to state a material fact in any preliminary or final prospectus (or amendment or supplement thereto) of the Company shall not inure to the benefit of or be available to the Company or any other person if the Holder corrected such untrue statement or alleged untrue statement or omission or alleged omission and sent it to the Company for inclusion in the

prospectus within the time required by the Act and the Rules and Regulations thereto.

7.3 Defense of Claims. Each party entitled to indemnification under this Section 7 (the "Indemnified Party") shall give notice to the party required to provide indemnification (the "Indemnifying Party") promptly after such Indemnified Party has actual knowledge of any claim as to which indemnity may be sought, and shall permit the Indemnifying Party to assume the defense of any such claim or any litigation resulting therefrom, provided that counsel for the Indemnifying Party, who shall conduct the defense of such claim or litigation, shall be approved by the Indemnified Party (whose approval shall not unreasonably be withheld), and the Indemnified Party may participate in such defense at such party's expense; provided, however, that the Indemnifying Party shall pay such expense if representation of the Indemnified Party by counsel retained by the Indemnifying Party would be inappropriate due to actual or potential differing interests between the Indemnified Party and any other party represented by such counsel in such proceeding, and provided further that the failure of any Indemnified Party to give notice as provided herein shall not relieve the Indemnifying Party of its obligations under this Section 7 unless the failure to give such notice is materially prejudicial to an Indemnifying Party's ability to defend such action. No Indemnifying Party, in the defense of any such claim or litigation shall, except with the consent of each Indemnified Party which consent shall not be unreasonably withheld, consent to entry of any judgment or enter into any settlement which does not include as an unconditional term thereof the giving by the claimant or plaintiff to such Indemnified Party of a release from all liability in respect to such claim or litigation and include a statement as to or an admission of fault, culpability or a failure to act by or on behalf of any Indemnified Party. No Indemnifying Party shall be required to indemnify any Indemnified Party with respect to any settlement entered into without such Indemnifying Party's prior written consent.

Section 8
RULE 144 REPORTING

With a view to making available the benefits of certain rules and regulations of the SEC which may at any time permit the sale of the Registrable Securities to the public without registration, the Company agrees to use its reasonable best efforts to:

(a) Make and keep public information available, as those terms are understood and defined in Rule 144 under the Securities Act, at all times from and after ninety (90) days following the effective date of the IPO;

(b) File with the SEC in a timely manner all reports and other documents required of the Company under the Securities Act and the Exchange Act at any time after it has become subject to such reporting requirements; and

(c) So long as a Holder owns any Registrable Securities, furnish to such Holder forthwith upon request a written statement by the Company as to its compliance with the reporting requirements of said Rule 144 (at any time from and after ninety (90) days following the effective date of the IPO), and of the Securities Act and the Exchange Act (at any time after it has become subject to such reporting requirements), a copy of the most recent annual or quarterly report of the Company, and such other reports and documents of the Company, and such other reports and documents so filed as a Holder may reasonably request in availing itself of any rule or regulation of the SEC allowing such Holder to sell any such securities without registration.

Section 9
STANDOFF AGREEMENT

In connection with the Company's Initial Public Offering, if requested by the Company and the managing underwriter, each Holder agrees not to offer to sell or sell, make any short sale of, loan, grant any option for the purchase of, or otherwise dispose of any securities of the Company held by Holder at any time during such period (other than those included in the Initial Public Offering, if any), directly or indirectly, without the prior written consent of the Company or the underwriters for such period of time (not to exceed one-hundred eighty (180) days) as may be requested by the Company and the managing underwriter, provided that all officers, directors and other shareholders of the Company enter into similar agreements. In order to enforce the foregoing, the Company may impose stop-transfer instructions with respect to the Registrable Securities of each Holder (and the share or securities of every other person subject to the foregoing restrictions) until the end of such period.

Section 10
LIMITATIONS ON SUBSEQUENT REGISTRATION RIGHTS

From and after the date of this Agreement, the Company shall not, without the prior written consent of Holder(s) of at least a majority of the outstanding Registrable Securities (excluding Ron Higgins), enter into any agreement with any holder or prospective holder of any securities of the Company giving such holder or prospective holder any registration rights the terms of which are pari passu or more favorable than the registration rights granted to Holders hereunder or to require the Company to effect a registration earlier than the date on which Holders can first require a registration under Section 3.1.

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Section 11
INFORMATION RIGHTS

11.1 Financial Information. The Company shall deliver the following reports or information indicated below to each Holder or any transferee of a Holder who holds, together with Affiliates, at least 500,000 shares of Series A Preferred, Series B Preferred, Series C Preferred, Series D Preferred, Series E Preferred or Registrable Securities (the "Requisite Minimum Shares"):

(a) Monthly Financial Statements. As soon as available, but in any event not later than 30 days after the end of each month (other than the last month of any fiscal year of the Company), the unaudited consolidated balance sheet of the Company and its subsidiaries as at the end of each such month and the related unaudited consolidated statements of income and cash flows of the Company and its subsidiaries for such month and for the elapsed period in such fiscal year, all in reasonable detail and stating in comparative form (i) the figures as of the end of and for the comparable periods of the preceding fiscal year and (ii) the figures reflected in the operating budget for such period as specified in the financial plan of the Company delivered pursuant to subparagraph (d) hereof. All such financial statements shall be certified by the Company's Chief Financial Officer, shall be complete and correct in all material respects, and shall be prepared in accordance with generally accepted accounting principles ("GAAP") applied on a consistent basis throughout the periods reflected therein except as stated therein and subject to normal year-end adjustments.

(b) Quarterly Financial Statements. As soon as available, but in any event not later than 30 days after the end of each quarter (other than the last quarter of any fiscal year of the Company), the unaudited consolidated balance sheet of the Company and its subsidiaries as at the end of each such quarter and the related unaudited consolidated statements of income and cash flows of the Company and its subsidiaries for such quarter and for the elapsed period in such fiscal year, all in reasonable detail and stating in comparative form (i) the figures as of the end of and for the comparable periods of the preceding fiscal year and (ii) the figures reflected in the operating budget for such period as specified in the financial plan of the Company delivered pursuant to subparagraph (c) hereof. All such financial statements shall be certified by the Company's Chief Financial Officer, shall be complete and correct in all material respects, and shall be prepared in accordance with GAAP applied on a consistent basis throughout the periods reflected therein except as stated therein and subject to normal year-end adjustments.

(c) Annual Financial Statements. As soon as available, but in any

event within 90 days after the end of each fiscal year of the Company, a copy of the audited consolidated and consolidating balance sheet of the Company and its subsidiaries as at the end of such fiscal year and the related audited consolidated statements of operations, shareholders' equity and cash flows of the Company and its subsidiaries for such fiscal year, all in reasonable detail and stating in comparative form the figures as at the end of and for the previous fiscal year, accompanied by an opinion of an accounting firm of recognized national standing selected by the Company, which opinion shall state that such accounting firm's audit was conducted in accordance

with generally accepted auditing standards. All such financial statements shall be complete and correct in all material respects and prepared in reasonable detail and in accordance with GAAP applied on a consistent basis throughout the periods reflected therein except as stated therein.

(d) Budgets and Other Information. As soon as available, but in any event not later than 30 days prior to the end of each fiscal year of the Company, the draft financial plan of the Company for the next succeeding fiscal year, and prior to the end of each fiscal year the final draft of such plan, in each such case, including but not limited to a cash flow projection and operating budget, calculated monthly, as contained in its operating plan approved by the Company's Board of Directors as well as any updates or revisions to such plan as soon as available. From time to time, such additional information which is normally prepared by the Company regarding results of operations, financial condition, business or prospects of the Company and its subsidiaries, as a Holder holding the Requisite Minimum Shares may reasonably request.

(e) Other Reports and Statements. Promptly (but in any event within ten days) after any distribution to the Company's shareholders generally, to its directors or to the financial community of an annual report, proxy statement or other report or communication, a copy of each such report, proxy statement or other report or communication and promptly (but in any event within ten days) after any filing by the Company with the SEC or with any national securities exchange or automated quotation system, of any publicly available annual or periodic or special report or proxy statement or registration statement, a copy of such report or statement and copies of all press releases and other statements made available generally by the Company to the public concerning material developments in the Company's business.

11.2 Inspection. The Company shall permit each Holder, at such Holder's expense, to visit and inspect the Company's properties, to examine its

books of account and records and to discuss the Company's affairs, finances and accounts with its officers, with reasonable written notice to the Company and all at such reasonable times as may be requested by such Holder; provided, however, that the Company shall not be obligated pursuant to this Section 11.2 to provide access to any information which it reasonably considers to be a trade secret or similar confidential information. In addition, one representative from each of JAFCO America Ventures, Inc., Partech International, E*Trade Group, Inc., Arbor Investors, L.L.C., and KECALP Inc. (each an "Investor Representative") shall be entitled to attend each meeting of the Company's Board of Directors as an observer, shall be given timely notice of each meeting of the Company's Board of Directors in the same manner and at the same time that directors of the Company are given notice of such meeting and shall have their reasonable out-of-pocket expenses incurred in attending such meetings reimbursed to the same extent and in the same manner as such expenses are reimbursed for the members of the Company's Board of Directors. Each Investor Representative may be changed or replaced from time to time at the discretion of JAFCO America Ventures, Inc., Partech International, E*Trade Group, Inc., Arbor Investors, L.L.C., and KECALP Inc., with respect to each entity's appointed Investor Representative by written notice to the Company.

11.3 Termination of Information and Inspection Covenants. The covenants set forth in Sections 11.1 and 11.2 shall terminate as to each Holder and be of no further force or effect immediately upon the earliest of (a) the consummation of an IPO; (b) at such time as the

Holder fails to own the Requisite Minimum Shares; or (c) when the Company first becomes subject to the periodic reporting requirements of Section 12(g) and 15(d) of the Exchange Act.

11.4 Confidentiality. Each of the Holders agrees to keep confidential and not to disclose to persons other than its employees, professional consultants and advisors any information concerning the Company which is confidential or proprietary ("Confidential Information"), except as otherwise required by law or as deemed necessary by a Holder to be disclosed to its own partners or Affiliates. No Confidential Information shall be used or disclosed by a Holder for any purpose except in connection with the transactions contemplated by the Purchase Agreement and the agreements executed and delivered in connection with the Purchase Agreement and in the enforcement of its rights thereunder. Each Holder shall use no less a level of care with the Confidential Information than it uses with its own confidential information. Notwithstanding the foregoing, the restrictions set forth in this Section 11.4 shall not be applicable to any information that is publicly available through no fault of a

Holder, any information independently developed by a Holder or its professional consultants, any information known to a Holder or its professional consultants before the disclosure thereof by the Company, or any information disclosed to a Holder by a person without any confidentiality duty to the Company. This provision shall survive any termination of this Agreement.

Section 12
RIGHT OF FIRST REFUSAL

The Company hereby grants to each Holder the right of first refusal to purchase, pro rata, a portion of "New Securities" (as defined in this Section 12) that the Company may, from time to time, propose to sell and issue. Each Holder's pro rata share, for purposes of this right of first refusal, is the ratio of (X) the number of shares of Common Stock owned (or issuable upon the conversion of the Series A Preferred, Series B Preferred, Series C Preferred, Series D Preferred or Series E Preferred held) by such Holder immediately after the Closing (as defined in the Purchase Agreement) to (Y) the total number of shares of Common Stock outstanding (or issuable upon the conversion of all outstanding Series A Preferred, Series B Preferred, Series C Preferred, Series D Preferred and Series E Preferred) immediately after the Closing, provided, however, that in the event that any Holder elects not to purchase its pro rata share in accordance with the above (a "Non-Participating Holder"), then each participating Holder purchasing New Securities may purchase, on a pro rata basis among the participating Holders, such Non-Participating Holder's pro rata share. This right of first refusal shall be subject to the following provisions:

(a) "New Securities" shall mean any Common Stock and Preferred Stock of the Company whether or not authorized on the date hereof, and rights, options or warrants to purchase such Common Stock or Preferred Stock, and securities of any type whatsoever that are, or may become, convertible into said Common Stock or Preferred Stock; provided, however, that "New Securities" does not include the following:

(i) shares of Common Stock, or options to purchase shares of Common Stock, issued or granted to directors, employees, vendors or consultants of the Company pursuant to option plans or other employee benefit plans or arrangements approved by

a majority of the Board of Directors of the Company, including the Option Plan (as that term is defined in Section 2.2(c) of the Purchase Agreement);

(ii) shares of Common Stock or other securities issuable upon conversion of the Company's Preferred Stock;

(iii) securities of the Company offered to the public pursuant to a bona fide public offering;

(iv) securities of the Company issued pursuant to an acquisition of or by the Company whether by merger, consolidation or purchase or sale of all or substantially all of the assets of the Company or another entity, or other reorganization;

(v) shares of Common Stock or Preferred Stock issued in connection with any stock split, stock dividend, or recapitalization by the Company; or

(vi) securities of the Company that are purchased pursuant to the rights provided in this Section 12.

(b) In the event that the Company proposes to undertake an issuance of New Securities, it shall give each Holder written notice of its intention, describing the type of New Securities, the price, and the general terms upon which the Company proposes to issue the same. Each Holder shall have ten (10) business days from the date such notice is given to agree to purchase its pro rata share of such New Securities or any portion thereof at the price and upon the general terms specified in the notice by giving written notice to the Company and stating therein the quantity of New Securities to be purchased.

(c) In the event that the Holders' aggregate pro rata exercised portion is less than the amount of New Securities proposed to be issued in the notice referred to above, the Company shall have sixty (60) days thereafter to sell (or enter into an agreement pursuant to which the sale of New Securities covered thereby shall be closed, if at all, within thirty (30) days from the date of such agreement) the New Securities respecting which the Holders' rights were not exercised at a price and upon general terms no more favorable to the purchaser thereof than specified in the Company's notice. In the event the Company has not sold the New Securities within such sixty (60) day period (or sold and issued New Securities in accordance with the foregoing within thirty (30) days from the date of such agreement), the Company shall not thereafter issue or sell any New Securities without first offering such New Securities to the Holders in the manner provided above.

(d) The right of first refusal granted under this Agreement shall terminate upon the first to occur of (i) the effective date of a merger of the Company with or into another corporation in which fifty percent (50%) or more of the voting power of the Company is disposed of, or the sale of all or substantially all of the assets of the Company unless the Company's shareholders, as of the date of this Agreement, control more than fifty percent (50%) of the surviving entity; (ii) the closing date of an IPO; or (iii) the liquidation or dissolution of the Company.

Section 13
TERMINATION OF RIGHTS

Unless otherwise specified herein, the rights and provisions of this Agreement shall terminate as to all Holders on the seventh (7th) anniversary of the date of the Company's seventh Initial Public Offering. The rights of any individual Holder to receive notice and to participate in a registration pursuant to the terms of Section 2 or Section 3 hereof or to request a registration pursuant to the terms of Section 4 hereof shall terminate at such time as such Holder (i) owns less than one percent (1%) of the outstanding Stock of the Company and (ii) could sell all of the Registrable Securities held by such Holder in any one three-month period pursuant to Rule 144 (including Rule 144(k)) under the Securities Act, and in any event, upon the second anniversary of the IPO.

Section 14
MISCELLANEOUS

14.1 Assignment. Subject to compliance with the Purchase Agreement, the rights to cause the Company to register Registrable Securities, the information rights provided in Section 11, and (upon the prior written consent of the Company, not to be unreasonably withheld) the right of first refusal provided in Section 12 granted to the Holders by the Company under this Agreement may be transferred or assigned by the Holders to an Affiliate or may be transferred or assigned by any Holder to a transferee which acquires at least 100,000 Shares of the Registrable Securities (including, for such purposes, the Series A Preferred, the Series B Preferred, the Series C Preferred, the Series D Preferred and the Series E Preferred) owned as of the date of this Agreement by such Holder; provided that the Company is given written notice at the time of or within a reasonable time after said transfer or assignment, stating the name and address of the transferee or assignee and identifying the securities with respect to which such rights are being transferred or assigned, and, provided further, that the transferee or assignee of such rights assumes the obligations of such Holder under this Agreement and agrees to be bound hereby pursuant to a written instrument in form and substance reasonably satisfactory to the Company. Subject to the preceding sentence, this Agreement shall be binding upon and shall inure to the benefit of the parties hereto and their respective successors and assigns. Any transferee or assignee shall thereafter be treated as a Holder in all respects, subject to the limitations herein. Until the Company receives actual notice of any transfer or assignment, it shall be entitled to rely on the then existing list of Holders and the failure to notify the Company of any transfer or assignment shall not affect the validity of a notice properly given

by the Company to the Holders pursuant to lists maintained by the Company.

14.2 Aggregation of Shares. All shares of Registrable Securities held
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or acquired by affiliated entities or persons, including without limitation, Affiliates, shall be aggregated together for the purpose of determining the availability of any rights under this Agreement.

14.3 Governing Law. This Agreement shall be governed by and construed
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under the laws of the State of California as applied to agreements entered into solely between residents of and to be performed entirely within, such state.

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14.4 Counterparts. This Agreement may be executed in two or more
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counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

14.5 Titles and Subtitles. The titles and subtitles used in this
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Agreement are used for convenience only and are not to be considered in construing or interpreting this Agreement.

14.6 Notices. All notices, requests, demands and other communications
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under this Agreement or in connection herewith shall be given to or made upon the Holder at the addresses set forth in the Company's records and, if to the Company, at the address previously furnished by the Company to the Holders, addressed to the attention of the President.

(a) All notices, requests, demands and other communications given or made in accordance with the provisions of this Agreement shall be in writing, and shall be sent by airmail, return receipt requested, or by facsimile with confirmation of receipt, and shall be deemed to be given or made when receipt is so confirmed.

(b) Any party may, by written notice to the other, alter its address or respondent, and such notice shall be considered to have been given three (3) days after the airmailing or faxing thereof.

14.7 Attorneys' Fees. If any action at law or in equity (including
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arbitration) is necessary to enforce or interpret the terms of this Agreement, the prevailing party shall be entitled to reasonable attorneys' fees, costs and necessary disbursements in addition to any other relief to which such party may be entitled.

14.8 Amendments and Waivers. Any term of this Agreement may be amended
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or any right hereunder waived with the written consent of the Company and the Holders of 66-2/3% of the outstanding Series A Preferred, Series B Preferred, Series C Preferred, Series D Preferred, Series E Preferred and Registrable Securities. Any amendment or waiver effected in accordance with this Section 14.8 shall be binding upon the Holders and each transferee of the Registrable Securities, each future holder of all such Registrable Securities and the Company.

14.9 Severability. If one or more provisions of this Agreement are
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held to be unenforceable under applicable law, portions of such provisions, or such provisions in their entirety, to the extent necessary, shall be severed from this Agreement, and the balance of the Agreement shall be interpreted as if such provision were so excluded and shall be enforceable in accordance with its terms.

14.10 Delays or Omissions. No delay or omission to exercise any
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right, power or remedy accruing to any party to this Agreement, upon any breach or default of the other party, shall impair any such right, power or remedy of such non-breaching party nor shall it be construed to be a waiver of any such breach or default, or an acquiescence therein, or of any similar breach or default thereafter occurring; nor shall any waiver of any single breach or default be deemed a waiver of any other breach or default theretofore or thereafter occurring. Any waiver, permit, consent or approval of any kind or character on the part of any party of any breach or default under this Agreement, or any waiver on the part of any party of any provisions

or conditions of this Agreement, must be made in writing and shall be effective only to the extent specifically set forth in such writing. All remedies, either under this Agreement, or by law or otherwise afforded to any Holder, shall be cumulative and not alternative.

14.11 Entire Agreement; Superseding Effect. This Agreement and the
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documents referred to herein constitute the entire agreement between the parties hereto pertaining to the subject matter hereof and any other written or oral agreements between the parties hereto pertaining thereto are expressly canceled. This Agreement amends and restates the Existing Rights Agreement in its entirety, and the Existing Rights Agreement shall be deemed terminated upon the execution of this Agreement by the Company and the Holders of a majority of the Series A Preferred, Series B Preferred, Series C Preferred and Series D Preferred (and Common Stock issuable upon conversion thereof) party thereto.

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IN WITNESS WHEREOF, the parties have caused this Amended and Restated Investors' Rights Agreement to be executed as of the date first written above.

"Company" "Holders"

DIGITAL ISLAND, INC.

By: By:

Name: Name:

Title: Title:

AMENDED AND RESTATED INVESTORS' RIGHTS AGREEMENT
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EXHIBIT 10.4

DIGITAL ISLAND, INC.

INDEMNIFICATION AGREEMENT

THIS INDEMNIFICATION AGREEMENT (this "Agreement") is made and entered into this ___ day of _____, 1999, between Digital Island, Inc., a Delaware corporation (the "Company"), and _____ ("Indemnitee").

WHEREAS, Indemnitee, a member of the Board of Directors or an officer, employee or agent of the Company, performs a valuable service in such capacity for the Company;

WHEREAS, the stockholders of the Company have adopted Bylaws (the "Bylaws") providing for the indemnification of the officers, directors, employees and agents of the Company to the maximum extent authorized by Section 145 of the Delaware General Corporation Law, as amended (the "Code");

WHEREAS, the Bylaws and the Code, by their non-exclusive nature, permit contracts between the Company and the members of its Board of Directors, officers, employees or agents with respect to indemnification of such directors, officers, employees or agents;

WHEREAS, in accordance with the authorization as provided by the Code, the Company either has purchased and presently maintains or intends to purchase and maintain a policy or policies of Directors and Officers Liability Insurance ("D & O Insurance") covering certain liabilities which may be incurred by its directors and officers in the performance of their duties as directors and officers of the Company;

WHEREAS, as a result of developments affecting the terms, scope and availability of D & O Insurance there exists general uncertainty as to the extent of protection afforded members of the Board of Directors or officers, employees or agents by such D & O Insurance and by statutory and bylaw indemnification provisions; and

WHEREAS, in order to induce Indemnitee to continue to serve as a member of the Board of Directors, officer, employee or agent of the Company, the Company has determined and agreed to enter into this contract with Indemnitee.

NOW, THEREFORE, in consideration of Indemnitee's continued service as a director, officer, employee or agent after the date hereof, and for other good and valid consideration, the receipt and adequacy of which is hereby acknowledged, the parties hereto agree as follows:
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1. Indemnification of Indemnitee. The Company hereby agrees to hold harmless and indemnify Indemnitee to the fullest extent authorized or permitted by the provisions of the Code, as may be amended from time to time.

2. Additional Indemnity. Subject only to the exclusions set forth in Sections 3 and 6(c) hereof, the Company hereby further agrees to hold harmless and indemnify Indemnitee:

(a) against any and all expenses (including attorneys' fees),

witness fees, judgments, fines and amounts paid in settlement actually and reasonably incurred by Indemnitee in connection with any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (including an action by or in the right of the Company) to which Indemnitee is, was or at any time becomes a party, or is threatened to be made a party, by reason of the fact that Indemnitee is, was or at any time becomes a director, officer, employee or agent of the Company or any subsidiary of the Company, or is or was serving or at any time serves at the request of the Company as a director, officer, employee or agent of another corporation, partnership, joint venture, trust, employee benefit plan or other enterprise; and

(b) otherwise to the fullest extent as may be provided to Indemnitee by the Company under the non-exclusivity provisions of Article VII, Section 6 of the Bylaws of the Company and the Code.

3. Limitations on Additional Indemnity.

(a) No indemnity pursuant to Section 2 hereof shall be paid by the Company:

i) in respect to remuneration paid to Indemnitee if it shall be determined by a final judgment or other final adjudication that such remuneration was in violation of law;

ii) on account of any suit in which judgment is rendered against Indemnitee for an accounting of profits made from the purchase or sale by Indemnitee of securities of the Company pursuant to the provisions of Section 16(b) of the Securities Exchange Act of 1934 and amendments thereto or similar provisions of any federal, state or local statutory law;

iii) on account of Indemnitee's conduct which is finally adjudged to have been knowingly fraudulent or deliberately dishonest or to constitute willful misconduct;

iv) on account of Indemnitee's conduct which is the subject of an action, suit or proceeding described in Section 6(c)(ii) hereof;

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v) on account of any action, claim or proceeding (other than a proceeding referred to in Section 7(b) hereof) initiated by the Indemnitee unless such action, claim or proceeding was authorized in the specific case by action of the Board of Directors;

vi) if a final decision by a Court having jurisdiction in the

matter shall determine that such indemnification is not lawful (and, in this respect, both the Company and Indemnitee have been advised that the Securities and Exchange Commission believes that indemnification for liabilities arising under the federal securities laws is against public policy and is, therefore, unenforceable and that claims for indemnification should be submitted to appropriate courts for adjudication); and

vii) except to the extent the aggregate of losses to be indemnified thereunder exceeds the sum of (a) such losses for which the Indemnitee is indemnified pursuant to Section 1 hereof and (b) any additional amount paid to the Indemnitee pursuant to any D & O Insurance purchased and maintained by the Company.

(b) No indemnity pursuant to Section 1 or 2 hereof shall be paid by the Company if the action, suit or proceeding with respect to which a claim for indemnity hereunder is made arose from or is based upon any of the following:

i) Any solicitation of proxies by Indemnitee, or by a group of which he was or became a member consisting of two or more persons that had agreed (whether formally or informally and whether or not in writing) to act together for the purpose of soliciting proxies, in opposition to any solicitation of proxies approved by the Board of Directors.

ii) Any activities by Indemnitee that constitute a breach of or default under any agreement between Indemnitee and the Company.

4. Contribution. If the indemnification provided in Sections 1 and 2 hereof is unavailable by reason of a Court decision described in Section 3(a)(vi) hereof based on grounds other than any of those set forth in paragraphs (i) through (v) of Section 3 (a) hereof, then in respect of any threatened, pending or completed action, suit or proceeding in which the Company is jointly liable with Indemnitee (or would be if joined in such action, suit or proceeding), the Company shall contribute to the amount of expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred and paid or payable by Indemnitee in such proportion as is appropriate to reflect (i) the relative benefits received by the Company on the one hand and Indemnitee on the other hand from the transaction from which such action, suit or proceeding arose, and (ii) the relative fault of the Company on the one hand and of Indemnitee on the other in connection with the events which resulted in such expenses, judgments, fines or settlement amounts, as well as any other relevant equitable considerations. The relative fault of the Company on the one hand and of Indemnitee on the other shall be determined by reference to, among other things, the parties' relative intent, knowledge, access to information and opportunity to correct

or prevent the circumstances resulting in such expenses, judgments, fines or settlement amounts. The Company agrees that it would not be just and equitable if contribution pursuant to this Section 4 were determined by pro rata allocation or any other method of allocation which does not take account of the foregoing equitable considerations.

5. Notification and Defense of Claim. Not later than thirty (30) days after receipt by Indemnitee of notice of the commencement of any action, suit or proceeding, Indemnitee shall, if a claim in respect thereof is to be made against the Company under this Agreement, notify the Company of the commencement thereof; but Indemnitee's omission so to notify the Company will not relieve the Company from any liability which it may have to Indemnitee otherwise than under this Agreement. With respect to any such action, suit or proceeding as to which Indemnitee notifies the Company of the commencement thereof:

(a) The Company will be entitled to participate therein at its own expense.

(b) Except as otherwise provided below, to the extent that it may wish, the Company shall, jointly with any other indemnifying party similarly notified, be entitled to assume the defense thereof, with counsel reasonably satisfactory to Indemnitee. After notice from the Company to Indemnitee of its election to assume the defense thereof, the Company will not be liable to Indemnitee under this Agreement for any legal or other expenses subsequently incurred by Indemnitee in connection with the defense thereof, other than reasonable costs of investigation or as otherwise provided below. Indemnitee shall have the right to employ its own counsel in such action, suit or proceeding, but the fees and expenses of such counsel incurred after notice from the Company of the Company's assumption of the defense thereof shall be at the expense of Indemnitee unless (i) the employment of counsel by Indemnitee has been authorized by the Company; (ii) Indemnitee shall have reasonably concluded that there may be a conflict of interest between the Company and Indemnitee in the conduct of the defense of such action; or (iii) the Company shall not in fact have employed counsel to assume the defense of such action; in each of which cases the fees and expenses of Indemnitee's separate counsel shall be paid by the Company. The Company shall not be entitled to assume the defense of any action, suit or proceeding brought by or on behalf of the Company or as to which Indemnitee shall have made the conclusion provided for in (ii) above.

(c) The Company shall not be liable to indemnify Indemnitee under this Agreement for any amounts paid in settlement of any action or claim effected without its written consent. The Company shall be permitted to settle any action except that it shall not settle any action or claim in any manner which would impose any penalty or limitation on Indemnitee without Indemnitee's written consent. Neither the Company nor Indemnitee will unreasonably withhold its consent to any proposed settlement.

6. Advancement and Repayment of Expenses.

(a) In the event that Indemnitee employs his or her own counsel pursuant to Sections 5(b)(i) through (iii) above, the Company shall advance to Indemnitee, prior to any final disposition of any threatened or pending action, suit or proceeding, whether civil, criminal, administrative or investigative, any and all reasonable expenses (including legal fees and expenses) incurred in investigating or defending any such action, suit or proceeding within ten (10) days after receiving from Indemnitee copies of invoices presented to Indemnitee for such expenses.

(b) Indemnitee agrees that Indemnitee will reimburse the Company for all reasonable expenses paid by the Company in investigating or defending any civil or criminal action, suit or proceeding against Indemnitee in the event and only to the extent it shall be ultimately determined by a final judicial decision (from which there is no right of appeal) that Indemnitee is not entitled, under the provisions of the Code, the Bylaws, this Agreement or otherwise, to be indemnified by the Company for such expenses.

(c) Notwithstanding the foregoing, the Company shall not be required to advance such expenses to Indemnitee in respect of any action arising from or based upon any of the matters set forth in subsection (b) of Section 3 or if Indemnitee (i) commences any action, suit or proceeding as a plaintiff unless such advance is specifically approved by a majority of the Board of Directors or (ii) is a party to an action, suit or proceeding brought by the Company and approved by a majority of the Board which alleges willful misappropriation of corporate assets by Indemnitee, disclosure of confidential information in violation of Indemnitee's fiduciary or contractual obligations to the Company, or any other willful and deliberate breach in bad faith of Indemnitee's duty to the Company or its shareholders.

7. Enforcement.

(a) The Company expressly confirms and agrees that it has entered into this Agreement and assumed the obligations imposed on the Company hereby in order to induce Indemnitee to continue as a director, officer, employee or other agent of the Company, and acknowledges that Indemnitee is relying upon this Agreement in continuing in such capacity.

(b) In the event Indemnitee is required to bring any action to enforce rights or to collect moneys due under this Agreement and is successful in such action, the Company shall reimburse Indemnitee for all Indemnitee's reasonable fees and expenses, including attorney's fees, in bringing and

pursuing such action.

8. Subrogation. In the event of payment under this agreement, the
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Company shall be subrogated to the extent of such payment to all of the rights of recovery of Indemnitee, who shall execute all documents required and shall do all acts that may be

necessary to secure such rights and to enable the Company effectively to bring suit to enforce such rights.

9. Continuation of Obligations. All agreements and obligations of
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the Company contained herein shall commence upon the date that Indemnitee first became a member of the Board of Directors or an officer, employee or agent of the Company, as the case may be, and shall continue during the period Indemnitee is a director, officer, employee or agent of the Company (or is or was serving at the request of the Company as a director, officer, employee or agent of another corporation, partnership, joint venture, trust, employee benefit plan or other enterprise) and shall continue thereafter so long as Indemnitee shall be subject to any possible claim or threatened, pending or completed action, suit or proceeding, whether civil, criminal or investigative, by reason of the fact that Indemnitee was a director, officer, employee or agent of the Company or serving in any other capacity referred to herein.

10. Survival of Rights. The rights conferred on Indemnitee by this
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Agreement shall continue after Indemnitee has ceased to be a director, officer, employee or other agent of the Company and shall inure to the benefit of Indemnitee's heirs, executors and administrators.

11. Non-Exclusivity of Rights. The rights conferred on Indemnitee by
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this Agreement shall not be exclusive of any other right which Indemnitee may have or hereafter acquire under any statute, provision of the Company's Certificate of Incorporation or Bylaws, agreement, vote of stockholders or directors, or otherwise, both as to action in his official capacity and as to action in another capacity while holding office; provided, however, that this Agreement shall supersede and replace any prior indemnification agreements entered into by and between the Company and Indemnitee and that any such prior indemnification agreement shall be terminated upon the execution of this Agreement.

12. Separability. Each of the provisions of this Agreement is a
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separate and distinct agreement and independent of the others, so that if any or

all of the provisions hereof shall be held to be invalid or unenforceable for any reason, such invalidity or unenforceability shall not affect the validity or enforceability of the other provisions hereof or the obligation of the Company to indemnify the Indemnitee to the full extent provided by the Bylaws or the Code.

13. Governing Law. This Agreement shall be interpreted and enforced in accordance with the laws of the State of Delaware.

14. Binding Effect. This Agreement shall be binding upon Indemnitee and upon the Company, its successors and assigns, and shall inure to the benefit of Indemnitee, his or her heirs, personal representatives and assigns and to the benefit of the Company, its successors and assigns.

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15. Amendment and Termination. No amendment, modification, termination or cancellation of this Agreement shall be effective unless it is in writing and is signed by both parties hereto.

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

DIGITAL ISLAND, INC.
a Delaware corporation

By: _____
T.L. Thompson, Secretary

INDEMNITEE

By: _____

Name: _____

Address: _____

_____

_____

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EXHIBIT 10.5

EMPLOYMENT AGREEMENT

EMPLOYMENT AGREEMENT made as of the 20th day of May, 1998 by and between DIGITAL ISLAND, a California corporation (the "Corporation"), and Ruann Ernst ("Executive").

WHEREAS, the Corporation and Executive wish to enter into a formal employment contract which will govern the terms and conditions applicable to Executive's employment with the Corporation and will provide certain severance benefits for Executive in the event her employment should be involuntarily terminated.

NOW, THEREFORE, the parties hereto agree as follows:

PART ONE-- TERMS AND CONDITIONS OF EMPLOYMENT

1. DUTIES AND RESPONSIBILITIES.

A. Executive shall serve as the Chief Executive Officer of the Corporation and shall in such capacity report directly to the Corporation's Board of Directors (the "Board"). As Chief Executive Officer, Executive shall have primary responsibility for the formulation, implementation and execution of strategic policies relating to the Corporation's business operations, financial objectives and market growth and shall accordingly have overall responsibility for the formulation of the business plan for each fiscal year to be submitted for Board approval. Executive shall be appointed to the Board of the Directors (the "Board") at the time she commences service as President and Chief Executive Officer, and her membership on the Board shall continue during the period of this Agreement while the Corporation remains privately held. Once the Corporation is publicly held, the Corporation shall use its best efforts to maintain Executive on the Board throughout the remainder of her period of employment with the Corporation as Chief Executive Officer by taking all action necessary to nominate Executive for election to the Board at each shareholders

meeting held during her period of service as Chief Executive Officer at which Board members are to be elected.

B. Executive hereby agrees to remain in such executive capacity during the employment period specified in Paragraph 2 and to perform in good faith and to the best of her ability all services which may be required of Executive hereunder and to be available to render services at all reasonable times and places in accordance with such reasonable directions and requests made by the Corporation acting by majority vote of the Board.

C. Executive shall, during the term hereof, devote her full time, ability, energy and skill to the performance of her duties and responsibilities hereunder. Executive shall be based at the Corporation's principal offices in the San Francisco/Bay Area, California, but Executive shall be required to travel to other geographic locations in connection with the performance of her executive duties hereunder.

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2. PERIOD OF EMPLOYMENT. Executive's employment with the Corporation
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shall be governed by the provisions of this Agreement for the period commencing June 1, 1998 and continuing until this Agreement is terminated in accordance with the provisions of Paragraph 10. The period during which Executive's employment continues in effect shall be hereafter referred to as the "Employment Period."

3. CASH COMPENSATION.

A. Executive shall be paid a base salary at the annual rate of not less than One Hundred Fifty Thousand Dollars ($150,000.00). Such rate shall be subject to annual review by the Board and may be increased at the Board's discretion. Base salary shall be paid at periodic intervals in accordance with the Corporation's payroll practices for salaried employees.

B. For each fiscal year of the Corporation during the Employment Period, beginning with the 1999 fiscal year commencing October 1, 1998, Executive shall be entitled to incentive compensation in an amount not less than forty percent (40%) of her base salary which is to become payable upon the Corporation's achievement of the financial objectives and performance milestones mutually agreed upon by the Board and Executive for each such year. For the period June 1, 1998 to September 30, 1998, the target bonus shall be Twenty Thousand Dollars ($20,000.00) to become payable upon the Corporation's achievement of the financial milestones mutually agreed upon by the Board and Executive.

C. The Corporation shall deduct and withhold from the compensation payable to Executive hereunder any and all applicable Federal, State and local

income and employment withholding taxes and any other amounts required to be deducted or withheld by the Corporation under applicable statutes, regulations, ordinances or orders governing or requiring the withholding or deduction of amounts otherwise payable as compensation or wages to employees.

4. EQUITY COMPENSATION

A. Effective immediately upon Executive' s commencement of employment on or before June 1, 1999, Executive shall be granted two separate stock options to acquire shares of the Corporation's common stock (the "Common Stock"). The first option will cover 635,327 shares of Common Stock (representing four percent (4%) of the Corporation's currently outstanding equity securities on a fully-diluted basis), and the second option will cover 158,832 shares of Common Stock (representing an additional one percent (1%) of the Corporation's currently outstanding equity securities on a fully-diluted basis). Each option will have an exercise price per share of $1.50, the current fair market value per share of Common Stock as determined by the Board.

B. The first option will be an incentive stock option for 333,333 shares and a non-statutory option for the balance of the shares. The second option will be a non-statutory option for all 158,832 shares. Each option will have a term of ten (10) years, subject to earlier termination upon Executive's termination of employment with the Corporation.

C. The incentive stock option will be immediately exercisable for 66,666 shares and will become exercisable for the remaining shares in a series of four (4) successive equal annual installments on the first trading day in January in each of the 1999 through 2002 calendar years. Each of the non-statutory options will be immediately exercisable for all the option shares. All shares purchased under the incentive stock and non-statutory options and unvested at the time of Executive's termination of employment with the Corporation will be subject to repurchase by the Corporation at the exercise price paid per share. Executive shall vest in the shares subject to the four percent (4%) option (both the incentive stock option and non-statutory stock option components) in a series of fifty (50) successive equal monthly installments upon her completion of each of her first fifty (50) months of employment with the Corporation. Executive shall vest in the shares subject to the one percent (1%) option in a series of fifty (50) successive equal monthly installments upon her completion of each month of employment over the fifty (50)-month period beginning one year after the grant date of such option. Except as otherwise provided in Paragraphs 4.D and 11, no additional shares will vest after Executive's termination of employment with the Corporation.

D. In the event of a Change in Control, all of the shares subject to your two stock options will immediately vest, unless the acquiring entity

assumes those options. Should those options be assumed, then the shares subject to those options will vest on accelerated basis in accordance with the following terms:

- Should there occur an Involuntary Termination of Executive's employment with the Corporation (or the successor entity) within eighteen (18) months after the effective date of the Change in Control, then all the option shares shall immediately vest at that time.

- Should Executive voluntarily resign from employment (other than in connection with an event which constitutes grounds for an Involuntary Termination) within six (6) months after the effective date of the Change in Control, then Executive shall immediately vest in the lesser of (i) fifty percent (50%) of the
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total number of shares for which the two options were granted or (ii) the total number of unvested shares at the time subject to the two options.

D. For purposes of this Agreement, the following definitions shall be in effect'

CHANGE IN CONTROL shall mean any of the following transactions
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effecting a change in ownership or control of the Corporation:

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(i) a merger, consolidation or reorganization approved by the Corporation's stockholders, unless securities
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representing more than fifty percent (50%) of the total combined voting power of the voting securities of the successor corporation are immediately thereafter beneficially owned, directly or indirectly and in substantially the same proportion, by the persons who beneficially owned the Corporation's outstanding voting securities immediately prior to such transaction, or

(ii) any stockholder-approved transfer or other disposition of all or substantially all of the Corporation's assets, or

(iii) the acquisition, directly or indirectly by any person or related group of persons (other than the Corporation or a person that directly or indirectly controls, is controlled by, or is under common control with, the Corporation), of beneficial

ownership (within the meaning of Rule 13d-3 of the 1934 Act) of securities possessing more than fifty percent (50%) of the total combined voting power of the Corporation's outstanding securities pursuant to a tender or exchange offer made directly to the Corporation's stockholders.

In no event, however, shall a Change in Control be deemed to occur in connection with any public offering of the Common Stock.

INVOLUNTARY TERMINATION shall mean (i) the involuntary termination of Executive's employment with the Corporation other than a termination for Cause or (ii) Executive's voluntary resignation within ninety (90) days following (A) a material reduction in the scope of her duties and responsibilities or the level of management to which she reports, (B) a reduction in her level of base salary or (C) a relocation of her principal place of employment by more than fifty (50) miles. Involuntary Termination shall not include the termination of Executive's employment by reason of death or Disability.

CAUSE shall have the meaning assigned to such term in Paragraph 10.C of this Agreement.

5. EXPENSE REIMBURSEMENT. In addition to the compensation specified in Paragraph 3, Executive shall be entitled, in accordance with the reimbursement policies in effect from time to time, to receive reimbursement from the Corporation for all business expenses incurred by Executive in the performance of her duties hereunder, provided Executive furnishes the Corporation with vouchers, receipts and other details of such. expenses in the form required by the Corporation sufficient to substantiate a deduction for such business expenses under all applicable roles and regulations of federal and state taxing authorities.

D. FRINGE BENEFITS.

A. Executive shall, throughout the Employment Period, be eligible to participate in all group term life insurance plans, group health plans, accidental death and dismemberment plans and short-term disability programs and other executive perquisites which are made available to the Corporation's executives and for which Executive qualifies.

B. Executive shall accrue paid vacation benefits during the Employment Period at the rate of one (1) week per calendar quarter and may take

her accrued vacation at such times as are mutually convenient to Executive and the Corporation.

6. DEATH OR DISABILITY. Upon Executive's death or Disability during the Employment Period, the employment relationship created pursuant to this Agreement shall immediately terminate, and no further compensation shall become payable to Executive pursuant to Paragraph 3. In connection with such termination, the Corporation shall only be required to pay Executive or her estate (i) any unpaid base salary earned under Paragraph 3 for services rendered through the date of her death or Disability, (ii) the dollar value of all accrued and unused vacation benefits based upon Executive's most recent level of base salary and (iii) any incentive compensation which becomes due and payable for the calendar year of the Executive's death or Disability, pro-rated in amount on the basis of the portion of that year completed prior to Executive's death or Disability. No additional shares purchased or purchasable under the stock options granted to Executive pursuant to Paragraph 4 shall vest following the termination of the employment relationship by reason of Executive's death or Disability. However, should Executive die within the first six (6) months of the Employment Period after having purchased at least One Hundred Thousand (100,000) shares of Common Stock pursuant to her stock options under Paragraph 4, then a portion of those shares shall immediately vest upon her death. The portion which shall so vest shall be equal to One Hundred Thousand (100,000) shares less Twelve Thousand Seven Hundred and Eight (12,708) shares for each full calendar month of employment completed by Executive during the Employment Period.

For purposes of this Paragraph 6, Disability shall mean the Executive's inability, by reason of any physical or mental injury or illness, to substantially perform the services required of her hereunder for a period in excess of one hundred eighty (180) consecutive days. In such event, Executive shall be deemed to have terminated employment by reason of Disability on the last day of such one hundred eighty (180)-day period.

7. RESTRICTIVE COVENANTS. During the Employment Period'

(i) Executive shall devote Executive's full time and energy solely and exclusively to the performance of Executive's duties described herein, except during periods of illness or vacation periods.

(ii) Executive shall not directly or indirectly provide services to or through any person, firm or other entity except the Corporation, unless otherwise authorized by the Board in writing. However, Executive may continue to serve during the Employment Period as a non-employee member of the board of

directors of any companies for which she so serves on the effective date of this Agreement and may join the board of directors of other companies in the future with the Board's consent.

(iii) Executive shall not render any services of any kind or character for Executive's own account or for any other person, firm or entity without first obtaining the Corporation's written consent.

However, Executive shall have the right to perform such incidental services as are necessary in connection with (a) Executive's private passive investments, but only if Executive is not obligated or required to (and shall not in fact) devote any managerial efforts which interfere with the services required to be performed by her hereunder, or (b) Executive's charitable or community activities, or participation in trade or professional organizations, but only if such incidental services do not interfere with the performance of Executive's services hereunder.

8. NON-COMPETITION. During any period for which Executive is receiving payments from the Corporation, either pursuant to Paragraph 3 of this Part One or Paragraph 11 of Part Two of this Agreement, Executive shall not directly or indirectly:

(i) own, manage, operate, join, control or participate in the ownership, management, operation or control of, or be employed by or connected in any manner with, any enterprise which is engaged in any business competitive with or similar to that of the Corporation; provided, however, that such restriction shall not apply to any passive investment representing an interest of less than two percent (2%) of an outstanding class of publicly-traded securities of any corporation or other enterprise which is not, at the time of such investment, engaged in a business competitive with the Corporation's business; or

(ii) encourage or solicit any of the Corporation's employees to leave the Corporation's employ for any reason or interfere in any other manner with employment relationships at the time existing between the Corporation and its employees; or

(iii) solicit any client of the Corporation, induce any ofthe Corporation's clients to terminate its existing business relationship with the Corporation or interfere in any other manner with any existing business relationship between the Corporation and any client or other third party.

Executive hereby acknowledges that monetary damages may not be sufficient to compensate the Corporation for any economic loss which may be incurred by reason of her breach of the foregoing restrictive covenants. Accordingly, in the event of any such breach, the Corporation shall, in addition to the termination of this Agreement and any remedies available to the Corporation at law, be entitled to obtain equitable relief in the form of an injunction precluding Executive from continuing such breach.

9. PROPRIETARY INFORMATION.

A. Executive hereby acknowledges that the Corporation may, from time to time during the Employment Period, disclose to Executive confidential information pertaining to the Corporation's business and affairs, technology, research and development projects and client base, including (without limitation) financial information concerning clients and prospective business opportunities. All information and data, whether or not in writing, of a private or confidential nature concerning the business, technology or financial affairs of the Corporation and its clients (collectively, "Proprietary Information") is and shall remain the sole and exclusive property of the Corporation. By way of illustration, but not limitation, Proprietary Information shall include all trade secrets, research and development projects, financial records, business plans, personnel data, computer programs and client lists and accounts relating to the business operations, technology or financial affairs of the Corporation, other similar items indicating the source of the Corporation's revenue, all information pertaining to the salaries, duties and performance ratings of the Corporation's employees and all financial information relating to the Corporation's clients and their proposed or contemplated business transactions.

B. Executive shall not, at any time during or after such Employment Period, disclose to any third party or directly or indirectly make use of any such Proprietary Information, other than in connection with the Corporation's business and affairs.

C. All files, letters, memoranda, reports, records, data or other written, reproduced or other tangible manifestations of the Proprietary Information, whether created by Executive or others, to which the Executive has access during the Employment Period shall be used by Executive only in the performance of her duties hereunder. All such materials (whether written, printed or otherwise reproduced or recorded) shall be returned by Executive to the Corporation immediately upon the termination of the Employment Period or upon any earlier request by the Corporation, without Executive retaining any copies, notes or excerpts thereof.

D. Executive's obligation not to disclose or use Proprietary

Information shall also extend to any and all information, records, trade secrets, data and other tangible property of the Corporation clients or any other third parties who may .have disclosed or entrusted the same to the Corporation or Executive in connection with the Corporation's business operations.

E. Executive's obligations under this Paragraph 9 shall continue in effect after the termination of her employment with the Corporation, whatever the reason or reasons for such termination, and the Corporation shall have the right to communicate with any future or prospective employer of Executive concerning Executive's continuing obligations under this Paragraph 9.

10. TERMINATION OF EMPLOYMENT.

A. The Corporation, acting by majority vote of the Board, may terminate Executive's employment under this Agreement at any time for any reason, with or without cause, by giving at least sixty (60) days prior written notice of such termination to the Executive. However, such sixty (60)-day notice requirement shall not apply to the termination of Executive's employment for Cause under Paragraph C below. If such termination notice is given to Executive, the Corporation may, if it so desires, immediately relieve Executive of some or all of her duties.

B. Executive may terminate her employment under this Agreement at anytime by giving the Corporation at least sixty (60) days prior written notice of such termination.

C. The Corporation, acting by majority vote of the Board, may at any time, upon written notice, terminate the Executive's employment with the Corporation hereunder for Cause. Such termination shall be effective Immediately upon such notice. For purposes of this Agreement, termination for Cause shall mean the termination of the Executive's employment for any of the following reasons: (i) Executive's conviction of a felony or her embezzlement of the Corporation's funds, (ii) a material breach by Executive of one or more of her obligations under Paragraph 7, 8 or 9 of this Agreement, (iii) any intentional misconduct by Executive which has a materially adverse effect upon the Corporation's business or reputation, (iv) Executive's material dereliction of the major duties, functions and responsibilities of her executive position after written warning from the Corporation or (v) a material breach by Executive of any of Executive's fiduciary obligations as an officer of the Corporation. However, prior to any termination of Executive's employment for a Cause event defined in clauses (ii) through (v), the Corporation shall give written notice to Executive of the actions or omissions deemed to constitute the Cause event, and Executive shall have a period of thirty (30) days in which to cure the specified default in her performance.

D. Upon the termination of Executive's employment for any reason during the Employment Period, Executive shall be paid all salary and unused vacation earned through the date of such termination. The following provisions shall govern the treatment of Executive's outstanding stock options and unvested shares upon her termination of employment:

- If Executive' s employment is terminated for Cause or should Executive voluntarily resign from employment (other than in connection with an event which constitutes grounds for an Involuntary Termination), then all vesting in Executive's outstanding stock options and unvested shares shall cease at the time of such termination.

- If there is an Involuntarily Termination of Executive's employment, then the provisions of Paragraph 12 of this Agreement shall be controlling.

- Executive shall not have more than a three (3)-month period (twelve (12)-months in the event of death or disability) following the termination of her employment for any reason in which to exercise any outstanding options for the Corporation's common stock which are vested and exercisable at the time of such termination of employment.

PART TWO -- SEVERANCE BENEFITS

11. BENEFIT ENTITLEMENT. Executive shall be entitled to receive the severance benefits specified in Paragraph 12 in the event of an Involuntarily Termination (as such term is defined in Paragraph 4.D) during the Employment Period. Under no circumstances shall any severance benefits be payable pursuant to this Part Two if Executive's employment is terminated for Cause (as such term is defined in Paragraph 10.C).

12. NATURE OF SEVERANCE BENEFITS. The severance benefits payable to Executive under this Part Two shall consist of the following:

(a) Salary Continuation. Executive shall receive salary continuation payments, at the monthly rate of base salary in effect for her under Paragraph 3 at the time of her Involuntary Termination, for a period of six (6) months. Such salary continuation payments shall be made at semi-monthly intervals on the 15th and last day of each calendar month and shall be subject to all applicable withholding requirements as set forth in Paragraph 3.D.

(b) Incentive Compensation. Executive shall be entitled to fifty
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percent (50%) of the dollar amount of any incentive compensation which would have actually become payable to her on the basis of the Corporation's financial performance for the fiscal year in which such Involuntary Termination occurs, had she continued in employ through the end of that fiscal year. Payment shall be made within ninety (90) days after the close of such fiscal year.

(c) Health Care Coverage. Continued health care coverage under
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the Corporation's medical plan shall be provided, without charge, to Executive and her eligible dependents upon her election to receive such continued health care coverage under Internal Revenue Code Section 4980B ("COBRA"). Such Corporation-paid coverage shall continue until

the earlier of (i) the expiration of the six (6)-month period measured from the
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effective date of her Involuntary Termination or (ii) the first date on which Executive is covered under another employer's health benefit program without exclusion for any pre-existing medical condition. Any additional health care coverage to which Executive and her dependents may be entitled under COBRA following the period of such Corporation-paid coverage shall be at Executive's sole cost and expense.

(d) Partial Option Acceleration. The vesting schedules in
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effect under Paragraph 4.C for the shares of Common Stock purchased or purchasable under the stock options granted to Executive under Paragraph 4 will be accelerated by six (6) months. Executive shall have until the earlier of (i)
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the expiration of the option term or (ii) the end of the three (3)-month period following the date of such Involuntary Termination in which to exercise her options for any or all of those vested option shares.

The benefits provided Executive under Paragraph 10 or Paragraph 11 are the only severance benefits to which Executive is entitled upon the termination of her employment with the Corporation, and no other benefits shall be provided to Executive by the Corporation pursuant to any other severance plan or program of the Corporation.

13. CESSATION OF SEVERANCE BENEFITS. In the event Executive breaches
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any of her obligations under Paragraph 7, 8 or 9 of this Agreement, no further severance benefits under this Part Two shall become due and payable to her

14. DEATH. Should Executive die before she receives the full amount
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of salary continuation payments to which she may become entitled under Part Two of this Agreement, then the balance of such payments shall be made, on the due dates hereunder had Executive survived, to the executors or administrators of her estate.

PART THREE - MISCELLANEOUS PROVISIONS

15. SUCCESSORS AND ASSIGNS. The provisions of this Agreement shall
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inure to the benefit of, and shall be binding upon, the Corporation, its successors and assigns, and the Executive, the personal representative of her estate and her heirs and legatees.

16. GENERAL CREDITOR STATUS. The benefits to which Executive may
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become entitled under Part Two of this Agreement shall be paid, when due, from the Corporation's general assets, and no trust fund, escrow arrangement or other segregated account shall be established as a funding vehicle for such payments. Accordingly, Executive's right (or the right of the executors or administrators of Executive's estate) to receive such benefits shall at all times be that of a general creditor of the Corporation and shall have no priority over the claims of other general creditors.

17. NOTICES.

A. Any and all notices, demands or other communications required or desired to be given hereunder by any party shall be in writing and shall be validly given or made to another party if served either personally or if deposited in the United States mail, certified or registered, postage prepaid, return receipt requested. If such notice, demand or other communication shall be served personally, service shall be conclusively deemed made at the time of such personal service. If such notice, demand or other communication is given by mail, such notice shall be conclusively deemed given forty-eight (48) hours after the deposit thereof in the United States mail addressed to the party to whom such notice, demand or other communication is to be given as hereinafter set forth.

To the Corporation: Digital Island
353 Sacramento Street
Suite 1520
San Francisco, California 94111
Attention' Marcello Gumucio

To Executive: Ruann Ernst
28525 Matadero Creek Lane
Los Altos Hills, CA 94022

B. Any party hereto may change its address for the purpose of receiving notices, demands and other communications as herein provided by a written notice given in the manner aforesaid to the other party hereto.

18. GOVERNING DOCUMENT. This Agreement constitutes the entire agreement and understanding of the Corporation and Executive with respect to the terms and conditions of Executive's employment with the Corporation and the payment of severance benefits and supersedes all prior and contemporaneous written or verbal agreements and understandings between Executive and the Corporation relating to such subject matter. This Agreement may only be amended by written instrument signed by Executive and an authorized officer of the Corporation. Any and all prior agreements, understandings or representations relating to the Executive's employment with the Corporation are hereby terminated and cancelled in their entirety and are of no further force or effect.

19. GOVERNING LAW. The provisions of this letter agreement will be construed and interpreted under the laws of the State of California applicable to agreements executed and to be wholly performed within the State of California. If any provision of this Agreement as applied to any party or to any circumstance should be adjudged by a court of competent jurisdiction to be void or unenforceable for any reason, the invalidity of that provision shall in no way affect (to the maximum extent permissible by law) the application of such provision under circumstances different from those adjudicated by the court, the application of any other provision of this Agreement, or the enforceability or invalidity of this Agreement as a whole.

Should any provision of this Agreement become or be deemed invalid, illegal or unenforceable in any jurisdiction by reason of the scope, extent or duration of its coverage, then such provision shall be deemed amended to the extent necessary to conform to applicable law so as to be valid and enforceable or, if such provision cannot be so amended without materially altering the intention of the parties, then such provision will be stricken and the remainder of this Agreement shall continue in full force and effect.

20. REMEDIES. All rights and remedies provided pursuant to this Agreement or by law shall be cumulative, and no such right or remedy shall be

exclusive of any other. A party may pursue any one or more rights or remedies hereunder or may seek damages or specific performance in the event of another party's breach hereunder or may pursue any other remedy by law or equity, whether or not stated in this Agreement.

21. ARBITRATION. Any and all disputes between Executive and the
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Corporation which arise out of Executive's employment under the terms of this Agreement shall be resolved through final and binding arbitration. This shall include, without limitation, disputes relating to this Agreement, Executive's employment by the Corporation or the termination thereof, claims for breach of contract or breach of the covenant of good faith and fair dealing, and any claims of discrimination or other claims under Title VII of the Civil Rights Act of 1964, the Age Discrimination in Employment Act, the Americans With Disabilities Act, the California Fair Employment and Housing Act, or any other federal, state or local law or regulation now in existence or hereinafter enacted and as amended from time to time concerning in any way the subject of Executive's employment with the Corporation or its termination. The only claims not covered by this Agreement are claims for benefits under the workers'
- ---
compensation or unemployment insurance laws, which will be resolved pursuant to those laws. Binding arbitration will be conducted in San Francisco, California in accordance with the rules and regulations of the American Arbitration Association. Each party will split the cost of the arbitration filing and hearing fees, and the cost of the arbitrator; each side will bear its own attorneys' fees, that is, the arbitrator will not have authority to award attorneys' fees unless a statutory section at issue in the dispute authorizes
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the award of attorneys' fees to the prevailing party, in which case the arbitrator has authority to make such award as permitted by the statute in question. Executive understands and agrees that the arbitration shall be instead of any civil litigation and that this means that she is waiving her right to a jury trial as to such claims. The parties further understand and agree that the arbitrator's decision shall be final and binding to the fullest extent permitted by law and enforceable by any court having jurisdiction thereof.

23. COUNTERPARTS. This Agreement may be executed in more than one
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counterpart, each of which shall be deemed an original, but all of which together shall constitute but one and the same instrument.

SIGNATURES ON NEXT PAGE

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IN WITNESS WHEREOF, the parties have executed this Employment Agreement as of the day and year written above.

DIGITAL ISLAND

By: /s/ [SIGNATURE ILLEGIBLE]^^

Title: Chairman

/s/ Ruann F. Ernst

RUANN ERNST, EXECUTIVE

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EXHIBIT 10.6

[LOGO OF DIGITAL ISLAND APPEARS HERE]

EMPLOYMENT AGREEMENT

This Employment Agreement ("Agreement") is entered into as of February 3, 1997 between Digital Island, Inc., a California corporation (the "Company"), and Allan Leinwand ("Employee").

In consideration of the mutual covenants and conditions set forth herein, the parties hereby agree as follows:

1. EMPLOYMENT. The Company hereby employs Employee in the capacity of Chief Technical Officer (CTO). Employee accepts such employment and agrees to perform such services as are customary to such office and as shall from time to time be assigned to him by the Board of Directors. As a condition to such employment, Employee will complete, execute and deliver to the Company the Nondisclosure and Assignment of Inventions Agreement in the form attached hereto as Exhibit A.

2. TERM. The employment hereunder shall be for a period of 3 year, commencing on February 3, 1997 (the "Term of Employment"), unless earlier terminated as provided in Section 4. Employee's employment will be on a full-time basis requiring the devotion of such amount of his productive time as is necessary for the efficient operation of the business of the Company.

3. COMPENSATION

3.1. SALARY. Dining the Term of Employment, Employee shall be entitled to an annual salary of$105,000, payable (less required withholdings) no less frequently than twice monthly. In addition to annual salary, Employee will be eligible for a bonus of $10,000 per quarter based on successful achievement of agreed upon objectives.

3.2. OTHER BENEFITS. During the Term of Employment, Employee and their family shall be entitled to such medical, disability and life insurance coverage and such vacation, sick leave and holiday benefits, if any, as are made available to the Company's top executive personnel, all in accordance with the Company's benefits program in effect from time to time.

3.3. REIMBURSEMENT OF EXPENSES. During the Term of Employment, Employee shall be entitled to be reimbursed for reasonable expenses incurred by Employee in connection with and reasonably related to the furtherance of the Company's business.

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3.4. INCENTIVE STOCK OPTIONS (ISO). The Company will offer the employee a qualified option to purchase 240,000 shares of Class C stock at a exercise price of $.10 per share vesting over four years under the following conditions. In lieu of forgiving employee's current option which has vested 66,667 shares employee will vest immediately 66,667 shares in the qualified option. The remaining 173,333 shares will vest 2% per month of continuous employment until fully vested over 50 months.

4. TERMINATION

4.1. TERMINATION EVENTS. The employment hereunder will terminate upon the occurrence of any of the following events:

(i) Employee voluntarily terminates the employment at Employee's option, which Employee may do at any time, with at least thirty (30) days advance notice, with or without stating any reason therefor;

(ii) Employee dies;

(iii) the Company, by written notice to Employee or Employee's personal representative, terminates Employee due to the inability of Employee to perform the duties assigned to Employee hereunder by reason of injury, physical or mental illness or other disability, which, in the reasonable judgment of the Board of Directors of the Company, prevents Employee from satisfactorily performing such duties for a continuous period exceeding 365 days; or

(iv) Employee is discharged by the Board of Directors of the Company for cause. As used in this Agreement, the term "cause" includes any act of gross negligence, willful misconduct or dishonesty by Employee in the performance of his duties hereunder; habitual non-performance of duties after warning and an opportunity to correct; willful refusal to contribute to the well-being of the company; or Employee's conviction of (or pleading guilty or nolo contendere to) a felony or any misdemeanor involving dishonesty or moral
- ---- ----------
turpitude; prodded, however, that prior to terminating Employee for cause, the Company shall give written notice to Employee generally outlining the grounds on which cause is based, and Employee shall have a period of ten (10) days thereafter to respond either verbally or in writing to the Board of Directors' findings.

(v) The company discharges the employee upon thirty (30) day's prior written notice for any lawful reason.

4.2 EFFECTS OF TERMINATION. Upon termination of Employee's employment hereunder, (i) the Company will promptly pay Employee all compensation owed to Employee and unpaid through the date of termination, and (ii) neither Employee nor the Company shall have further obligations hereunder to the other, except that Employee's obligations under the Nondisclosure and Assignment of Inventions Agreement attached hereto as Exhibit A will continue to the extent there specified.

4.3 SEVERANCE. Upon termination of Employee's employment pursuant to paragraph 4.1 (v) above, then, as additional consideration for past services to the corporation, the employee shall receive one hundred percent (100%) of the employee's then current annual base salary, in one installment, payable within 10 days of the employee's last day of employment with Employer.

5. GENERAL PROVISIONS

5.1. ASSIGNMENT. Employee shall not assign or delegate any of his rights or obligations under this Agreement.

5.2. ENTIRE AGREEMENT. This Agreement contain the entire agreement between the parties with respect to the subject matter hereof and supersedes any and all prior agreements between the parties relating to such subject matter.

5.3. MODIFICATIONS. This Agreement may be changed or modified only by an agreement in writing signed by both parties hereto.

5.4. SUCCESSORS AND ASSIGNS. The provisions of this Agreement shall inure to the benefit of, and be binding upon, the Company and its successors and

assigns and Employee and Employee's legal representative, heirs, legatees, distributees, assigns and transferees by operation of law, whether or not any such person shall have become a party to this Agreement and have agreed in writing to join and be bound by the terms and conditions hereof.

5.5. GOVERNING LAW. This Agreement shall be governed by, and construed in accordance with, the laws of the State of California as such laws are applied to agreements among California residents entered into and performed entirely within California.

5.6. SEVERABILITY. If any provision of this Agreement is held by a court of competent jurisdiction to be invalid, void or unenforceable, the remaining provisions shall nevertheless continue in full force and effect.

5.7. FURTHER ASSURANCES. The parties will execute such further instruments and take such further action as may be reasonably necessary to carry out the intent of this Agreement

5.8. NOTICES. Any notices or other communications required or permitted hereunder shall be in writing and shall be deemed received by the recipient when delivered personally or, if mailed, five (5) days alter the date of deposit in the United States mail, certified or registered, postage prepaid and addressed, in the case of the Company, to 1132 Bishop St., Suite 1001, Honolulu, Hawaii, 96813, and in the case of Employee, to the address shown for Employee on the signature page hereof, or to such other address as either party may later specify by at least ten (10) days advance written notice delivered to the other party in accordance herewith.

5.9. CAPTIONS. Section headings used in this Agreement are for convenience of reference only and shall not be considered a part of this Agreement.

<PAGE>

5.10. NO WAIVER. The failure of either party to enforce any provision of this Agreement shall not be construed as a waiver of that provision, nor prevent that party thereafter from enforcing that provision or any other provision of this Agreement.

5.11. ENFORCEMENT. If any action at law or in equity or any arbitration is brought to enforce or interpret the terms of this Agreement or to protect the rights obtained hereunder, the prevailing party shall be entitled to recover its reasonable attorneys' fees, costs and other expenses in addition to any other relief to which it may be entitled.

5.12. COUNTERPARTS. This Agreement may be executed in counterparts, each of which shall be deemed to be an original, but all of which together shall constitute one and the same instrument.

IN WITNESS WHEREOF, the Company and Employee have executed this Agreement, effective as of the day and year first above written.

COMPANY	EMPLOYEE
Digital island, Inc. a California corporation	Allan Leinwand ----------
By: /s/ Ron Higgins ---------- Name: Ron Higgins ---------- Title: CEO ----------	Address: 2064 Green St ---------- SF California 94123 ----------, -----

EXHIBIT A

NONDISCLOSURE AND ASSIGNMENT OF INVENTIONS AGREEMENT

In exchange for my becoming employed as an employee or engaged as a consultant by Digital Island, Inc. or its subsidiaries, affiliates or successors (collectively, "Company"), or my employment or engagement being continued by the Company, I hereby agree as follows:

1. I will perform such duties or services as may be designated by the Company from time to time. During my period of employment or engagement by the Company (collectively referred to herein as "employment"), I will devote my best efforts to the interests of the Company and, without the prior written consent of the Company, will not engage in any activities that might be detrimental to the best interests of the Company.

2. Without further compensation, I hereby agree promptly to disclose to the Company, and I hereby assign and agree to assign to the Company or its designee, my entire right, title and interest in and to all Inventions (as defined below) which (a) pertain to any line of business activity of the Company, or (b) are aided by the use of time, material or facilities of the Company, whether or not during working hours. As used in this Agreement, the term "Inventions" means designs, devices, trademarks, discoveries, development formulae, processes, patterns, compilations, manufacturing techniques, trade secrets, inventions, improvements, ideas or works of authorship, including all rights to obtain, register, perfect and enforce these proprietary interests.

3. No rights are hereby conveyed in Inventions, if any, made by me prior

to my employment with the Company which are identified in the List of Inventions attached hereto as Attachment I and made a part of this Agreement, which attachment contains no confidential information. In addition, this Agreement does not apply to an Invention which qualifies fully under the provisions of Section 2870 of the California Labor Code, which provides as follows:

> Any provision in an employment agreement which provides that an employee shall assign or offer to assign any of his or her rights in an invention to his or her employer shall not apply to an invention for which no equipment, supplies, facility, or trade secret information of the employer was used and which was developed entirely on the employee's own time, and (a) which does not relate (1) to the business of the employer or (2) to the employer's actual or demonstrably anticipated research or development, or (b) which does not result from any work performed by the employee for the employer. Any provision which purports to apply to such an invention is to that extent against the public policy of this state and is to that extent void and unenforceable.

I agree to disclose all Inventions made by me in confidence to the Company to permit a determination as to whether or not the Inventions should be the property of the Company.

4. I agree to perform, during and after my employment, all acts deemed necessary or " desirable by the Company to permit and assist it, at its expense, in obtaining and enforcing the full benefits, enjoyment, rights and title throughout the world in the Inventions hereby assigned to the Company as set forth in paragraph 2 above. Such acts may include, but are not limited to, execution of documents and assistance or cooperation in legal proceedings.

5. I agree to hold in confidence and not directly or indirectly to use or disclose, either during or after termination of my employment with the Company, any Confidential Information (as defined below) I obtain or create during the period of my employment, whether or not during working hours, except to the extent authorized by the Company, until such Confidential Information becomes generally known. I agree not to make copies of such Confidential Information except as authorized by the Company. Upon termination of my employment or upon an earlier request of the Company I will return or deliver to the Company all tangible forms of such Confidential Information in my possession or control, including but not limited to drawings, specifications, documents, records, devices, models or arty other material and copies or reproductions thereof. As used in this Agreement, the term "Confidential Information" means information pertaining to arty aspect of the Company's business which is either information not known by actual or potential competitors of the Company or is proprietary information of the Company or its customers or suppliers, whether of a technical nature or otherwise.

6. I represent that my performance of all the terms of this Agreement and as an employee of or consultant to the Company does not and will not breach any agreement to keep in confidence proprietary information, knowledge or data acquired by me in confidence or in trust prior to my employment with the Company, and I will not disclose to the Company, or induce the Company to use, any confidential or proprietary information or material belonging to any previous employer or others. I agree not to enter into any agreement either written or oral in conflict with the provisions of this Agreement.

7. I agree that, during the term of my employment and for a period of one year thereafter, I will not solicit or encourage any employee of the Company to terminate his or her employment with the Company or to accept employment with any subsequent employer with whom I am affiliated in any way.

8. This agreement (a) shall survive my employment by the Company, (b) does not in any way restrict my fight or the fight of the Company to terminate my employment, with or without cause (although such fights may be restricted by applicable employment agreements, if any), (c) inures to the benefit of successors and assigns of the Company, and (d) is binding upon my heirs and legal representatives.

9. I certify that, to the best of my information and belief, I am not a party to any other agreement which will interfere with my full compliance with this Agreement.

10. In the event that any of the terms or provisions herein shall violate any statutory provisions or may be otherwise unlawful or inoperative, it is the intent and desire of the parties

that this Agreement operate and be in full force and effect insofar as it does not violate the statutory provision or is otherwise lawful and that this Agreement be carded out as far as possible in a manner consistent with its tenor and effect.

11. I CERTIFY AND ACKNOWLEDGE THAT I HAVE CAREFULLY READ ALL OF THE PROVISIONS OF THIS AGREEMENT AND THAT I UNDERSTAND AND WILL FULLY AND FAITHFULLY COMPLY WITH SUCH PROVISIONS.

DIGITAL ISLAND,INC	EMPLOYEE
By: Ron Higgins	Allan Leinwand
Name: Ron Higgins	Allan Leinwand
Title: CEO	

<PAGE>

Attachment 1

Nondisclosure and
Assignment of Inventions Agreement

For: Allan Leinwand

LIST OF INVENTIONS or PUBLICATIONS

Leinwand, A. and Fang, K., Network Management: A Practical Perspective.

Addison-Wesley Publishing Company, Reading, MA., 1993. ISBN 0-201-52771-5.

Leinwand, A. and Fang Conroy, K., Network Management: A Practical Perspective,
---
2/nd/ edition. Addison-Wesley Publishing Company, Reading, MA., 1996. ISBN
- ---
0-201-60999-1.

Work in progress with Bruce Pinsky. Tentative title: The Basics of the Cisco
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IOS. Under contract with MacMillan Computer Publishing USA.
- ---

INITIALS

Employee: /s/ [SIGNATURE ILLEGIBLE]^^

Company: [ILLEGIBLE]^^

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EXHIBIT 10.7

[LOGO OF DIGITAL ISLAND APPEARS HERE]

EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (this "Agreement") is entered into as of May 5, 1997 by Digital Island, Inc., a California corporation and Michael Sullivan ("Employee").

In consideration of the mutual covenants and conditions contained in this Agreement, the parties agree as follows:

1. AT WILL EMPLOYMENT. The Company hereby employees Employee in the capacity of Vice President Finance. The parties agree that employment at the Company is at will and may be terminated by either the Company or Employee at any time with or without cause and with or without notice. Employee acknowledges that Employee has no right to be employed for a specific term and no right to insist on specific grounds for termination. Employee acknowledges and agrees that the at will nature of this Agreement extends to all employment decisions and that any change in the terms and conditions of employment, including without limitation work assignments, production standards, job responsibilities, compensation and promotions, shall be at the Company's sole discretion.

2.a. COMPENSATION AND EXPENSES. Employee shall be entitled to a monthly salary of $10,000, payable (less required withholdings) no less frequently than twice monthly. In addition to your base salary, you will be eligible for a minimum incentive bonus of $5,000 per quarter paid quarterly based on the achievement of mutually agreed upon corporate objectives. This bonus will be guaranteed for the first quarter of employment. The Company will, in accordance with the Company's policy in effect from time to time, reimburse Employee for all approved business expenses incurred by Employee in connection with the performance of Employee's duties.

2.b. INCENTIVE STOCK OPTIONS (ISO). The Company will offer the employee a qualified option to purchase 50,000 shares of Digital Island at the initial ISO price of $.40. This option will be vested over 50 months with an initial 12 month employment requirement. At the end of the first 12 months of employment, you will vest 24% and then 2% per month thereafter. In the event the Board of Directors elects to offer you the position of Chief Financial Officer, you will be entitled to receive an additional option grant of 50,000 shares with the same vesting start date as your original grant.

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2.c. OTHER BENEFITS. During the Term of Employment, Employee shall be entitled to such medical and disability coverage and such vacation, sick leave and holiday benefits, if any, as are made available to the Company's personnel, all in accordance with the Company's benefits program in effect from time to time. You will also be entitled to all future benefits awarded the executive management team.

3. COMPANY'S TRADE SECRETS: In performance of Employee's job duties as may be designated by the Company from time to time, Employee will be exposed to the Company's Trade Secrets. "Trade Secrets" means information or material that is commercially valuable to the Company and not generally known in the industry. This includes:

(a) any and all versions of the Company's proprietary computer software (including source code and object code), hardware, firmware and documentation;

(b) technical information concerning the Company's products and services, including product data and specifications, diagrams, flow charts, drawings, test results, know-how, processes, inventions, research projects and product development;

(c) information concerning the Company's business, including cost information, profits, sales information, accounting and unpublished financial information, business plans, markets and marketing methods, customer lists and customer information, purchasing techniques, supplier lists and supplier information and advertising strategies;

(d) information concerning the Company's employees, including their salaries, strengths, weaknesses and skills;

(e) information submitted by the Company's customers, suppliers, employees, consultants or co-venturers with the Company for study, evaluation or use; and

(f) any other information not generally known to the public which, if misused or disclosed, could reasonably be expected to adversely affect the Company's business.

4. NONDISCLOSURE OF TRADE SECRETS: Employee will keep the Company's Trade Secrets (and Trade Secrets of any person or company contracting with the Company), whether or not prepared or developed by Employee, in the strictest confidence. Employee will not use or disclose such secrets to others without the Company's written consent, except when necessary to perform Employee's job. Employee agrees that any customer, publisher or other third party who provides

confidential information to the Company is an intended third party beneficiary of this provision. However, Employee shall have no obligation to treat as confidential any information which:

(a) was in Employee's possession or known to Employee, without an obligation to keep it confidential, before such information was disclosed to Employee by the Company;

(b) is or becomes public knowledge through a source other than Employee and through no fault of Employee's;

(c) is or becomes lawfully available to Employee from a source other than the Company; or

(d) is disclosed pursuant to a requirement of a governmental agency or as otherwise required by any court of competent jurisdiction.

5. NO CONFLICTING OBLIGATIONS. Employee's performance of this Agreement and as an employee of the Company does not and will not breach any agreement to keep in confidence proprietary information, knowledge or data acquired by Employee prior to Employee's employment with the Company. Employee will not disclose to the Company, or induce the Company to use, any confidential or proprietary information or material belonging to any previous employer or other person or entity. Employee is not a party to any other agreement which will interfere with Employee's full compliance with this Agreement. Employee will not enter into any agreement, whether written or oral, in conflict with the provisions of this Agreement.

6. RETURN OF MATERIALS: When Employee's employment with the Company ends, for whatever reason, Employee will promptly deliver to the Company all originals and copies of all documents, records, software programs, media and other materials containing any of the Company's Trade Secrets. Employee will also return to the Company all equipment, files, software programs and other personal property belonging to the Company or to any of its customers.

7. CONFIDENTIALITY OBLIGATION SURVIVES EMPLOYMENT: Employee's obligation to maintain the confidentiality and security of the Company's Trade Secrets continues even after Employee's employment with the Company ends and continues for so long as such material remains a Trade Secret.

8. COMPUTER PROGRAMS ARE WORKS MADE FOR HIRE: Company may ask, as part of Employee's job duties, Employee to create, or contribute to the creation of,

computer programs, audiovisual works, documentation, artwork and other copyrightable works (collectively called "Work Product"). Employee agrees that any and all Work Product shall be "works made for hire" and that the Company shall own all the copyright rights in such works. Employee retains no rights to use the Work Product or the Developments and agrees not to challenge the validity of the ownership by the Company of the Work Product or the Developments. IF AND TO THE EXTENT ANY SUCH MATERIAL DOES NOT SATISFY THE LEGAL REQUIREMENTS TO CONSTITUTE A WORK MADE FOR HIRE, EMPLOYEE HEREBY ASSIGNS ALL RIGHT, TITLE AND INTERESTS TO ALL EMPLOYEE'S COPYRIGHT AND OTHER INTELLECTUAL PROPERTY RIGHTS IN THE WORK PRODUCT TO THE COMPANY.

9. DISCLOSURE OF DEVELOPMENTS: While Employee is employed by the Company, Employee will promptly inform the Company of the full details of all Employee's works of

authorship, new or useful art, inventions, discoveries, findings, improvements, designs, innovations and ideas (collectively called "Developments"), whether or not the Developments are patentable, copyrightable or otherwise protectable, that Employee conceives, completes or reduces to practice (whether individually or in collaboration with others) and which:

(a) relate to the Company's present or prospective business, or actual or demonstrably anticipated research and development; or

(b) result from any work Employee does using any equipment, facilities, materials, Trade Secrets or personnel of the Company; or

(c) result from or are suggested by any work that Employee may do for the Company.

10. ASSIGNMENT OF DEVELOPMENTS: Employee hereby assigns to the Company or the Company's designee, Employee's entire fight, title and interest in all of the following, that Employee conceives or make (whether alone or with others) while employed by the Company:

(a) all Developments;

(b) all copyrights, Trade Secrets, trademarks and mask work rights in Developments; and

(c) all patent applications filed and patents granted on any Developments, including those in foreign countries.

11. WAIVER OF RIGHTS. In the event Employee has any fight in and to the

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Work Product or Developments that cannot be assigned to the Company, Employee hereby unconditionally and irrevocably (a) waives the enforcement of all such fights, and all claims and causes of action of any kind with respect to any of the foregoing against the Company, its distributors and customers, whether now known or hereafter to become known, and (b) agrees, at the request and expense of the Company and its respective successors and assigns, to consent to, and to join in, any action to enforce such fights or to procure a waiver of such rights from the holders of such fights.

12. LICENSE. In the event Employee has any fights in and to the Work
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Product or the Developments that cannot be assigned to the Company and cannot be waived, Employee hereby grants to the Company, and its respective successors and assigns, an exclusive, worldwide, royalty-free license during the term of the fights to reproduce, distribute, modify, publicly perform and publicly display, with the fight to sublicense and assign such fights in and to the Work Product or the Developments including, without limitation, the fight to use in any way whatsoever the Work Product or the Developments. Each of Company's clients, customers and business partners is an intended third party beneficiary of this provision and may independently enforce Employee's obligations hereunder.

13. EXECUTION OF DOCUMENTS: Both while employed by the Company and
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afterwards, Employee agrees to execute and aid in the preparation of any papers that the Company may consider necessary or helpful to obtain or maintain any patents, copyrights, trademarks or other proprietary rights at the Company's expense.

14. APPOINTMENT OF ATTORNEY-IN-FACT. In the event that the Company is
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unable for any reason whatsoever to secure Employee's signature to any lawful and necessary document required to apply for or execute any patent, copyright or other applications with respect to any of the Work Product or the Developments (including improvements, renewals, extensions, continuations, divisions or continuations in part hereof), Employee hereby irrevocably appoints the Company and its duly authorized officers and agents as Employee's agents and attorneys-in-fact to execute and file any such application and to do all other lawfully permitted acts to further the prosecution and issuance of patents, copyrights or other rights thereon with the same legal force and effect as if executed by Employee.

15. CONFLICT OF INTEREST: During Employee's employment by the Company,
---

Employee will not engage in any business activity competitive with the Company's business activities.

16. NONINTERFERENCE WITH COMPANY EMPLOYEES: While employed by the Company, Employee will not:

(a) induce, or attempt to induce, any Company employee to quit the Company's employ;

(b) recruit or hire away any Company employee; or

(c) hire or engage any Company employee or former employee whose employment with the Company ended less than six months before the date of such hiring or engagement.

17. ENFORCEMENT: Employee agrees that in the event of a breach or threatened breach of this Agreement, money damages would be an inadequate remedy and extremely difficult to measure. Employee agrees, therefore, that the Company shall be entitled to an injunction to restrain Employee from such breach or threatened breach. Nothing in this Agreement shall be construed as preventing the Company from pursuing any remedy at law or in equity for any breach or threatened breach.

18. ASSIGNMENT. This Agreement may be assigned by the Company. Employee may not assign or delegate Employee's duties under this Agreement without the Company's prior written approval. This Agreement shall be binding upon Employee's heirs, successors, and permitted assignees.

19. GOVERNING LAW: This Agreement is made and shall be construed and enforced in accordance with the laws of the State of California.

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20. ARBITRATION: In the event of any dispute in connection with this Agreement, the Parties agree to resolve the dispute by binding arbitration in San Francisco, California, under the Commercial Arbitration Rules of the American Arbitration Association ("AAA"), with a single arbitrator familiar with software development disputes appointed by the AAA. In the event of any dispute, the prevailing party shall be entitled to its reasonable attorneys' fees and costs from the other party, whether or not the matter is litigated or arbitrated to a final judgment or award.

21. CHOICE OF FORUM. The parties hereby submit to the jurisdiction of, and waive any venue objections against, the United States District Court for the

Northern District of California and the Superior and Municipal Courts of the State of California, San Francisco County, in any litigation arising out of this Agreement.

22. SEVERABILITY: If any provision of this Agreement is determined to be invalid or unenforceable, the remainder shall be unaffected and shall be enforceable against both the Company and Employee.

23. ENTIRE AGREEMENT: This Agreement supersedes and replaces all prior agreements or understandings, oral or written, between the Company and Employee, except for any prior confidentiality agreements.

24. MODIFICATION: This Agreement may not be modified except by a writing signed both by the Company and Employee.

25. EMPLOYEE REVIEW AND RECEIPT OF AGREEMENT. Employee acknowledges that Employee has carefully read and considered all provisions of this Agreement and agrees that all of the restrictions set forth herein are fair and reasonably required to protect the Company's interests. Employee acknowledges that Employee has received a copy of this Agreement as signed by Employee.

26. NOTICE PURSUANT TO STATE LAW: Employee acknowledges that Employee has been notified of its fights, if any, under California Labor Code Section 2870, "Employment Agreements Assignment of Rights," and that Employee has had a full and fair opportunity to read the provisions of Section 2870, a copy of which is attached hereto as Exhibit A. Employee understands that this Agreement does not apply to any invention that qualifies fully under the provisions of Section 2870. This section shall serve as written notice to Employee as required by California Labor Code Section 2872.

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27. PRIOR DEVELOPMENTS: As a matter of record, Employee has identified all prior developments ("Prior Developments") that have been conceived or reduced to practice or learned by Employee, alone or jointly with others, before Employee's employment with the Company, which Employee desires to remove from the operation of this Agreement. The Prior Developments are listed on attached Exhibit B. Employee represents and warrants that this list is complete. If there is no such list, Employee represents that it has made no such Prior Developments at the time of signing this Agreement.

Michael Sullivan

/s/ Michael J. Sullivan

Date: 6/30/97 Employee's Signature

Michael Sullivan

Typed or Printed Name

DIGITAL ISLAND, INC,:

/s/ [SIGNATURE ILLEGIBLE]^^

Date:_____ Signature

_____
Typed or Printed Name

CEO

Title

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EXHIBIT A

California Labor Code Section 2870 provides as follows:

(a) Any provision in an employment agreement that provides that an employee shall assign, or offer to assign, any of his or her rights in an invention to his or her employer shall not apply to an invention that the employee developed entirely on his or her own time without using the employer's equipment, supplies, facilities, or trade secret information except for those inventions that either:

(1) Relate at the time of conception or reduction to practice of the invention to the employer's business, or actual or demonstrably anticipated research or development of the employer or

(2) Result from any work performed by the employee for the employer.

(b) To the extent a provision in an employment agreement purports to require an employee to assign an invention otherwise excluded from being required to be assigned under subdivision (a), the provision is against the

public policy of this state and is unenforceable.
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EXHIBIT B

PRIOR DEVELOPMENTS

[LIST OF ALL PRIOR DEVELOPMENTS; IF BLANK WRITE "NONE"]

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EXHIBIT 10.8
353 SACRAMENTO STREET OFFICE LEASE

BETWEEN

JOHN HANCOCK MUTUAL LIFE INSURANCE COMPANY,
A MASSACHUSETTS CORPORATION
("LANDLORD")

AND

DIGITAL ISLAND
A CALIFORNIA CORPORATION
"TENANT"

DATED AS OF APRIL 8, 1997
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BASIC LEASE INFORMATION
353 SACRAMENTO STREET

Lease Date: April 8, 1997

Landlord: John Hancock Mutual Life Insurance Company,
a Massachusetts corporation

Address of Landlord: c/o The Galbreath Company
353 Sacramento Street, Suite 320
San Francisco, CA 94111

Tenant: Digital Island,
a California corporation

Address of Tenant: 353 Sacramento Street, Suite 1520
San Francisco, CA 94111

Contact for Tenant: Attn: Ron Higgins

Contact for Landlord: Melody Hanhan
353 Sacramento Street Building Manager

Tenant's Address
Prior to Occupancy: 1139 Bishop Sweet, Suite 1001
Honolulu, HI 96813
Attn: Ron Higgins

Section 1:

Premises: Suite 1520, 15th floor

The Building: 353 Sacramento Street
San Francisco, CA 94111

Building Rentable
Area (Office and
Retail Space): 251,777 square feet

Building Rentable.
Area (Office Space): 241,683 square feet

Premises Rentable
Area: 6,132 square feet

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Section 2:

Lease Term: 5 years

Term Commencement Date The date Landlord delivers the Premises to Tenant

Scheduled Term Commencement for
Phase I portion: Approximately May 15, 1997

Scheduled Term Commencement for
Phase 2 portion: Approximately July 1, 1997

Term Expiration Date: May 30, 2002

Section 3:

Use: General office purposes

Section 4:

Year	P.S.F. Annual Rental	Monthly Minimum Rental	Annual Minimum Rental
*First	$29.00	$14,819	$177,828
Second	$30.00	$15,330	$183,960
Third	$31.00	$15,841	$190,092
Fourth	$32.00	$16,352	$196,224
Fifth	$33.00	$16,863	$202,356

*Until the Phase 2 portion of the Premises is delivered to Tenant the Monthly Minimum Rental is $7,566.60.

Security Deposit: $200,000 (See Section 4.6)

Section 5:

**Tenant's Expense Share: 2.54%

Tenant's Tax Share: 2.44%

**Until the Phase 2 portion of the Premises is delivered to Tenant, Tenant's Expense Share is 1.30% and Tenant's Tax share is 1.24%

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Section 42:

Landlord's Broker: The Galbreath Company

Tenant's Broker: CB Commercial

The foregoing Basic Lease Information is hereby incorporated into and made a part of this Lease. Each reference in this Lease to any of the Basic Lease Information shall mean the information set forth above. In the event of a conflict between any Basic Lease Information and the Lease, the Lease shall control.

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353 SACRAMENTO STREET
OFFICE LEASE AGREEMENT

This Lease Agreement ("LEASE") is made and entered into as of April 8, 1997, by and between JOHN HANCOCK MUTUAL LIFE INSURANCE COMPANY, a Massachusetts corporation ("Landlord"), and DIGITAL ISLAND, a California Corporation ("TENANT")

Section I. Premises

1.1 Subject to all of the terms and conditions set forth in this Lease, Landlord hereby leases to Tenant and Tenant hereby leases from Landlord those certain premises (the "LEASED PREMISES"), as described in attached Exhibit A

The Leased Premises are part of the office building known as 353 Sacramento Street (the "BUILDING"), located in San Francisco California. As used herein the term "BUILDING" includes the Building, the underlying land and all improvements thereon and appurtenances thereto. The Premises and the Building contain the rentable square footage set forth in the Basic Lease Information (calculated pursuant to the American National Standard method adopted by the Building Owners and Managers Association International). The Building, the land and improvements under and surrounding the Building and designated from time to time by Landlord as laud or common areas appurtenant to the Building, together with utilities, facilities; drives, walkways and other amenities appurtenant to or servicing the Building are herein sometimes collectively called the "REAL PROPERTY." Tenant is hereby granted the right to the non-exclusive use of the common corridors and hallways, stairwells, elevators, electrical and telephone closets, restrooms and other public or common areas; provided, however, that the maximum in which the public and common areas are maintained and operated shall be at the sole discretion of Landlord and the use thereof shall be subject to such rules, regulations and restrictions as Landlord may make from time to time. Tenant shall also have the right to the non-exclusive use of the loading dock of the

Building without charge, which use shall also be subject to such rules, regulations and restrictions as Landlord may establish or alter at any time or from time to time during the term hereof. Landlord reserves the right to make alterations or additions to or to change the location of elements of the Real Property and the common areas thereof.

1.2 The term "RENTABLE AREA" shall be computed by measuring from the inside surface of the exterior glass of the outer building walls, to the center of corridor walls, and to the center of all partitions which separate the Leased Premises from adjoining areas, plus Tenant's pro rata portion of areas common to all tenants of the Building including, without limitation, corridors, lobbies, rest rooms, public areas, mechanical, electrical, telephone, janitorial or equipment room, closet or space, and spaces within the entire Building. Elevator shafts shall be excluded in computing Rentable Area.

SECTION 2. TERM

2.1 This Lease shall remain in effect for a term (the "INITIAL TERM") commencing on the date Landlord delivers the Premises to Tenant as provided in attached Exhibit C (which date is herein referred to as the "COMMENCEMENT DATE")
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and expiring at 6:00 P.M. on the Expiration Date specified in the Basic Lease Information (the "EXPIRATION DATE") unless sooner terminated or extended as provided in this Lease. The earlier of the Expiration Date or the date this Lease is terminated is herein referred to as

the "TERMINATION DATE". The Premises will be delivered to Tenant in two phases, Phase 1 (consisting of approximately 3131 square feet) and Phase 2 (consisting of approximately 3001 square feet). The estimated delivery date for each of Phase 1 and Phase 2 is set forth in the Basic Lease Information.

2.2 Tenant accepts the Leased Premises in its "as is" condition, as of the date hereof subject only to Landlord's obligations under Exhibit C. Except as
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provided in Exhibit C. Landlord shall have no obligation to modify or improve
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the Leased Premises and shall not be liable for any claims or damages arising in connection with any modifications or improvements.

SECTION 3. USE, NUISANCE OR HAZARD

3.1 The Leased Premises shall be used and occupied by Tenant solely for general office purposes and for no other purposes without Landlord's prior written consent which consent may be given or withheld in Landlord's sole discretion.

3.2 Tenant shall not use, occupy or permit the use or occupancy of the Leased Premises for any purpose which Landlord, in its reasonable discretion, deems to be illegal, immoral or dangerous; permit any public or private nuisance; do or permit any act or thing which may disturb the quiet enjoyment of any other tenant or occupancy of the Building; keep any substance or carry on or permit any operation which might introduce offensive odors or conditions into other portions of the Building; use any apparatus which might make undue noise or set up vibrations in or about the Building; permit anything to be done which would increase the premiums paid by Landlord for fire and extended coverage insurance on the Building or its contents or cause a cancellation of any insurance policy covering the Building or any part thereof or any of its contents; or permit anything to be done which is prohibited by or which shall in any way conflict with any Law (as defined in Section 34). Should Tenant do any of the above without the prior written consent of Landlord, it shall constitute an Event of Default (as defined in Section 22) and Landlord shall be entitled to exercise any of its rights and remedies under this Lease or at law or in equity.

3.3 Without limiting the generality of the foregoing, Tenant shall promptly comply with all requirements of the Americans with Disabilities Act and the regulations promulgated thereunder in effect from time to time ("ADA REQUIREMENTS") relating to the conduct of Tenant's business. Tenant shall have exclusive responsibility for compliance with ADA Requirements pertaining to the interior of the Premises, including the design and construction of the access thereto and egress therefrom. Landlord shall have responsibility for compliance with ADA Requirements which affect the common areas of the Building, subject to Tenant's obligation to pay for its share of the expense of such compliance pursuant To Section 5 of this Lease. Tenant shall comply promptly with any direction of any governmental authority having jurisdiction which imposes any duty upon Tenant or Landlord with respect to the Premises or with respect to the use or occupation thereof, and Tenant agrees to furnish Landlord with a copy of any such direction promptly after receipt of the same. In addition, Tenant shall comply with any reasonable plan adopted by Landlord which is designed to fulfill the requirements of any Laws, including ADA Requirements.

Should compliance by Tenant with this Section require Landlord's consent pursuant to Section 15.1, Tenant shall promptly seek such consent, provide the assurances and documents required

by Section 15.1 and, following receipt of such consent, promptly comply with the provisions of Section 15.1 and this Section 3.3.

If Tenant fails to comply with ADA Requirements as required in this Section 3.3, then, after notice to Tenant, Landlord may comply or cause such compliance, in which case Tenant shall reimburse Landlord upon demand for Landlord's costs incurred in connection therewith.

SECTION 4. RENT

4.1 Tenant shall pay to Landlord an initial base annual rental ("BASE RENT") in the amount specified in the Basic Lease Information. Reference to "BASE RENT" shall refer both to the initial Base Rent and the adjustment thereto specified in the Basic Lease Information. The Base Rent shall be due and payable, without notice, in twelve equal installments ("MONTHLY RENT") by check or money order, in advance, on or before the first day of each calendar month. In addition to the Base Rent, Tenant shall pay any and all other sums of money as shall be become due and payable by Tenant as set forth in this Lease ("ADDITIONAL RENT"). The Monthly Rent and/or Additional Rent are sometimes collectively called the "RENT" and shall be paid when due in lawful money of the United States without demand, deduction, abatement or offset at the address specified in the Basic Lease Information or such other place as Landlord may designate from time to time. All Rent and any other charges due and unpaid as of the Termination Date shall be deemed due and payable on the Termination Date and, if unpaid as of such date, shall sin-rive the Termination Date. Landlord expressly reserves the right to apply the payment of Base Rent to any other items of Rent that are not paid by Tenant.

4.2 Notwithstanding the above, in the event any Rent or other amounts owing under this Lease are not paid within five days after the due date, then Landlord and Tenant agree that Landlord will incur additional administrative expenses, the amount of which will be difficult, if not impossible, to determine Accordingly, in addition to such required payment, Tenant shall pay to Landlord, upon demand, an additional one time late charge ("LATE CHARGE"), as Additional Rent, for any such late payment in the amount often percent of the amount of such late payment. Failure to pay any applicable Late Charge shall be deemed a Monetary Default (as defined in Section 22). Provision for the Late Charge shall be in addition to all other rights and remedies available to Landlord under this Lease, at law or in equity, and shall not be construed as liquidated damages or limiting Landlord's remedies in any manner. Failure to charge or collect such Late Charge in connection with any one or more such late payments shall not constitute a waiver of Landlord's right to charge and collect such Late Charges in connection with any other or similar or like late payments.

4.3 If the Term commences on a date other than the first day of a calendar month or terminates on a date other than the last day of a calendar month, the Rent for such partial months shall be prorated to the actual number of days the Lease is in effect for said partial months.

4.4 All Rents and any other amounts payable by Tenant to Landlord, if not paid when due, shall bear interest from the date due until paid at the rate of interest publicly announced from time to time by Bank of America National Trust and Savings Association in San Francisco as its Reference Rate (the "REFERENCE RATE") plus four percent per annum, but not in excess of the maximum legal rate permitted by law. Failure to charge or collect such interest in connection with any one or more such late

payments shall not constitute a waiver of Landlord's right to charge and collect such interest in connection with any other or similar or like late payments.

4.5 If Tenant fails to timely make two consecutive payments of Monthly Rent or makes two (2) consecutive payments of Money Rent which are returned to Landlord by Tenant's financial institution for insufficient funds, Landlord may require, by giving written notice to Tenant, that all future payments of Rent shall be made in cashier's check or money order. The above is in addition to any other remedy of Landlord under this Lease, at law or in equity.

4.6 The first payment of Monthly Rent shall be due and payable upon the execution of this Lease by Tenant, which sum shall be applied to the Base Rent for the first month of the Term. Additionally, Tenant shall pay to Landlord the security deposit (the "SECURITY DEPOSIT") in the amount specified in the Basic Lease Information as security for Tenant's faithful performance of all of the terms, covenants, conditions and obligations required to be performed by Tenant hereunder. Without waiving any of Landlord's other rights and remedies under this Lease, but after notice and expiration of any cure period (if required under Section 22), Landlord may apply any part or all of the Security Deposit to remedy any failure by Tenant to repair or maintain the Leased Premises or to perform any other term, covenants or conditions contained in this Lease or to compensate Landlord for damages incurred in connection with any event of default by Tenant under this Lease. If Landlord so applies the Security Deposit, Tenant shall within ten days after demand from Landlord restore the Security Deposit to the full amount required hereunder. Failure of Tenant to do so shall be a default under this Lease. Landlord's application of the Security Deposit shall in no event be construed as in any way limiting Tenant's liability or obligation with respect to any such default. If Tenant has kept and performed all terms, covenants and conditions of this Lease, Landlord will, within thirty days following termination of this Lease, return the Security Deposit to Tenant or the last permitted assignee of Tenant's interest hereunder at the Termination Date. Landlord shall not be required to keep the Security Deposit separate from its general funds, and Tenant shall not be entitled to interest on the Security Deposit. No trust or fiduciary relationship is created by this Lease between Landlord and Tenant with respect to the Security Deposit. If the Security Deposit is in the form of a letter of credit, the letter of credit shall conform to the Letter of Credit Requirements provided by Landlord to Tenant and shall be drawable at a location in the San Francisco Bay Area.

SECTION 5. ADDITIONAL RENT; OPERATING EXPENSES AND APPLICABLE TAXES

5.1 As used in this Lease, the following terms have the meanings hereinafter set forth:

(a) "EXPENSE BASE YEAR" and "TAX BASE YEAR" shall mean calendar year 1997.

(b) "EXPENSE COMPARISON YEAR" shall mean each successive calendar year after the Expense Base Year during the Lease Term.

(c) "TAX COMPARISON YEAR" shall mean each successive calendar year after the Tax Base Year during the Lease Term.

(d) "TENANT'S EXPENSE SHARE" shall mean the percentage of Operating Expenses set forth in the Basic Lease Information. Tenant's Expense Share was calculated by dividing the rentable area of the

Premises by the total rentable area of the office space in the Building. In the event either the rentable area of the Premises and/or the total rentable area of the office space in the Building is changed, Tenant's Expense Share shall be appropriately adjusted, and, as to the Expense Year in which such change occurs, Tenant's Expense Share for such year shall be prorated for the periods before and after such change on the basis of the number of days during such Expense Year.

(e) "TENANT'S TAX SHARE" shall mean the percentage of Applicable Taxes set forth in the Basic Lease Information. Tenant's Tax Share was calculated by dividing the rentable area of the Premises by the total rentable area of the office and retail space in the Building. In the event either the rentable area of the Premises or the total rentable area of the office and retail space in the Building is changed, Tenants Tax Share shall be appropriately adjusted, and, as to the Tax Year in which such change occurs, Tenant's Tax Share for such year shall be prorated for the periods before and after such change on the basis of the number of days during such Tax Year.

(f) "OPERATING EXPENSES" shall mean any and all costs and expenses paid or incurred by Landlord in connection with the operation, maintenance, management, repair and replacement of the Real Property. By way of illustration but not limitation, Operating Expenses shall include the following: (i) the cost of air conditioning, electricity, steam, heating, water, mechanical, ventilating, sanitary and storm drainage (including provision of services, maintenance, repair and replacement), the cost of environmental surcharges imposed by any government entity, escalator and elevator systems and all other utilities and the cost of supplies and equipment and maintenance and service contracts in connection therewith; (ii) the cost of repairs and general maintenance and cleaning, including all goods, services and supplies purchased by Landlord in connection therewith; (iii) the cost of fire, extended coverage, boiler, sprinkler, public liability, property damage, loss of rent, earthquake and other insurance on or coveting operations of the Building, including such other endorsements as Landlord may desire, all in such amounts as Landlord may reasonably determine, and the cost of any losses payable by Landlord as a deductible; (iv) wages, salaries and other labor costs, including uniforms, taxes, insurance, retirement, medical and other employee benefits; (v)

reasonable fees, charges and other costs, including management fees, consulting fees, legal fees and accounting fees, of all independent contractors engaged by Landlord or reasonably charged by Landlord if Landlord or its affiliate(s) perform management services in connection with the Real Property, and the costs of supplying, replacing and cleaning employee uniforms; (vi) the cost of licenses, permits and inspections and the cost of contesting the validity or applicability of any governmental enactments which may affect Operating Expenses; (vii) the cost of window coverings, carpeting and other wall or floor coverings furnished by Landlord from time to time in public corridors and common areas; (viii) the amount of reasonable reserves established for anticipated expenditures; (ix) the cost of repairs, changes, alterations or improvements of any kind to the Building (collectively, "CHANGES") in a good faith effort to comply with the requirements of any Laws, the entire cost of such changes ("CODE COSTS") to be deemed Operating Expenses in the year in which they accrue or are paid by Landlord, at Landlord's option, except that if Landlord's accountants determine that any portion of Code Costs must be. capitalized rather than expensed, then each year Landlord shall include in Operating Expenses only the properly chargeable portion of capitalized Code Costs during such year based on a determination of the useful life of the Changes for which the Code Costs were incurred together with interest on the unamortized balance at the rate of interest publicly announced from time to time by Bank of America National Trust and Savings Association in San Francisco, California as its Reference Rate (the "B OF A REFERENCE RATE") and two percentage points; (x) the cost of any capital improvements made to the Building after completion of its construction as a

labor-saving or energy conservation device or to effect other economies in the operation or maintenance of the Building, or made to the Building after the date of this Lease that are required under any governmental law or regulation that was not applicable to the Building at the time that permits for the construction thereof were obtained, to be capitalized if appropriate under clause (ix); and (xi) management fees paid by Landlord to third parties or to management companies owned by, or management divisions of, Landlord for management services directly rendered to the Building.

For purposes of computing Tenant's Expense Share pursuant to this Section 5.1, Operating Expenses for the entire Building that are not, in Landlord's sole discretion, allocable or chargeable solely to either the office or retail space of the Building shall be allocated between and charged to the office and retail space of the Building on an equitable basis as determined by landlord.

For purposes of this Lease, Operating Expenses shall not include Applicable Taxes covered under clause (g) below, depreciation on the improvements contained in the Building (except as provided above), the cost of capital improvements (except as provided above). The computation of Operating Expenses, and whether a particular item must be capitalized or expensed, shall be consistent with generally accepted real estate accounting practices.

(g) "APPLICABLE TAXES" shall mean all taxes, assessments and charges levied on or with respect to the Building, the Real Property, or any personal property of Landlord used in the operation thereof and payable by Landlord. Applicable Taxes shall include, without limitation, all general real property taxes and general and special assessments; fees, assessments or charges for transit, police, fire, housing, other governmental services, or purported benefits to the Building; service payments in lieu of taxes; and any tax, fee or excise on the act of entering into this Lease or on the use or occupancy of the Building or any part thereof, or on the rent payable under any lease or in connection with the business of renting space in the Building, that are now or hereafter levied on or assessed against Landlord by, or payable by Landlord as a result of, the requirements oft he United States of America, the State of California, or any political subdivision, public corporation, district or other political or public entity, and shall also include any other tax, fee or other excise, however described, that may be levied or assessed as a substitute for, or as an addition to, in whole or in part, any other taxes. Applicable Taxes shall not include franchise, transfer, inheritance or capital stock taxes or income taxes measured by the net income of Landlord from all sources, unless, due to a change in the method of taxation, any of such taxes are levied or assessed against Landlord as a substitute for, in whole or in part, any other tax which would otherwise constitute an Applicable Tax. Applicable Taxes shall also include reasonable legal fees, costs and disbursements incurred in connection with proceedings to contest, determine or reduce Applicable Taxes. Notwithstanding anything to the contrary in this Lease, in the event that any Applicable Taxes are payable, or may at the option of the taxpayer be paid in installments, such Applicable Taxes shall be deemed to have been paid in installments, regardless of the method of actual payment by Landlord, and Tenant's share of such Applicable Taxes shall only include those installments which would become due and payable during the Term.

5.2 If, with respect to any Expense Comparison Year, the Operating Expenses shall be higher than the Operating Expenses for the Expense Base Year, Tenant shall pay to Landlord, as Additional Rent, Tenant's Expense Share of any such increase in Operating Expenses in the manner provided herein. If, with respect to any Tax Comparison Year, the Applicable Taxes shall be higher than the

Applicable Taxes for the Tax Base Year, Tenant shall pay to Landlord as Additional Rent Tenant's Tax Share of any such increase in Applicable Taxes in the manner provided herein.

5.3 The payments contemplated under Section 5.2 shall be made as follows:

(a) During each month of each Comparison Year, Tenant shall pay to Landlord, with each installment of Monthly Rent, such amounts as are reasonably

estimated by Landlord to be one-twelfth (1/12th) of the amounts payable pursuant to Section 5.2 with respect to each of the Tax Comparison Year and the Expense Comparison Year, provided, however, that Landlord may, by written notice to Tenant, reasonably revise its estimates for such year and subsequent payments during the Comparison Year shall be based upon such revised estimates.

(b) With reasonable promptness after the end of each Tax and/or Expense Comparison Year, Landlord shall deliver to Tenant a statement setting forth the actual Operating Expenses and Applicable Taxes for the Comparison Year, a comparison with the Operating Expenses and Applicable Taxes for the Base Year and a comparison of any mounts payable under Section 5.2 with the estimated payments made by Tenant. If the amounts payable under Section 5.2 are less than the estimated payments made by Tenant with respect to such Comparison Year, the statement shall be accompanied by a refund of the excess by Landlord to Tenant, or, at Landlord's election, a notice that Landlord shall credit the excess to the next succeeding monthly installments of the Monthly Rent. If the amounts payable under Section 5.2 are more than the estimated payments made by Tenant with respect to such Comparison Year, Tenant shall pay the deficiency to Landlord within ten days after delivery of such statement. Statements provided by Landlord shall be final and binding upon Tenant, if Tenant fails to contest the same within ninety days after the date of delivery to Tenant.

5.4 If the Expiration Date shall occur on a date other than the first or last day of a Comparison Year, Tenant's Tax Share and Tenant's Expense Share for such Comparison Year shall be prorated according to the ratio that the number of days during said Comparison Year that the Lease was in effect bears to 365.

5.5 Notwithstanding anything to the contrary in this Lease, if during any Expense Base Year or Expense Comparison Year the Building is less than 95% occupied, for the purposes of computing Tenant's share of Operating Expenses for said year, those Operating Expenses which vary based upon occupancy levels shall be adjusted as though the Building were 95% occupied; provided, however, in no event shall the aggregate amount billed by Landlord to all tenants in the Building exceed the actual Operating Expenses for said year.

5.6 Tenant shall reimburse Landlord upon demand for any and all taxes required to be paid by Landlord (subject to the same exclusions provided for in Section 5.2(g) in connection with Applicable Taxes), whether or not now customary or within the contemplation of the parties hereto, when:

(a) Said taxes are measured by or reasonably attributable to the cost or value of Tenant's equipment, furniture, fixtures and other personal property located in the Premises or by the cost or value of any above Building Standard Alterations made in or to the Leased Premises by or for Tenant, regardless of whether title to such improvements shall be vested in Tenant or Landlord;

(b) Said taxes are measured by or reasonably attributable to the Base Rent and/or Additional it, Rent payable hereunder, or either of them, including, without limitation, any gross income tax or excise tax levied by any governmental entity (local, state or federal), with respect to the receipt of such Base Rent and/or Additional Rent;

(c) Said taxes are assessed upon or with respect to the possession, leasing, operation, management, maintenance, alteration, repair, use or occupancy by Tenant of the Premises or any portion thereof; or

(d) Said taxes are assessed upon this transaction or any document to which Tenant is a party creating or transferring any interest or an estate in the Leased Premises.

The portion of any taxes payable by Tenant pursuant to this Section 5.6 and other tenants of the Building pursuant to similar provisions in their leases shall be excluded from Applicable Taxes for purpose of computing Tenant's Tax Share thereof.

5.7 In the event that it shall not be lawful for Tenant to reimburse Landlord for the items specified in Section 5.6, the Monthly Rent payable to Landlord under this Lease shall be increased to net Landlord the same net rent after imposition of any such tax upon Landlord as would have been payable to Landlord if any such tax had not been imposed.

SECTION 6. SERVICES TO BE PROVIDED BY LANDLORD

6.1 Subject to Section 5 above, Landlord shall furnish to Tenant, while occupying the Leased Premises, the following services:

(a) Electrical facilities to furnish sufficient power for building standard lighting and customary and usual office machinery in the Leased Premise's, such as typewriters, calculating machines, personal computers, and other machines of similar electrical consumption, but not including any item of electrical equipment which requires electricity in excess of the building standard. Tenant shall pay to Landlord monthly, as billed, such charges as may be separately metered (the cost of such meter and its installation shall be borne by Tenant) or as Landlord's engineer may compute for any electrical service in excess of that stated above;

(b) Water for lavatory and drinking purposes at those points of supply provided for general use of all tenants in the Building;

(c) Air conditioning and heating as reasonably required for comfortable use and occupancy under ordinary office conditions during reasonable and customary office hours, as determined by Landlord; and

(d) Replacement of all standard fluorescent bulbs in all areas and all incandescent bulbs in public areas, rest room areas, and

stairwells. Routine maintenance and

electric lighting service for all public areas of the Building in a manner and to the extent deemed by Landlord to be standard.

6.2 Landlord shall not be liable for any loss or damage arising or alleged to arise in connection with the failure, stoppage or interruption of any such services; nor shall the same be construed as an eviction of Tenant, result in an abatement of Rent, entitle Tenant to any reduction in Rent, or relieve Tenant from the operation of any covenant or condition of this Lease. Landlord reserves the right to temporarily discontinue such services or any of them at such times as may be necessary or appropriate by reason of accident, unavailability of employees, repairs, alterations, or improvements, or strikes, lockouts, riots, acts of God or any other happening or occurrence beyond the reasonable control of Landlord. In the event of any such failure, stoppage or interruption of services, Landlord shall use reasonable diligence to have the same restored. Neither diminution nor shutting off of light or air or both nor any other effect on the Building by any structure erected or condition now or subsequently existing on lands adjacent to the Building shall affect this Lease, abate Rent, or otherwise impose any liability on Landlord.

6.3 Landlord shall have the right to reduce heating, cooling or lighting within the Leased Premises and in the public area in the Building as required by any mandatory fuel or energy-saving program. Landlord shall be entitled to cooperate voluntarily in a reasonable manner with the efforts of national, state or local governmental bodies or of' suppliers of utilities in reducing energy or other resources consumption. Landlord's acts under this Section 6.3 shall not affect this Lease, abate Rent or otherwise impose any liability on Landlord.

6.4 Unless otherwise provided by Landlord, Tenant shall separately arrange with the applicable local public authorities or utilities, as the case may be, for the furnishing of and payment for all telephone services as may be required by Tenant in the use of the Leased Premises. Tenant shall directly pay for such telephone services, including the establishment and connection thereof, at the rates charged for such services by said authority or utility. The failure of Tenant to obtain or to continue to receive such services for any reason whatsoever shall not relieve Tenant of any of its obligations under this Lease.

6.5 The above services are the only services which Landlord shall be required to provide to Tenant. Without limiting the foregoing, Landlord shall not be required to provide, and Tenant expressly waives, any right to receive, any security services with respect to the Leased Premises or the Building. It is expressly understood and agreed that Landlord shall have no liability to Tenant for injury or losses due to theft or burglary caused by unauthorized persons in the Building.

SECTION 7. REPAIRS AND MAINTENANCE BY LANDLORD

7.1 Landlord shall provide for the cleaning and maintenance of the public portions of the Building in keeping with the ordinary standard for office buildings similar to the Building as a pan of Operating Expenses. Unless otherwise expressly stipulated herein, Landlord shall not be required to make any improvements or repairs of any kind or character to the Leased Premises during the Term, except such repairs as may be required to the exterior walls, corridors, windows, roof and other structural elements and equipment of the Building, and such additional maintenance as may be necessary because of the damage caused by persons other than Tenant, its agents, employees, licensees or invitees.

7.2 Landlord, or Landlord's officers, agents and representatives (subject to any security regulations imposed by any governmental authority) shall have the right to enter all parts of the Leased Premises at all reasonable hours to inspect, make repairs, alterations, and additions to the Building or the Leased Premises which Landlord may deem necessary or desirable, to make repairs to adjoining spaces, to cure any Event of Default of Tenant that Landlord elects to cure, to show the Leased Premises to prospective Tenants, or to provide any service which it is obligated or elects to furnish to Tenant. Tenant shall not be entitled to any abatement or reduction of Rent by mason of Landlord's right of entry. Landlord shall have the right to enter the Leased Premises at any time and by any means in the case of an emergency. Tenant hereby waives and releases its right to make repairs at Landlord's expenses under Sections 1932(1), 1941 and 1942 of the California Civil Code or under any similar law, statute or ordinance now or subsequently in effect.

SECTION 8. REPAIRS AND CARE OF BUILDING BY TENANT

8.1 If the Building or any portion of the Building, including without limitation, the elevators, boilers, engines, pipes and other apparatus, or elements of the Building (or any of them) used for the purpose of climate control of the Building or operating the elevators, or if the water pipes, drainage pipes, electric lighting or other equipment of the Building or the roof or outside walls of the Building or the Leased Premises' improvements including without limitation, the carpet, wall covering, doors and woodwork, become damaged or are destroyed through negligence, carelessness or misuse by Tenant, its agents, employees, licensees or invitees, or through it or them, then the cost of the necessary repairs, replacements or alterations shall be borne by Tenant who shall promptly pay the same on demand to Landlord as Additional Rent. Landlord shall have the exclusive right, but not the obligation, to make any repairs necessitated by such damage.

8.2 At its sole cost and expense, Tenant shall repair or replace any damage or injury done to the Building, or any part of the Building, caused by

Tenant, Tenant's agents, employees, licensees or invitees which Landlord elects not to repair. Tenant shall not injure the Building or the Leased Premises and shall maintain the Leased Premises in a clean, attractive condition and in good repair. If Tenant fails to keep the Leased Premises in such good order, condition and repair as required under this Lease to Landlord's reasonable satisfaction, Landlord may restore the Leased Premises to such good order and condition and make such repairs without liability to Tenant for any loss or damage that may accrue to Tenant's property or business by reason of the same, and upon completion, Tenant shall pay to Landlord, as Additional Kent, upon demand, the cost of restoring the Leased Premises to such good order and condition and of the making of such repairs plus an additional charge of fifteen percent (15%) thereof. Upon the Termination Date, Tenant shall surrender and deliver up the Leased Premises to Landlord in the same condition as existed at the Commencement Date, excepting only ordinary wear and tear and damage arising from any cause not required to be repaired by Tenant. Upon the Termination Date, Landlord shall have the right to reenter and take possession of the Leased Premises.

SECTION 9. TENANT'S EQUIPMENT AND INSTALLATIONS; EXCESS UTILITIES

Except for desk or table mounted typewriters, calculating machines, personal computers, and other similar office equipment, Tenant shall not install within the Leased Premises any fixtures, equipment, facilities or other improvements without the specific written consent of Landlord. Tenant

shall not, without Landlord's prior written consent, use heat generating machines other than normal fractional horsepower office machines, or equipment or lighting other than building standard lights in the Leased Premises which may affect the temperature otherwise maintained by the air conditioning system or increase the electricity or water normally furnished for the Leased Premises. If such consent is given, Landlord shall have the right to install supplementary air conditioning units or other facilities in the Leased Premises, and the cost thereof, including the cost of installation, operation and maintenance, increased wear and tear on existing equipment and other similar charges, shall by paid by Tenant to Landlord upon billing by Landlord. Said costs shall include the cost of electrical metering or surveying necessary 1o determine the additional operating cost attributable to the supplementary equipment. Landlord shall also have the light to impose reasonable additional charges (payable by Tenant to Landlord upon billing) by reason of Tenant's off-hours or additional use of utilities or services, for the use of non-standard machine, s, equipment or lighting, and because of the carelessness of Tenant or the nature of Tenant's business. Tenant shall not, without Landlord's prior written consent, install additional lighting or equipment requiring electric current to be supplied to the Leased Pries in excess of the building standard. If such consent is given, Tenant shall pay to Landlord upon billing for the cost of such excess consumption.

SECTION 10. FORCE MAJEURE

Landlord shall not be liable for, and Tenant shall not be entitled to any reduction of the Base Rent or Additional Rent by reason of, Landlord's failure to furnish any of the services or utilities described in this Lease such failure is caused by acts of God, accident, breakage, repairs, strikes, lockouts or other labor disturbances or disputes of any character, interruption of service by suppliers thereof, unavailability of materials or labor, or by any other cause, similar or dissimilar, beyond the reasonable control of Landlord, or by rationing or restrictions on the use of said services and utilities due to energy shortages or other causes, or the making of repairs, alterations or improvements to the Leased Premises or Building, whether or not any of the above result from acts or omissions of Landlord. Furthermore, Landlord shall not be liable under any circumstances for a loss of or injury to property or for injury to or interference with Tenant's business, including, without limitation, loss of profits, however occurring, through or in connection with or incidental to failure to furnish any of the foregoing services or utilities, and Tenant shall not be relieved of its obligation to pay the full Base Rent or Additional Rent by reason of the same.

SECTION 11. MECHANIC'S SAD MATERIALMAN'S LIENS

11.1 Tenant shall not suffer or permit any mechanic's or materialman's lien to be filed against the Leased Premises or any portion of the Building by reason of work, labor, services, or materials supplied or claimed to have been supplied to Tenant. Nothing in this Lease shall be deemed or construed in any way as constituting the consent or request of Landlord, expressed or implied, by inference or otherwise, for any contractor, subcontractor, laborer or materialman to perform any labor or to furnish any materials or to make any specific improvement, alteration or repair of or to the Leased Premises or any portion of the Building, nor of giving the Tenant any right, power or authority to contract for, or permit the rendering of, any services or the furnishing of any materials that could give rise to the filing of any mechanic's or materialman's lien against the Leased Premises or any portion of the Building. Landlord shall have the right at all times to post and keep posted on the Leased Premises any notices which it deems necessary for protection from such liens.

11.2 If any such mechanic's or materialman's lien shall at any time be filed against the Leased Premises or any portion of the Building as the result of any act or omission of Tenant, Tenant covenants that it shall, within ten (10) days after Tenant has notice of the claim for lien, procure the discharge thereof by payment or by giving security or in such other manner as may be required or permitted by law or which .shall otherwise satisfy Landlord. If Tenant fails to take such action, Landlord, in addition to any other right or remedy it may have, may take such action as may be reasonably necessary to

protect its interests. Any amounts paid by Landlord in connection with such action and all reasonable legal and other expenses of Landlord incurred in connection with the same, in. eluding reasonable attorney's fees, court costs and other necessary disbursements shall be repaid by the Tenant to the Landlord on demand.

SECTION 12. INSURANCE

12.1 Landlord shall maintain during the Term a commercial (comprehensive) insurance policy (written on an occurrence, not claims made, basis) including coverage for contractual liability, public liability and property damage in a commercially reasonable amount, as determined by Landlord, covering the Building. Landlord may maintain during the Term a policy of insurance insuring the Building against loss or damage due to fire and other casualties covered by a standard "all risk" coverage policy. Such coverage in such amounts as Landlord may from time to time determine may include the risks of lightning, vandalism and malicious mischief, and, at the option of Landlord, the risks of earthquakes and additional hazards, a rental loss endorsement and one or more loss payee endorsements in favor of the holders of any mortgages or deeds of trust encumbering the interest of Landlord in the Building or the ground or underlying lessors. The parties acknowledge that the premiums for insurance specified in Section 12.1 are Operating Expenses, as defined in Section 5.

12.2 At its own expense, Tenant shall maintain during the Term a commercial (comprehensive) liability insurance policy (written on an occurrence, not claims made, basis), including coverage for contractual liability, public liability and property damage in the amount of Two Million and 00/100 Dollars ($2,000,000.00) per person and per occurrence for personal injuries or deaths of persons occurring in or about the Leased Premises.

12.3 At its own expertise, Tenant shall maintain during the Term "all risk" casualty insurance for the full replacement value of all Alterations and all of Tenant's Property and other items in the Premises.

12.4 At its own expense, Tenant shall maintain during the Term workers' compensation insurance and all such other insurance as may be required by applicable Laws.

12.5 All such insurance shall: (i) name Landlord, and any oilier party which Landlord so specifies, as additional insureds; (ii) specifically cover the liability assumed by Tenant under this Lease; (iii) be issued by an insurance company which has a general policy holder's rating of not less than "A", and a financial rating of not less than Class "X", in the most current edition of Best's Insurance Reports, and is licensed to do business in the State of' California; (iv) be primary insurance as to all claims thereunder; (v) provide that said insurance shall not be canceled or coverage changed unless thirty (30) days' prior written notice shall have been given to Landlord, any other named insured and the holders of any mortgages or deeds of trust referred to above; and (vi) shall not eliminate cross-liability and shall

contain a severability of interest clause. Tenant shall deliver certificates thereof to Landlord on or before the Commencement Date and at least thirty days before the expiration dates thereof. In the event Tenant shall fail to procure such insurance, or to deliver such certificates, Landlord may, without waiving any of its rights or remedies, procure such policies for the account of Tenant, and the cost thereof shall be paid to Landlord as Additional Rent within five days after delivery to Tenant of bills therefor. Tenant's compliance with the provisions of this Section 12 shall in no way limit Tenant's liability under any of the other provisions of this Lease. The limits of insurance required to be maintained by Tenant hereunder shall not be a limitation on any obligation of Tenant, including Tenant's indemnification obligations under Section 21 below. Not more frequently than once every two years, Landlord may require Tenant to increase the amount of liability insurance coverage if, in the opinion of Landlord's lender or insurance consultant, the amount of such coverage is not then adequate.

12.6 Landlord and Tenant shall have their respective insurance companies issuing property damage insurance waive any rights of subrogation that such companies may have against Landlord or Tenant, as the case may be, so long as the insurance carried by Landlord and Tenant, respectively, is not invalidated thereby. As long as such waivers of subrogation are contained in their respective insurance policies, Landlord and Tenant hereby waive any right that either may have against the other on account of any loss or damage to their respective property to the extent such loss or damage is insured under policies of insurance for fire and all risk coverage, theft, public liability, worker's compensation or other similar insurance.

SECTION 13. QUIET ENJOYMENT

Provided Tenant has performed all its obligations under this Lease, including but not limited to the payment of Rent and all other sums due hereunder, Tenant shall peace, ably and quietly hold and enjoy the Leased Premises for the Term, without hindrance by Landlord, subject to the provisions and conditions set forth in this Lease.

SECTION 14. TENANT IMPROVEMENT ALLOWANCE

Landlord shall construct or install in the Leased Premises the improvements (the "TENANT IMPROVEMENT WORK") as specified in, and in accordance with the provisions of attached Exhibit C. Landlord shall provide an allowance (the
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"TENANT IMPROVEMENT ALLOWANCE") in the amount specified in Exhibit C. The
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Tenant Improvement Allowance shall be applied to the actual costs of the Tenant Improvement Work. Any costs of the Tenant Improvement Work in excess of the

Tenant Improvement Allowance shall be paid by Tenant.

SECTION 15. ALTERATIONS

15.1 Tenant shall not make or allow to be made any alterations, physical additions, or improvements in or to the Leased Premises (collectively, "ALTERATIONS") without first obtaining Landlord's written consent in each instance, which consent may be given or withheld in Landlord's sole discretion. At the time of said request, Tenant shall submit to Landlord plans and specifications of the proposed Alterations. Landlord shall have a period of not less than sixty days therefrom in which to review and approve or disapprove said plans. Tenant shall pay upon demand the reasonable costs of Landlord's review of such plans and specifications, not to exceed One Thousand Dollars ($1,000.00).

The contractor or person selected by Tenant to make such Alterations must be approved in writing by Landlord prior to commencement of any work. Such contractor or person shall carry insurance in forms and amounts reasonably satisfactory to Landlord and shall at all times be subject to Landlord's rules and regulations while in the Building. All Alterations shall be performed in full compliance with plans and specifications approved by Landlord, all applicable Laws and the requirements of the Board of Underwriters, Fire Rating Bureau or similar body. All Alterations shall be performed at Tenant's sole cost and expense (including reasonable costs for Landlord's supervision, not to exceed 5% of the project's cost), at such time and in such manner as Landlord may designate, and shall be promptly completed in a good and workmanlike manner. Tenant shall reimburse Landlord's review and supervision costs within thirty days after receipt of Landlord's invoice(s) therefor. Landlord's approval of the plans, specifications and working drawings for Tenant's Alterations shall create no responsibility or liability on the part of Landlord for their completeness, design sufficiency, or compliance with all applicable Laws.

15.2 Tenant shall give to Landlord at least fifteen business days' prior written notice of commencement of construction of any Alterations. Landlord shall have the right to require that (a) any contractor hired by .Tenant shall, prior to commencing work in the Leased Premises, provide Landlord with a performance bond and labor and materials payment bond in the amount of the contract price for the work, naming Landlord and Tenant (and any other persons designated by Landlord) as co-obligees, and that (b) any such contractor employ such labor as necessary to avoid any delay in or interruption to the progress of work under in the Leased Premises or elsewhere in the Building due to union picket lines. Tenant's contractors shall not use any portion of the common areas of the Building for performance of the work unless the written consent of Landlord is first obtained. The granting or withholding of such consent shall be at Landlord's sole discretion.

15.3 All Alterations, whether made by Tenant or Landlord or at either's

expense, including, without limitation, all Tenant Improvement Work and all carpeting and fixtures of any kind, shall become a part of the Building immediately upon installation in the Leased Premises, and shall be and remain the property of Landlord, except for trade fixtures, office supplies and moveable furniture and furnishings placed on the Premises by Tenant that are removable without damage to the Building or the Leased Premises, which shall be subject to Section 16. Notwithstanding any other provisions of this Lease, upon Landlord's written request made within thirty days prior to the expiration or termination of this Lease, Tenant at Tenant's sole cost and expense shall promptly remove any Alterations or Tenant Improvement Work, designated by Landlord to be removed and repair any damage to the Promises or the Building resulting from such removal.

15.4 Tenant shall be responsible for the entire cost of the Alterations and Tenant Improvement Work (subject to Landlord's obligation to fund the Tenant Improvement Allowance), including any cost or expense of Landlord, relating to the interior of the Leased Premises, on account of the need to comply with the ADA (as defined in Section 34) or other Laws. Under no circumstances shall Landlord be responsible to Tenant or any third party for determining whether the Alterations comply with all applicable Laws, including the ADA, regardless of whether Tenant must obtain Landlord's approval of the Alterations or the plans and specifications therefor as a condition to making them.

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15.5 Should any construction, alteration, addition, improvements or decoration of the Leased Premises by Tenant interfere with harmonious labor relations in the Building, all such work shall be halted immediately by Tenant until such time as construction can proceed without such interference.

SECTION 16. FURNITURE, FIXTURES AND PERSONAL PROPERTY

16.1 Tenant, at its sole cost and expense, may remove its trade fixes, office supplies and moveable office furniture and equipment not attached to the Building or Leased Premises provided:

(a) such removal is made prior to the Termination Date;

(b) no Event of Default exists at the time of such removal; and

(c) Tenant promptly repairs all damage caused by such removal.

16.2 If Tenant does not remove its trade fixtures, office supplies and moveable furniture and equipment prior to the Termination Date (unless prior arrangements have been made with Landlord and Landlord has agreed in writing to permit Tenant to leave such items in the Leased Premises for an agreed period), then, in addition to its other remedies at law or in equity, Landlord shall have the right to have such items removed and stored at Tenant's sole cost and

expense and all damage to the Building or the Leased Premises resulting from said removal shall be repaired at Tenant's cost. Any such items not removed prior to the Termination Date, shall, at Landlord's option, subject to applicable Laws, become the property of Landlord upon the Termination Date, and Tenant shall not have any further rights with respect thereto or reimbursement therefor.

16.3 All furnishings, Fixtures, equipment, effects and property of every kind, nature and description of Tenant and of all persons claiming by, through or trader Tenant which, during the Term or any occupancy of the Leased Premises by Tenant or anyone claiming under Tenant, may be on the Leased Premises or elsewhere in the Building shall be at the sole risk and hazard of Tenant If the whole or any part thereof is destroyed or damaged by fire, water or otherwise, or by the leakage or bursting of water pipes, steam pipes, or other pipes, by theft, or from any other cause, no part of said loss or damage is to be charged to or be borne by Landlord.

SECTION 17. TAXES

During the Term, Tenant shall pay, prior to delinquency, all business and other taxes, charges, notes, duties and assessments levied, and rates or fees imposed, charged, or assessed against or in respect of Tenant's occupancy of the Leased Premises or in respect of the personal property, trade fixtures, furnishings, equipment, and all other personal property of Tenant contained in the Building, and shall hold Landlord harmless from and against all payment of such taxes, charges, notes, duties, assessments, rates, and fees. Tenant shall cause said fixtures, furnishings, equipment, and other personal property to' be assessed and billed separately from the real and personal property of Landlord. In the event any or all of Tenant's fixtures, furnishings, equipment, and other personal property shall be assessed and taxed with Landlord's real property, Tenant shall pay to Landlord Tenant's share of such taxes within ten days after delivery to Tenant by Landlord of a statement in writing setting forth the amount of such taxes applicable to Tenant's property.

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SECTION 18. ASSIGNMENT AND SUBLETTING

18.1 Neither Tenant nor Tenant's legal representatives nor successors in interest by operation of law or other shall assign this Lease or sublease the Leased Premises or any part thereof or mortgage, pledge or hypothecate its leasehold interest, nor make any attempt to do so, without the prior express written consent of Landlord. Any such attempt shall be void, of no effect, and constitute an Event of Default This prohibition against assigning or subletting shall be construct to include a prohibition against any assignment or subletting by operation of law. The voluntary or other surrender of this Lease by Tenant or a mutual cancellation hereof shall not work a merger and shall, at the option of Landlord, terminate all or any existing subleases or may, at the option of

Landlord, operate as an assignment to Landlord of Tenant's interest in any or all such subleases.

18.2 The following shall constitute a prohibited assignment subject to Section 18.1 a sale, transfer, pledge or hypothecation by Tenant of all or substantially all of its assets or all or substantially all of its stock, if Tenant's stock is publicly traded; a merger of Tenant with another corporation; the sale, transfer, pledge or hypothecation of fifty percent or more of Tenant's stock if Tenant's stock is not publicly waded; or the sale, transfer, pledge or hypothecation of fifty percent or more Tenant's beneficial ownership interest if Tenant is a partnership; provided, however, that Landlord's consent shall not be required for the assignment of the Lease or subletting of the Leased Premises to a Permitted Affiliate. For purposes hereof, the term "Permitted Affiliate" means a subsidiary of Tenant with an independent net worth as of the date of the proposed assignment or subletting equal to or greater than the net worth of Tenant as of the date hereof.

18.3 If Tenant should desire to assign this Lease or sublease the Leased Premises or any portion thereof, Tenant shall give Landlord written notice of such desire to make such assignment or effect such sublease. At the time of giving such notice, Tenant shall provide Landlord with a copy of the proposed assignment or sublease document, and such information as Landlord may reasonably request concerning the proposed sublessee or assignee to assist Landlord in making an informed judgment regarding the financial condition, reputation, operation and general desirability of the proposal sublessee or assignee. Landlord shall then have a period of thirty days following receipt of such notice within which to notify Tenant in writing of Landlord's election to:

(a) terminate this Lease as to the space so affected as of the date specified by Tenant, in which event Tenant shall be relieved of all obligations accruing under this Lease after the termination as to the Leased Premises or such portion, after paying all Rent due as of the Termination Date, or

(b) permit Tenant to assign or sublet the Lease Premises or such portion, or

(c) refuse to consent to Tenant's assignment or subleasing of the Leased Premises or such portion and to continue this Lease in full force and effect as to the entire Leased Premises.

If Landlord should fail to notify Tenant of its election within the thirty day period, Landlord shall be deemed to have elected option (c). In the event of any approved assignment or subletting, the rights of

any such assignee or sublessee shall be subject to all of the terms, conditions

and provisions of this Lease, including without limitation, restrictions on use and the covenant to pay Rent. If Landlord, approves the proposed assignment or sublease, Tenant may, not later than ninety days thereafter, enter into such assignment or sublease with the proposed assignee or sublessee upon the terms and conditions set forth in the notice provided to Landlord, and 50% of the Excess Rent received by Tenant shall be paid to Landlord as and when received by Tenant. For purposes hereof "EXCESS RENT" means any rent or other consideration received by Tenant in excess of (i) the Base Rent and Additional Rent payable hereunder (or the amount thereof proportionate to the portion of the Leased Premises subject to such sublease in the case of a sublease of a portion of the Premises) and (ii) reasonable brokerage commissions incurred in connection with such sublease or assignment. No such consent to or recognition of any such assignment or subletting shall constitute a release of Tenant or any guarantor of Tenant's performance from further performance by Tenant or such guarantor of covenants undertaken to be performed by Tenant. Tenant and/or such guarantor shall remain liable and responsible for all Rent and other obligations of Tenant under this Lease. Consent by Landlord to a particular assignment, sublease or other transaction shall not be deemed a consent to any other or subsequent transaction. Whether or not Landlord consents to any assignment, sublease or other transaction, Tenant shall pay any reasonable attorneys' fees incurred by Landlord in connection with such transaction. All documents utilized by Tenant to evidence any subletting or assignment for which Landlord's consent has been requested, shall be subject to prior approval by Landlord or its attorney. If any consideration payable to Tenant by any sublessee, assignee, licensee or other transferee exceeds the Rent, then Tenant shall pay to Landlord all such excess within ten days following receipt by Tenant.

18.4 If this Lease is assigned to any person or entity pursuant to the provisions of the Bankruptcy Code, 11 U.S.C. Section 101 et. seq. (the "BANKRUPTCY CODE"), any and all monies or other consideration payable or otherwise to be delivered in connection with such assignment shall be paid or delivered to Landlord, shall be and remain the exclusive property of Landlord, and shall not constitute property of Tenant or of the estate of Tenant within the meaning of the Bankruptcy Code. Any such monies or other consideration not paid or delivered to Landlord shall be held in trust for the benefit of Landlord and shall be promptly paid or delivered to Landlord. Any person or entity to whom this Lease is so assigned shall be deemed, without further act or deed, to have assumed all of the obligations arising under this Lease as of the date of such assignment. Upon demand therefor, any such assignee shall execute and deliver to Landlord an instrument confirming such assumption. In no event shall Tenant have any right to sublet or assign if there exists any default under this Lease.

18.5 Notwithstanding the above, any consents required by Landlord under this Section 18 shall not be unreasonably withheld or untimely delayed.

SECTION 19. FIRE AND CASUALTY

19.1 If the Leased Premises or any part thereof shall be damaged by fire

or other casualty, Tenant shall give prompt written notice to Landlord. If (i) in Landlord's reasonable opinion the insurance proceeds available to Landlord are not insufficient for restoration, or (ii) in Landlord's reasonable opinion the Building shall be so damaged by fire or other casualty that substantial alteration or reconstruction of the Building shall be required (whether or not the Leased Premises shall have been damaged by such fire or other casualty), or (iii) if any mortgagee under a mortgage or deed of trust covering the Building requires that the insurance proceeds payable as a result of said fire or other

casualty be used to retire the mortgage debt; then Landlord, at its option, may terminate this Lease by notifying Tenant in writing of such termination within sixty days after the date of such damage or casualty, in which event the Rent shall be abated proportionately as of the date of such damage, based upon the extent the Leased Premises are rendered unfit for occupancy.

19.2 If Landlord does not elect to terminate this Lease as provided in Section 19.1, and if repairs have not been commenced within ninety days from the date of such damage and thereafter completed within nine months (excluding delays caused by force majeure events, as described in Section 10), then Tenant may terminate this Lease upon thirty days written notice to Landlord; provided, however, that if Landlord completes repairs within thirty days' after receipt of Tenant's termination notice (or such longer period of time as it reasonably required because the delays were due to force majeure events), then Tenant's exercise of its termination right shall be void and this Lease shall continue in effect

19.3 To the extent of the insurance proceeds available to Landlord therefor, Landlord shall repair and restore the Building and/or the Leased Premises to substantially the same condition in which they were immediately prior to the fire or other casualty, except that Landlord shall not be required to rebuild, repair or replace any part of Tenants Alterations, trade fixtures, office supplies and materials, furniture and equipment. Landlord shall not be liable for any inconvenience, annoyance, or injury done to the business of Tenant resulting in any way from such damage or the repair thereof, except Landlord shall allow Tenant an equitable reduction of Rent during the time and to the extent the Leased Premises are unfit for occupancy, save for Tenant's fault or negligence described in Section 19.4.

19.4 If the Leased Premises or the Building shall be totally or partially damaged by fire or other casualty resulting from the fault or negligence of Tenant, or its agents, employees, licensees, or invitees, such damage shall be repaired by and at the expense of Tenant (to the extent that such destruction or damage is not covered by the fire and extended coverage insurance carried by Landlord as provided in Section 12), under the direction and supervision of Landlord, and Rent shall continue without abatement.

19.5 The provisions of this Lease, including this Section 19, constitute an express agreement between Landlord and Tenant with respect to any and all damage to, or destruction of, all or any part of the Leased Premises, the Building or any other portion of the Real Property, and any statute or regulation of the State of California, including without limitation, Sections 1932(2) and 1933(4) of the California Civil Code, with respect to any rights or obligations concerning damage or destruction in the absence of an express agreement between the parties and any other statute or regulation, now or subsequently in effect, shall have no application to this Lease or any damage or destruction to all or any part of the Premises, the Building or any other portion of the Real Property. Tenant hereby specifically waives all rights to terminate this Lease under said Civil Code sections or any similar provisions of law.

SECTION 20. CONDEMNATION

20.1 If any part of the Leased Premises or the Building is taken by exercise of the power of eminent domain, or by conveyance in lieu thereof, Landlord may elect to terminate this Lease upon written notice to Tenant within thirty days after the date of such taking or transfer in lieu thereof or to

continue the same in effect. All compensation awarded for any taking (or the proceeds of private sale in lieu thereof) of the Leased Premises or the Building shall be the property of Landlord, and Tenant hereby assigns its interest in any such award to Landlord; provided, however, Landlord shall have no interest in any award made to Tenant for the taking of Tenant's personal property or moving expenses if a separate award for such items is made to Tenant. If this Lease is terminated under this Section 20. l, Rent shall be payable up to the date that possession is taken by the condemning authority, Landlord shall refund to Tenant any prepaid unaccrued Rent less any sum then owing by Tenant to Landlord, and Tenant shall have no claim against Landlord for the value of any unexpired portion of the Term.

20.2 In the event of a taking of any portion of the Leased Premises, or a conveyance in lieu thereof, and if this Lease is not terminated by Landlord as provided above, then this Lease shall automatically terminate as to the portion of the Leased Premises so taken as of the earlier of the date of vesting of title or the date possession is taken by the condemning authority, and the Base Rent as well as the Additional Rent shall be apportioned according to the ratio that the remaining Rentable Area of the Leased Premises bears to the total original Rentable Area of the Leased Premises. Tenant hereby waives any and all rights it might otherwise have pursuant to Section 1265.130 of California Code of Civil Procedure or any similar provisions of Laws now or subsequently in effect.

20.3 In the event of temporary taking of all or any portion of the Leased

Premises for a period of ninety days or less, then this Lease shall not terminate but the Base Rent and the Additional Rent shall be abated for the period of such taking in proportion to the ratio that the remaining Rentable Area of the Leased Premises bears to the total Rentable Area of the Leased Premises. Landlord shall be entitled to receive the entire award made in connection with any such temporary taking.

SECTION 21. INDEMNIFICATION

21.1 Landlord shall not be liable to Tenant for and Tenant hereby waives all claims against Landlord for damage to any property or injury, illness or death of any person in, upon, or about the Leased Premises, the Building or the Real Property arising at any time and from any cause whatsoever except to the extent caused by the gross negligence or willful misconduct of Landlord or its employees or agents. Without limiting the generality of the foregoing, Landlord shall not be liable for any damage or damages of any nature whatsoever to persons or property caused by explosion, fire, theft or breakage, by sprinkler, drainage or plumbing systems, by failure for any cause to supply adequate drainage, by the intention of any public utility or service, by steam, gas, water, rain or other substances leaking, issuing or flowing into any part of the Leased Premises, by natural occurrence, acts of a public enemy, riot, strike, insurrection, war, court order, requisition or order of governmental body or authority, or for any damage or inconvenience which may arise through repair, maintenance or alteration of any part of the Building, or by anything done or omitted to be done by any tenant, occupant or person in the Building. In addition, Landlord shall not be liable for any loss or damage for which Tenant is required to insure or for any loss or damage resulting from any construction, alterations or repair by Landlord or by others.

21.2 Tenant shall defend, with counsel approved by Landlord, all actions against Landlord, any partner, trustee, stockholder, officer, director, employee or beneficiary of Landlord, holders of mortgages secured by the Leased Premises or the Building and any other party having an interest therein ("INDEMNIFIED PARTIES") with respect to, and shall pay, protect, indemnify and save harmless, to the

extent permitted by law, all Indemnified Parties from and against, any and all liabilities, losses damages, costs, expenses (including reasonable attorneys' fees and expenses), causes of action, suits, claims, demands or judgments of any nature (i) to which any Indemnified Party is subject because of its estate or interest in the Leased Premises or the Building or the Real Property, or (ii) arising from (1) injury to or death of' any person, or damage to or loss of property, on the Leased Premises, the Building or the Real Property, or on adjoining sidewalks, streets or ways; or connected with the use, condition or occupancy of any thereof (except to the extent caused by the gross negligence or willful misconduct of Landlord or its agents or employees), (2) any violation by

Tenant in the observance or performance of its obligations under this Lease, or (3) any act, fault, omission, or other misconduct of Tenant or its agents, contractors, licenses, sublessees or invitees. Tenant shall use and occupy the Leased Premises and other facilities of the Building at its own risk, and hereby releases the Indemnified Parties from any and all claims for any damage or injury to the fullest extent permitted by law.

21.3 The provisions of this Section 21 shall survive the expiration or sooner termination of this Lease.

SECTION 22. DEFAULT BY TENANT

22.1 The term "EVENT OF DEFAULT" refers to the occurrence of any one or more of the following:

(a) failure of Tenant to pay when due any sum required to be paid hereunder (a "MONETARY DEFAULT")

(b) failure of Tenant, after ten (10) days Written notice, to perform any of Tenant's obligations, covenants or agreements except a Monetary Default;

(c) if Tenant, or any guarantor of Tenant's obligations under this Lease (a "GUARANTOR"), admits in writing that it cannot meet its obligations as they become due; or is declared insolvent according to any law; or assignment of Tenant's or Guarantor's property is made for the benefit of creditors; or a receiver or trustee is appointed for Tenant or Guarantor or its property; or the interest of Tenant or Guarantor under this Lease is levied on under execution or other legal process; or any petition is filed by or against Tenant or Guarantor to declare Tenant bankrupt or to delay, reduce or modify Tenant's debts or obligations; or any petition is fried or other action taken to reorganize or modify Tenant's or Guarantor's capital structure, if Tenant is a corporation or other entity; provided that, any involuntary levy, execution, legal process or petition filed against Tenant or Guarantor shall not constitute an Event of Default provided Tenant or Guarantor shall vigorously contest the same by appropriate proceedings and shall remove or vacate the same within sixty days from the date of its creation, service or filing;

(d) the abandonment of the Leased Premises by Tenant, which shall mean that Tenant has vacated the Leased Premises for ten consecutive days, whether or not Tenant is in Monetary Default; or that Tenant, in the judgment of Landlord, is vacating the Leased Premises by removing fracture and fixtures;

(e) the discovery by Landlord that any financial statement given by Tenant or any of its assignees, subtenants or successors-in-interests, or Guarantors, was materially false; or

(f) if Tenant or any Guarantor shall die, cease to exist as a corporation or partnership or be otherwise dissolved or liquidated or become insolvent, or shall make a transfer in fraud of creditors.

22.2 Upon the occurrence of any Event Default by Tenant, Landlord may at any time thereafter, without limiting Landlord in the exercise of any right or remedy which Landlord may have under this Lease, at law or in equity by mason of such Event of Default:

(a) Terminate this Lease and recover from Tenant as provided by California Civil Code Section 1951.2: (i) the worth at the time of award of the unpaid rent and other amounts which had been earned at the time of termination; (ii) the worth at the time of award of the amount by which the unpaid rent which would have been earned after termination until the time of award exceeds the amount of such rental loss that Tenant proves could have been reasonably avoided; (iii) the worth at the time of award of the amount by which the unpaid rent for the balance of the Term after the time of award exceeds the amount of such rental loss that Tenant proves could be reasonably avoided; and (iv) any other amount necessary to compensate Landlord for all the detriment proximately caused by Tenant's failure to perform its obligations under this Lease. or which, in the ordinary course of things, would be likely to result therefrom. The "worth at the time of award" of the amount referred to in (iii) shall be computed by discounting such mount at the discount rate of the Federal Reserve Bank of San Francisco at the time of award plus one percent (1%). For purposes of computing unpaid rent which would have accrued and become payable under this Lease pursuant to the provisions of this subsection (a), unpaid rent shall consist of the sum of the unpaid Base Rent and the Additional Rent as reasonably estimated by Landlord for the balance of the Term; or

(b) Continue this Lease in effect and enforce all of its rights and remedies under this Lease, as provided by California Civil Code Section 1951.4, including the right to recover Base Rent and Additional Rent as they become due, for so long as Landlord does not terminate Tenant's right to possession; provided, however, if Landlord elects to exercise its remedies described in this subsection (b) and Landlord does not terminate this Lease, and if Tenant requests Landlord's consent to an assignment of this Lease or a sublease of the Leased Premises at such time as Tenant is in default, Landlord shall not unreasonably withhold its consent to such assignment or sublease. Acts of maintenance or preservation, efforts to relet the Leased Premises, or the appointment of a receiver upon Landlord's initiative to protect its interest under this Lease, shall not constitute a termination of Tenant's right to possession; or

(c) With or without terminating this Lease, to reenter the

Leased Premises and remove all persons and property from the Leased Premises. Such property may be removed and stored in a public warehouse or elsewhere at the cost of and for the account of Tenant. No such reentry shall constitute an election to terminate this Lease unless a written notice of such intention is given to Tenant or unless the termination thereof is decreed by a court of competent jurisdiction. In addition to its other rights under this Lease, Landlord shall have the right, even though tenant is in default and has abandoned the Leased premises, (i) to maintain this Lease in

effect and not terminate Tenant's right to possession, and (ii) to enforce its rights and remedies under this Lease, including the right to recover Base Rent and Additional Rent as they become due under this Lease.

22.3 If Tenant fails to make any payment or cure any Event of Default hereunder within the time permitted, Landlord, without being under any obligation to do so and without thereby waiving such Event of Default, may make the payment and/or remedy the Event of Default for the account of Tenant (and enter the Leased Premises for such purpose), and Tenant shall pay Landlord, upon demand, all reasonable costs, expenses and disbursements plus fifteen percent (15%) overhead cost, incurred by Landlord in connection with such payment or cure.

22.4 Nothing contained in this Section 22 shall limit or prejudice the right of Landlord to prove and obtain as liquidate damages in any bankruptcy, insolvency, receivership, reorganization or dissolution proceeding, an amount equal to the maximum allowed by applicable Law, whether or not such amount is greater, equal to or less than the amounts recoverable, either as damages or Rent, referred to in any of the preceding provisions of this Section 22. Notwithstanding anything contained in this Section 22 to the contrary, any such proceeding or action involving bankruptcy, insolvency, reorganization, arrangement assignment for the benefit of creditors, or appointment of a receiver or trustee, shall be considered to be an Event of Default only when such proceeding, action or remedy shall be taken or brought by or against the then holder of the leasehold estate under this Lease or the guarantor under a Guaranty of this Lease.

22.5 In connection with an Event of Default Tenant shall also be liable and shall pay to Landlord, in addition to any sums provided to be paid above, broker's fees incurred by Landlord in connection with reletting the whole or any part of the Leased Premises, the costs of removing and storing Tenant's or other occupants' property, the costs of repairing, altering, remodeling, or otherwise putting the Leased Premises into condition acceptable to a new tenant or tenants, and all reasonable expenses incurred by Landlord in enforcing or defending Landlord's rights and/or remedies, including reasonable attorneys' fees whether suit was actually filed or not.

22.6 Landlord is entitled to accept, receive, in check or money order, and deposit any payment made by Tenant for any reason or purpose or in any amount whatsoever, and apply them at Landlord's option to any obligation of Tenant, and such amounts shall not constitute payment of any amount owed except that to which Landlord has applied them. No endorsement or statement on any check or letter of Tenant shall be deemed an accord and satisfaction or recognized for any purpose whatsoever. The acceptance of any such check or payment shall be without prejudice to Landlord's rights to recover any and all amounts owed by Tenant and shall not be deemed to cure any other default nor prejudice Landlord's rights to pursue any other available remedy.

22.7 Landlord shall not be in default unless Landlord fails to perform obligations required of Landlord within thirty days after written notice thereof from Tenant to Landlord, and after the notice and other requirements of Section 36 have been meg provided that, if such default cannot reasonably be cured within thirty days then Landlord shall not be in default if it commences to cure the default within the thirty day period and continues diligently to complete the cure within a reasonable time. Any such notice of default shall specify the obligation Landlord has allegedly failed to perform, and shall identify the Lease provision containing such obligation. If, by reason of the occurrence of any of the events

specified in Section 10 hereof, Landlord is unable to fulfill or is delayed in fulfilling any of Landlord's obligations under this Lease or any collateral instrument, no such inability or delay shall constitute an actual or constructive eviction, in whole or in pan, or entitle Tenant to any abatement or diminution of Base Rent or Additional Rent, or relieve Tenant from any of its obligations under this Lease, or impose any liability upon Landlord or its agents by reason of inconvenience or annoyance to Tenant or by mason of injury to or interruption of Tenant's business, loss of profits, or otherwise. Tenant hereby waives and releases its right to terminate this Lease under Section 1932(1) of the California Civil Code or under may similar law, statute or ordinance now or hereafter in effect

SECTION 23. LIEN FOR RENT

To secure the payment of all Rent and the faithful performance of all the other covenants of this Lease to be performed by Tenant, Tenant hereby gives to Landlord an express contract lien on and first security interest in and to all property, equipment, machinery, trade fixtures, chattels and merchandise ("LIEN") which may be placed in the Leased Premises and also upon all proceeds of any insurance which may accrue to Tenant by reason of damage to or destruction of any such property, and agrees that this Lease shall constitute a security agreement with respect thereto. All exemption laws are hereby waived by

Tenant. This Lien is given in addition to any statutory liens and shall be cumulative thereto. Tenant agrees to execute from time to time at the request of Landlord UCC-1 Financing Statements referencing this security agreement in a form satisfactory to Landlord, and to file originals of such statements with the clerk of the cities or towns where (i) the Leased Premises are located, and (ii) Tenant maintains its principal business office or residence, or wherever else such statements would ordinarily be filed to protect creditor's rights under California law. In addition to all other rights of Landlord under this Lease, upon Tenant's default, Landlord shall have all of the remedies of a secured party with respect to said property, equipment, machinery, trade fixtures, chattels and merchandise.

SECTION 24. RIGHT TO RELOCATE

Notwithstanding anything herein to the contrary, Landlord shall in all cases retain the right and power to relocate Tenant upon thirty (30) days' written notice within the Building in such space which is comparable in size and location and suited to Tenant's use, such right and power to be exercised reasonably. Landlord shall not be liable or responsible for any claims, damages or liabilities in connection with or occasioned by such relocation. Landlord's reasonable exercise of such right and power shall include, but not be limited to, a relocation to consolidate the Rentable Area occupied in order to provide Landlord's services more efficiently or a relocation to provide contiguous vacant space for a prospective tenant. If Landlord shall exercise said option, the substituted premises shall hereafter be deemed for the purposes hereof, the "LEASED PREMISES" hereunder, and a new amended Exhibit A showing the new Leased

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Premises will be substituted for the original Exhibit A attached hereto.

Landlord agrees to pay the Tenant's reasonable expenses to move its furniture, fixtures and equipment to such substituted Leased Premises and for reprinting stationary and business cards.

SECTION 25. ATTORNEYS' FEES

If either party commences litigation against the other in connection with this Lease, the parties hereby waive any right to a trial by jury. In the event of such litigation, the prevailing party shall be entitled to recover from the other party such costs and reasonable attorneys' fees as may have been

incurred. Further, if for any reason Landlord consults legal counsel or otherwise incurs any costs or expenses as a result of its rightful attempt to enforce the provisions of this Lease, even though no litigation is commenced, or if commenced is not pursued to final judgment, Tenant shall pay to Landlord, in

addition to all other amounts for which Tenant is obligated, all of Landlord's reasonable costs and expenses incurred in connection with any such acts, including reasonable attorneys fees.

SECTION 26. NON-WAIVER

Neither acceptance of any payment by Landlord from Tenant nor failure by Landlord to complain of any action, non-action, or default of Tenant shall constitute a waiver of any of Landlord's rights. Time is of the essence with respect to the performance of every obligation of Tenant under this Lease. Waiver by Landlord of any right in connection with any Event of Default shall not constitute a waiver of such right or remedy or any other right or remedy arising in connection with either a subsequent Event of Default with respect to the same obligation or any other obligation. No right or remedy of Landlord or covenant, duty, or obligation of Tenant shall be deemed waived by Landlord unless such waiver is in writing, signed by Landlord or Landlord's duly authorized agent.

SECTION 27. RULES AND REGULATIONS

Tenant shall comply with the rules and regulations set forth in Exhibit B.

Landlord shall have the right at all times to change such rules and regulations or to amend them in any manner as-may be deemed advisable by Landlord, all of which changes and amendments shall be sent by Landlord to Tenant in writing. Tenant shall thereafter comply with the changed or amended rules and regulations. Landlord shall have no liability to Tenant for any failure of any other tenants of the Building to comply with such rules and regulations.

SECTION 28. ASSIGNMENT BY LANDLORD

Landlord shall have the right to transfer, in whole or in part, all its rights and obligations under this Lease and in the Leased Premises and the Building.

SECTION 29. LIABILITY OF LANDLORD

The obligations of Landlord under this Lease shall be binding upon Landlord and its successors and assigns and any furore owner of the Building only with respect to events occurring during its and their respective ownership of the Building. In addition, Tenant shall look solely to Landlord's interest in the Building for recovery of any judgment against Landlord arising in connection with this Lease, it being agreed that neither Landlord nor any successor or assign of Landlord nor any future owner of the Building, nor any trustee, director, officer, employee, beneficiary, partner, shareholder, or agent of any

of the foregoing shall ever be personally liable for any such judgment.

SECTION 30. SUBORDINATION AND ATTORNMENT

At Landlord's option, this Lease shall be subordinate to any mortgage, deed of trust (now or subsequently placed upon the Building), ground lease, declaration of covenants (subsequently placed upon the Building) regarding maintenance and use of any areas contained in any portion of the Building,

and to any and all advances made under any mortgage or deed of trust and to all renewals, modifications, consolidations, replacements and extensions of the same. With respect to any of the above documents, Tenant agrees that no documentation other than this Lease shall be required to evidence the subordination. Any holder of a mortgage or deed of trust may elect, by written notice to Tenant, to make this Lease superior to the lien of its mortgage or deed of trust, in which case this Lease shall automatically be deemed prior to such mortgage or deed of trust, whether this Lease is dated earlier or later than the date of the mortgage or deed of trust or the date the same was recorded. Tenant shall execute such documents as may be required to evidence the subordination or to make this Lease prior to the lien of any mortgage or deed of trust, as the case may be. By failing to do so within five days after written demand, Tenant does hereby make, constitute and irrevocably appoint Landlord as Tenant's attorney-in-fact to do so. This power of attorney is coupled with an interest. Tenant hereby attorns to all successor owners of the Building, whether or not such ownership is acquired as a result of a sale through foreclosure of a deed of trust or mortgage, or other. Notwithstanding the above, Tenant shall be obligated to subordinate its leasehold interest to any mortgage, deed of trust, ground lease or declaration of covenants now or subsequently placed upon the Building only if the holder of such mortgage or deed of trust or the landlord under such ground lease or the declarant under such declaration of covenants will grant to Tenant a nondisturbance agreement, using the form of document then being employed by such holder, landlord or declarant for such purposes, which will provide that Tenant, notwithstanding any default of Landlord, shall have the right to remain in possession of the Leased Premises in accordance with this Lease for so long as Tenant shall not be in default under this Lease. Additionally, at such time or times as Landlord may request, upon not less than five days' prior written request by Landlord, Tenant shall sign and deliver to Landlord a certificate stating whether this Lease is in full force and effect; whether any amendments or modifications exist; whether there are any Events of Default; and such other information and agreements as may be reasonably requested. Any such statement delivered pursuant to this Section may be relied upon by Landlord and by any prospective purchaser of all or any portion of Landlord's interest, or a holder or prospective holder of any mortgage or deed of trust encumbering the Building. Tenant's failure to deliver such statement within such time shall constitute an Event of Default and shall conclusively be

deemed to be an admission by Tenant of the matters set forth in the request for an estoppel certificate.

SECTION 31. HOLDING OVER

In the event Tenant, or any party claiming under Tenant, retains possession of the Leased Premises after the Termination Date, the possession shall be an unlawful detainer. No tenancy or interest shall result from such possession, and such parties shall be subject to immediate eviction and removal. Tenant or any such party shall pay Landlord, as Rent for the period of such holdover, an amount equal to one hundred fifty percent (150%) of the Rent otherwise provided for in this Lease during the time of holdover. Tenant also shall be liable for any and all damages sustained by Landlord as a result of such holdover. Tenant shall vacate the Leased Premises and deliver the Leases Premises to Landlord immediately upon Tenant's receipt of notice from Landlord to so vacate. The Rent during such holdover period shall be payable to Landlord on demand. No holding over by Tenant, whether with or without Landlord's consent, shall operate to extend this Lease.

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SECTION 32. SIGNS

No sign, symbol or identifying marks shall be put upon the Building or the Real Property, or in the halls, elevators, staircases, entrances, parking areas or upon the doors or walls, without Landlord's prior written approval, which may be given or withheld in Landlord's sole discretion Should such approval be granted, the signs or lettering shall conform in all respects to the sign and/or lettering criteria established by Landlord. Landlord, at Landlord's sole cost and expense, reserves the right to change the door plaques as Landlord deems reasonably desirable.

SECTION 33. HAZARDOUS SUBSTANCES

With respect to Tenant's use of the Building, Tenant at all times, at its own cost and expense, shall comply with all Laws relating to the use, analysis, production, storage, sale, disposal or transportation of any hazardous materials ("HAZARDOUS SUBSTANCE LAWS"), including, without limitation, oil or petroleum products or their derivatives, solvents, PCB's, explosive substances, asbestos, radioactive materials or waste, and any other toxic, ignitable, reactive, corrosive, contaminating or pollution materials ("HAZARDOUS SUBSTANCES") which now or in the future are subject to any governmental regulation.

Tenant shall not use, generate, store or dispose of any Hazardous Substances in or on the Leased Premises or the Building (except to the extent and in the quantities any such Hazardous Substances are commonly used for general office purposes and then only in strict accordance with all Hazardous Substance Laws. Except in emergencies or as otherwise required by Law, Tenant

shall not take any remedial action in response to the presence or release of any Hazardous Substances on or about the Building without first giving written notice of the same to Landlord. Tenant shall not enter into any settlement agreement, consent decree or other compromise with respect to any claims relating to any Hazardous Substances in any way connected with the Building without first notifying Landlord of Tenant's intention to do so and affording Landlord the opportunity to participate in any such proceedings.

Landlord shall have the right at all reasonable times to (i) inspect the Leased Premises, (ii) conduct tests and investigations to determine whether Tenant is in compliance with the above provisions, and (iii) request lists of all Hazardous Substances used, stored or located on the Leased Premises by Tenant. All costs and expenses incurred by Landlord in connection with any environmental investigation shall be paid by Landlord (and may be included in Operating Expenses), except that if any such environmental investigation shows that Tenant has failed to comply with the provisions of this Section, or that the Building or the Real Property (including surrounding soil and any underlying or adjacent groundwater) have become contaminated due to the operations or activities in any way attributable to Tenant, then all of the costs and expenses of such investigation shall be paid by Tenant. Tenant's indemnity under-Section 21 shall specifically extend to all liability, including all foreseeable and unforeseeable consequential damages, directly or indirectly arising out of the use, generation, disposal or storage of Hazardous Substances by Tenant, including without limitation the costs of any required repair, cleanup or detoxification and the preparation of any closure or other required plans, whether such action is required or necessary prior to or following the termination of this Lease, to the full extent that such action is proximately caused by the use, generation, storage, or disposal of Hazardous Substances by Tenant. Neither the written consent by Landlord to the use, generation,

disposal or storage of Hazardous Substances by Tenant nor the strict compliance by Tenant with all Hazardous Substances Laws shall excuse Tenant from its indemnity obligation.

In the event Tenant's occupancy or conduct of business in or on the Leased Premises, whether or not Landlord has consented to the same, results in any increase in premiums for the insurance carried from time to time by Landlord with respect to the Building, Tenant shall pay any such increase in premiums as Rent within ten days after bills for the additional premiums shall be rendered by Landlord. In determining whether increased premiums are a result of Tenant's use or occupancy of the Leased Premises, a schedule issued by the organization computing the insurance rate on the Building showing the various components of such rate, shall be conclusive evidence of the several items and charges which make up such rate. Tenant shall promptly comply with all reasonable requirements of the insurance authority or of any insurer now or subsequently in effect relating to the Leased Premises.

Landlord hereby discloses to Tenant that a Phase I Environmental Site Assessment and Limited Asbestos Survey and Hazard Assessment were performed on the Property by Hygienetics, Inc. of Emeryville, California in 1990. Hygienetics, Inc. supplemented the Limited Asbestos Survey in June, 1991 and March, 1995. Such surveys and assessment revealed 13 samples of vinyl tile floor mastic, and two samples of vinyl floor files, in the Building, which contained asbestos and revealed the presence of limited quantities of hazardous and toxic substances such as cleaning materials, lead and acid batteries in the basement and diesel fuel storage tanks. Complete copies of the Site Assessment and Asbestos Surveys are available for inspection in the Building management office. Except as disclosed in the Site Assessment and Asbestos Surveys, Landlord has no actual knowledge of Hazardous Substances in the Building that must be removed in order for the Building to comply with Environmental Laws in effect as of the date of this Lease. Tenant has had the opportunity, prior to execution and delivery of this Lease, to make such further investigation and inquiry about such matters as Tenant deems appropriate and Tenant accepts the Premises with knowledge of the risks that may be associated with the presence of all materials or conditions disclosed in such surveys and assessment.

SECTION 34. COMPLIANCE WITH LAWS AND OTHER REGULATIONS

At its sole cost and expense, Tenant shall promptly comply with all laws, statutes, ordinances, decrees, orders, and governmental roles, regulations or requirements now in force or which may hereafter become in force, of federal, state, county, and municipal authorities, including but not limited to the Americans with Disabilities Act (the "ADA"), with the requirements of any board of fire underwriters or other similar body now or hereafter constituted, and with any occupancy certificate issued pursuant to any law by any public officer or officers, which impose any duty upon Landlord or Tenant, insofar as any thereof relate to or affect the condition, use, alteration or occupancy of the Leased Premises (collectively "LAWS"). Landlord's approval of Tenant's plans for any improvements shall create no responsibility or liability on the part of Landlord for their completeness, design sufficiency, or compliance with Laws.

SECTION 35. GOVERNING LAW; SEVERABILITY

This Lease shall be construed in accordance with the laws of the State of California. If any provision of this Lease or the application of it to any person or circumstance shall be invalid or unenforceable to any extent, it shall be adjusted, if possible, rather than voided, in order to achieve the

intent of the parties. In any event, the remainder of this Lease and the application of such provision to the other persons or circumstances shall not be affected thereby and shall be enforced to the greatest extent permitted by law. This Lease shall Ix: construed as though the covenants between Landlord and

Tenant are independent Tenant hereby expressly waives the benefit of any statute to the contrary and agrees that if Landlord fails to perform its obligations set forth heroin, Tenant shall not be entitled to make any repairs or perform any acts hereunder at Landlord's expense or to any set-off of the rent or other amounts owing hereunder against Landlord.

SECTION 36. NOTICES

All notices, demands, statements or communications (collectively, "NOTICES") given or required to be given by either party to the other hereunder shall be in writing, shall be sent by nationally recognized overnight courier service, or United States certified or registered mail, postage prepaid, return receipt requested, or delivered personally addressed as follows:

TO THE LANDLORD: John Hancock Mutual Life Insurance Company
c/o The Galbreath Company
353 Sacramento Street
San Francisco, CA 94111
Attn: Melody Hanhaa

with a copy to: John Hancock Mutual Life Insurance Company
Attn Investment Officer Real Estate Investment Group
200 Clarendon St. Floor T-53
Boston, MA 02117

TO THE TENANT: Digital Island
353 Sacramento Street, Suite 1520
San Francisco, CA 94104
Attn: Ken Higgins

Any Notice will be deemed given upon the date actually received. If Tenant is notified of the identity and address of the holder of any mortgage or deed of trust given by Landlord, or any ground or underlying lessor, Tenant shall give to such holder or ground or underlying lessor written notice of any default by Landlord under the terms of this Lease by registered or certified mail, and such holder or ground or underlying lessor shall be given a reasonable opportunity to cure such default prior to Tenant's exercising any termination remedy available to Tenant. Such addresses may be changed from time to time by either party serving notice as provided above.

SECTION 37. OBLIGATIONS OF SUCCESSORS, PLURALITY, GENDER

Landlord and Tenant agree that all the provisions hereof are to be construed as covenants and agreements as though the words imparting such covenants were used in each paragraph hereof, and that, except as restricted by the provisions hereof, shall bind and inure to the benefit of the parties hereto, their respective heirs, legal representatives, successors and assigns. If the rights of Tenant hereunder are owned by two or more parties or two or more parties are designated herein as Tenant, then all such

parties shall be jointly and severally liable for the obligations of Tenant hereunder. Whenever the singular or plural number, masculine or feminine or neuter gender is used herein, it shall equally include the other.

SECTION 38. ENTIRE AGREEMENT

This Lease and any attached addenda or exhibits constitute the entire agreement between Landlord and Tenant. No prior or contemporaneous written or oral or representations shall be binding. This Lease shall not be amended, changed or extended except by written instrument signed by Landlord and Tenant.

SECTION 39. SECTION CAPTIONS

Section captions are for Landlord's and Tenant's convenience only, and neither limit nor amplify the provisions of this Lease.

SECTION 40. CHANGES

Tenant shall consent to a modification of this Lease requested by any mortgagee or beneficiary under a deed of trust as long as the modification does not increase Tenant's costs or substantially change Tenant's rights and obligations.

SECTION 41. AUTHORITY

All rights and remedies of Landlord under this Lease, or those which may be provided by law, may be exercised by Landlord in its own name individually, or in its name by its agent, and all legal proceedings for the enforcement of any such rights or remedies, including actions for Rent, unlawful detains, and any other legal or equitable proceedings, may be commenced and prosecuted to final judgment and be executed by Landlord in its own name individually or in its name by its agent. Landlord and Tenant each represent to the other that each has full power and authority to execute this Lease and to make and perform the agreements herein contained. Tenant expressly stipulates that any rights or remedies available to Landlord, either by the provisions of this Lease or otherwise, may be enforced by Landlord in its own name individually or in its name by its agent or principal.

SECTION 42. BROKERAGE

Landlord and Tenant hereby warrant to each other that they have had no dealings with any real estate broker or agent in connection with the negotiation of this Lease, excepting only the real estate brokers or agents specified in the Basic Lease Information, and that they know of no other real estate broker or agent who is entitled to a commission in connection with this Lease. Each party

shall defend, indemnify and hold the other party harmless from and against all claims, actions, loss, cost, damage, expense and liability (including without limitation reasonable attorneys' fees and court costs) with respect to any leasing commission or equivalent compensation alleged to be owing on account of the indemnifying party's dealings with any real estate broker or agent other than that specified herein. Additionally, Tenant acknowledges and agrees that Landlord shall have no obligation for payment of any brokerage fee or similar compensation to any person with whom Tenant has dealt or may in the

future deal with respect to leasing of any additional or expansion space in the Building or renewals or extensions of this Lease.

SECTION 43. ADDITIONS TO LEASE

Exhibits "A" through "C" are attached hereto and incorporated in this Lease for all purposes and are hereby acknowledged by both panics to this Lease.

IN WITNESS WHEREOF, Landlord and Tenant, acting herein through duly authorized individuals, have caused this Lease to be executed in multiple counterparts, each of which shall have the force and effect of an original as of the date first above written

TENANT: DIGITAL ISLAND,
a California corporation

By: /s/ [SIGNATURE ILLEGIBLE]^^

Name: /s/ [SIGNATURE ILLEGIBLE]^^

Title:

TAX ID OR TAX EXEMPT NO._____

LANDLORD: JOHN HANCOCK MUTUAL LIFE INSURANCE COMPANY,
a Massachusetts, corporation

By: /s/ Meliha E. Amour

Meliha E. Amour
Its: Investment Officer

LEASE EXHIBIT A (MAP)

[FLOOR PLAN APPEARS HERE]

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EXHIBIT B

Rules and Regulations
353 Sacramento Street Building
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1. Tenant shall not alter any lock or install any new or additional locks or bolts on any doors or windows of the Leased Premises without obtaining Landlord's written consent. Tenant shall bear the cost of any lock changes or repairs required by Tenant. Two keys will be furnished by Landlord for the Leased Premises, and any additional keys required by Tenant must be obtained from Landlord at a reasonable cost to be established by Landlord. Upon termination of the Lease, all keys to the Building and the Leased Premises shall be surrendered to Landlord.

2. All doors opening to public corridors shall be kept closed at all times except for normal ingress to and egress from the Leased Premises.

3. Landlord reserves the right to close and keep locked all entrance and exit doors of the Building during such hours as are customary for comparable buildings in the City of San Francisco. Tenant and its employees and agents shall ascertain that the Building doors are securely closed and locked when leaving the Premises after normal business hours. When entering or leaving the Building after normal business hours Tenant and its employees and agents may be required to sign the Building Register. Access to the Building may be refused unless the person seeking access has proper identification or a previously arranged pass. Landlord and its agents shall in no event be liable for damages for any error with regard to the admission to or exclusion from the Building of any person. In the event of invasion, mob riot, public excitement, or other commotion, Landlord reserves the right to prevent access to the Building by any means Landlord deems appropriate for the protection of life and property.

4. No furniture, freight or equipment of any kind shall be brought into the Building without prior written notice to Landlord. All moving of the same into or out of the Building shall be scheduled with Landlord and done only at such time and in such manner as Landlord shall designate. Landlord shall have the right to prescribe the weight, size and position of all safes and other heavy property brought into the Building. Landlord may require safes and other heavy objects to stand on supports to properly distribute the weight. All damage done to any pan of the Building, its contents, occupants or visitors by the moving or maintenance of such safes or other property shall be the sole responsibility of Tenant.

5. No furniture, packages, supplies, equipment or merchandise shall be received in the Building or carried up or down in the elevators, except between such hours and in such elevator as shall be designated by Landlord.
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6. Landlord shall have the right to control and operate the public portions of the Building, the public facilities, the heating and air conditioning, and any other facilities furnished for the common use of tenants, in such manner as is customary for comparable buildings in the City of San Francisco.

7. Landlord shall furnish heating and air conditioning from 8:00 a.m. to 6:00 p.m., Monday through Friday. In the event Tenant requires heating and air conditioning during off hours, Saturdays, Sundays, or holidays, Landlord, on 24 hours' prior written notice from Tenant, shall provide such services at an hourly rate to be established by Landlord from time to time.

8. Tenant shall apply to the Building office for any work or maintenance to be provided by Landlord. Employees of Landlord shall not perform any work other than their regular duties except when so directed by Landlord.

9. Tenant shall not disturb, solicit, or canvass any occupant of the Building and shall cooperate with Landlord or Landlord's agent to prevent same.

10. The toilet rooms, urinals, wash bowls and other apparatus shall not be used for any purpose other than that for which they were constructed, and no foreign substance of any kind whatsoever shall be thrown therein. The expense of any breakage, stoppage or damage resulting from the violation of this rule by Tenant or its employees, agents and invitees shall be borne by Tenant

11. Tenant shall not overload the floor of the Leased Premises, nor mark, drive nails or screws, or drill into the partitions, woodwork or plaster or in any way deface the Leased Premises or any part thereof without Landlord's prior written consent.

12. No vending machine or machines of any description other than fractional horsepower office machines shall be installed, maintained or operated upon the Leased Premises without Landlord's prior written consent; provided that, Tenant may install art work, white boards and similar items, so long as Tenant patches any significant holes resulting from such installation.

13. Tenant shall not use or keep in or on the Leased Premises of the Building any kerosene, gasoline or other inflammable or combustible fluid or material. Tenant shall not use, keep or permit to be used or kept foul or noxious substances in or on the Leased Premises, or permit or allow the Leased Premises to be occupied or used in a manner offensive or objectionable to Landlord or other occupants of the Building by reason of noise, odors, or vibrations, or interfere in any way with other tenants or persons having business in the Building.

14. Tenant shall not use any heating or air conditioning equipment other than that supplied by Landlord without Landlord's prior written consent.

15. Tenant shall not bring into or keep within the Building or the Leased Premises any animals, birds, bicycles or other vehicles.

16. No cooking shall be done or permitted by any Tenant on the Leased Premises, nor shall the Leased Premises be used for the storage of merchandise (other than business samples), for lodging, or for any improper purposes. Notwithstanding the foregoing, Underwriters' Laboratory-approved equipment may be used in the Lease Premises for brewing coffee, tea, hot chocolate and similar beverages, and microwave heating of already prepared foodstuffs, provided that such use is in accordance with all applicable Federal, state and city laws, codes, ordinances, rules and regulations.

17. Introduction of telephone wires to the Leased Premises and the location of telephone, call boxes and other office equipment affixed to the Leased Premises shall be subject to Landlord's prior written approval, which shall not be unreasonably withheld or delayed.

18. Landlord reserves the right to exclude or expel from the Building any person who, in Landlord's sole judgment, appears under the influence of liquor or drugs, or who violates these rules and regulations.

19. Landlord shall have the right, exercisable without notice and without liability to Tenant, to change the name and street address of the Building.

20. Tenant shall not employ or admit any person or persons other than Landlord's janitor for the purpose of cleaning or maintaining the Leased Premises unless agreed to in writing by Landlord. Any damage to the Leased Premises caused by Tenant or its employees or agents while engaged in the cleaning or maintaining of the Leased Premises shall be Tenant's sole responsibility. Janitorial service shall include ordinary dusting and cleaning and shall not include cleaning of carpets or rugs, except normal vacuuming, nor moving of furniture or other special services. Landlord shall in no way be responsible to Tenant for any loss of or damage to property on the Leased Premises caused by the janitorial service, but Landlord shall use commercially reasonable efforts to pursue rights and remedies available against such janitorial service.

21. Tenant and its employees and agents shall not loiter in the entrances or corridors, nor in any way obstruct the sidewalks, lobby, halls, stairways or elevators, and shall use the same only for ingress to and egress flora the Leased Premises.

22. Tenant shall not waste electricity, water or air conditioning. Tenant shall cooperate fully with Landlord to ensure the most effective operation of the Building's heating and air conditioning, and shall not adjust any controls.

23. Tenant shall store all trash and garbage within the interior of the Leased Premises. No material shall be placed in trash boxes or receptacles if disposal in the ordinary and customary manner in the City of San Francisco would violate any applicable law or

ordinance. All trash, garbage and refuse disposal shall occur only through entryways and elevators provided for such purposes at times designated by Landlord.

24. Tenant shall comply with all safety, fire protection and evacuation procedures and regulations established by Landlord or any governmental agency.

25. Tenant shall assume all responsibility for protecting the Leased Premises from theft, robbery and pilferage, including without limitation preventing entry to the Leased Premises by unauthorized persons.

26. Landlord may waive any one or more of these Rules and Regulations for the benefit of any particular tenant or tenants, but no such waiver by Landlord shall be construed as a waiver of such Rules and Regulations in favor of any other tenant or tenants, nor prevent Landlord from thereafter enforcing any such Rules and Regulations against any or all tenants of the Building.

27. Landlord reserves the right to make other reasonable rules and regulations as in its judgment may from time to time be needed for security or for the preservation of good order, and Tenant shall abide by all such rules and regulations.

*****

EXHIBIT C

TENANT IMPROVEMENT WORK

This Exhibit C is incorporated in and is part of that certain Lease dated as of April 8, 1997 (the "LEASE"). Terms defined in the Lease shall have the

same meaning when used herein.

1. PREPARATION OF DRAWINGS

   A. DRAWINGS. The space plan prepared by Huntsman Associates has been approved by Landlord and Tenant and is incorporated herein and attached to the Lease as Exhibit A. Further detailed working drawings and specifications (the "WORKING DRAWINGS") as required for construction of the tenant improvement work (the "TENANT IMPROVEMENT WORK") in the Leased Premises shall be prepared by Landlord as soon as practicable.

   B. APPROVAL OF THE WORKING DRAWINGS. Within five (5) business days after Landlord's submission to Tenant of the Working Drawings, Tenant shall give Landlord written notice of its approval or disapproval of same. Tenant's approval shall not be unreasonably withheld or delayed provided that the Working Drawings are consistent with building standards. If the Working Drawings ate not approved by Tenant, Tenant shall in its notice of disapproval state specifically all corrections or changes requested, all of which must be consistent with building standards.

   C. CONSTRUCTION. Upon Tenant's approval of the Working Drawings, Landlord shall proceed diligently to perform the Tenant Improvement Work as soon as practicable in accordance with the Working Drawings, current building standards for labor and materials, and all applicable codes and regulations.

2. COMPUTER AND TELEPHONE EQUIPMENT. Landlord, at Tenant's request, will allow Tenant, its employees or other installation personnel, access to the Leased Premises for the purposes of installing telephone and computer lines, cables and equipment. Tenant agrees to coordinate its installation of telephones and computer equipment so as not to delay or increase the costs of Landlord's performance of the Tenant Improvement Work.

3. PAYMENT OF THE COSTS OF THE TENANT IMPROVEMENT WORK. Landlord shall pay the costs for design and construction of the Tenant Improvement Work in an amount not to exceed $85,848. Any costs in excess of $85,848 shall be paid by Tenant within ten (10) days after receipt of Landlord's invoice therefor. If the costs of the Tenant Improvement Work are reasonably estimated by Landlord to exceed $85,848, then Tenant shall deposit with Landlord the amount of such excess as reasonably estimated by Landlord prior to commencement of the Tenant Improvement Work Any amount deposited by Tenant in excess of the amount by which the actual costs of the Tenant Improvement Work exceed $85,848 shall be credited by Landlord to the next payment of Rent due under the Lease.

4. DELIVERY OF PREMISE AND COMMENCEMENT OF LEASE TERM. When the Tenant Improvement Work to be done by Landlord pursuant to this Exhibit C has been

substantially completed (i.e.,
<PAGE>

subject to normal "punch-list" items) for each of the Phase 1 and Phase 2 portions of' the Leased Premises, Landlord shall provide written notice of such event to Tenant and that portion of the Leased Premises shall be immediately inspected by Tenant's representative and accepted in writing as to whether the Tenant Improvement Work has been performed according to the Working Drawings and building standards; provided, however, that there shall be no withholding of acceptance if the Tenant Improvement Work to be done is substantially completed such that there would be no interference with Tenant's use or occupancy of the Leased Premises caused by any such incomplete work.

If the Tenant Improvement Work has been substantially but not entirely complete, Tenant's representative shall accept the Phase I or Phase 2 portion of the Leased Premises, as applicable, and give Landlord a written punchlist of such items necessary to complete, which items Landlord agrees in writing should be included on such punchlist are herein called the "PUNCHLIST ITEMS". Landlord shall promptly complete the Punchlist Items. Tenant shall be conclusively deemed to have agreed that Landlord has performed all its obligations with respect to the Tenant Improvement Work except only as to the Punchlist Items.

Upon Tenant's acceptance of the Tenant Improvement Work for each of the Phase I and Phase 2 portions of the Leased Premises, as applicable, that portion of the Leased Premises shall be deemed "Ready for Occupancy" and possession thereof deemed delivered to Tenant for all purposes of the Lease.

5. PERFORMANCE OF THE TENANT IMPROVEMENT WORK. Landlord warrants that all Tenant Improvement Work shall be completed in compliance with the Working Drawings and building standard materials and techniques. Except for the warranty continued in the previous sentence, no other warranties or representations are made by Landlord concerning the tenant improvements.

6. EXTRAS. All extras or changes made to the Tenant Improvement Work after the Working Drawings have been accepted shall be made only by a writing signed by both parties.

7. REMEDIES UPON BREACH. In the event of any breach by Tenant of the provisions of this Exhibit C, Landlord, upon thirty (:30) days' written notice to Tenant as provided in the Lease (which notice shall be in lieu of any notice required by the laws of the State of California, unless California law provides for a longer period), may elect to treat Such breach as a default under the Lease which shall entitle Landlord to any of the rights and remedies provided thereunder.

8. TENANT'S REPRESENTATIVE. Tenant has designated MARK NICHOLS as its sole

representative with respect the matters set forth in this Exhibit C, who shall full authority and responsibility to act on behalf to Tenant as required in this Exhibit C. If MARK NICHOLS shall not be available for inspection of the Leased Premises as provided in Paragraph 4 above, Tenant shall provide an authorized representative within one day after said notice to inspect and who shall have Tenant's authority to accept the Leased Premises at that time.

9. LANDLORD'S REPRESENTATIVE. Landlord has designated Melody Hanhan as its representative with respect to the matters set forth in the Exhibit C, who shall have the full authority and responsibility to act on behalf of the Landlord as required in this Exhibit C.

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[DEMOLITION PLAN APPEARS HERE]

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[CONSTRUCTION/FINISH PLAN APPEARS HERE]

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[POWER & SIGNAL PLAN APPEARS HERE]

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[REFLECTED CEILING PLAN APPEARS HERE]

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DEMOLITION LEGEND

DEMOLITION NOTES

SHEET NOTES

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CONSTRUCTION LEGEND

SHEET NOTES

DOOR SCHEDULE

HARDWARE GROUPS

DOOR AND HARDWARE NOTES

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FINISH LEGEND

FINISH KEYNOTES

REFLECTED CEILING LEGEND

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POWER AND SIGNAL LEGEND

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EXHIBIT 21.1

SUBSIDIARIES OF THE REGISTRANT

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2. Digital Island, B.V.i.o., incorporated in the Netherlands.
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Exhibit 23.1

CONSENT OF INDEPENDENT ACCOUNTANTS

We hereby consent to the use in the Prospectus constituting part of this Registration Statement on Form S-1 of our report dated February 19, 1999, relating to the financial statements of Digital Island, Inc., which appears in such Prospectus. We also consent to the reference to us under the heading "Experts" in such Prospectus.

/s/ PricewaterhouseCoopers LLP

San Francisco, California
April 23, 1999
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