

RITA MEDICAL SYSTEMS INC  
Form DEF 14A  
April 28, 2006

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**SCHEDULE 14A**  
(Rule 14a-101)

**INFORMATION REQUIRED IN PROXY STATEMENT**

**SCHEDULE 14A INFORMATION**

Proxy Statement Pursuant to Section 14(a) of the Securities  
Exchange Act of 1934

Filed by the Registrant

Filed by a party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, For Use of the Commission Only (as permitted by Rule 14a-6(e)(2))
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material Under Rule 14a-12

**RITA MEDICAL SYSTEMS, INC.**

\_\_\_\_\_  
(Name of Registrant as Specified in Its Charter)

\_\_\_\_\_  
(Name of Person(s) Filing Proxy Statement, if Other Than the Registrant)

Payment of Filing Fee (Check the appropriate box):

- No fee required.
- Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

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(2) Aggregate number of securities to which transactions applies:

\_\_\_\_\_

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11  
(set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

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(5) Total fee paid:

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o Fee paid previously with preliminary materials:

o Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the form or schedule and the date of its filing.

(1) Amount previously paid:

\_\_\_\_\_

(2) Form, Schedule or Registration Statement No.:

\_\_\_\_\_

(3) Filing Party:

\_\_\_\_\_

(4) Date Filed:

\_\_\_\_\_

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**RITA MEDICAL SYSTEMS, INC.**  
**46421 Landing Parkway**  
**Fremont, California 95438**

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**NOTICE OF ANNUAL MEETING OF STOCKHOLDERS**

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**TO BE HELD JUNE 7, 2006**

On Wednesday, June 7, 2006, RITA Medical Systems, Inc., a Delaware corporation (the "Company"), will hold its 2006 Annual Meeting of Stockholders (the "Meeting") at its corporate headquarters, located at 46421 Landing Parkway, Fremont, California 95438. The Meeting will begin at 9:00 a.m. local time.

Only stockholders who owned shares of our common stock at the close of business on April 10, 2006 can vote at the Meeting or any adjournment that may take place. At the Meeting you will be asked to:

Elect two Class III directors to serve until the annual meeting of the Company's stockholders for the year ending December 31, 2009;

Amend the 2005 Stock and Incentive Plan to increase the number of shares of common stock issuable under the plan by an additional 500,000 shares, to an aggregate of 5,876,746 shares;

Ratify the appointment of Stonefield Josephson, Inc. as our independent registered public accounting firm for the current fiscal year; and

Transact any other business properly brought before the Meeting.

You can find more information about each of these items, including the nominees for directors, in the attached Proxy Statement.

Our Board of Directors recommends that you vote in favor of each of the three proposals outlined in the Proxy Statement.

We cordially invite all stockholders to attend the Meeting in person. However, whether or not you expect to attend the Meeting in person, please mark, date, sign and return the enclosed proxy card as promptly as possible in the postage-prepaid envelope provided to ensure your representation and the presence of a quorum at the Meeting. If you send in your proxy card and then decide to attend the Meeting to vote your shares in person, you may still do so. Your proxy is revocable in accordance with the procedures set forth in the Proxy Statement.

At the Meeting, we will also report on our business results and other matters of interest to stockholders.

By Order of the Board of Directors,

/s/ Joseph DeVivo

Joseph DeVivo, President and Chief Executive Officer

Fremont, California  
April 28, 2006

*This Notice of Annual Meeting of Stockholders together with the attached Proxy Statement and Annual Report for the fiscal year ended December 31, 2005 will be mailed to stockholders on or about May 3, 2006.*

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**RITA MEDICAL SYSTEMS, INC.**

46421 Landing Parkway  
Fremont, California 94538

**PROXY STATEMENT  
FOR THE  
2006 ANNUAL MEETING OF STOCKHOLDERS**

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**June 7, 2006**

Our Board of Directors is soliciting proxies for the 2006 Annual Meeting of Stockholders. This Proxy Statement contains important information for you to consider when deciding how to vote on the matters brought before the Annual Meeting. Please read it carefully.

The Board set April 10, 2006 as the record date for the Annual Meeting. Stockholders of record who owned our common stock on that date are entitled to vote at and attend the Annual Meeting, with each share entitled to one vote. 43,086,256 shares of common stock were outstanding on the record date.

Voting materials, which include this Proxy Statement, a proxy card and the 2005 Annual Report, will be mailed to stockholders on or about May 3, 2006.

In this Proxy Statement:

We , us , our and the Company refer to RITA Medical Systems, Inc.

Annual Meeting or Meeting means our 2006 Annual Meeting of Stockholders.

Board of Directors or Board means our Board of Directors.

SEC means the Securities and Exchange Commission.

We have summarized below important information with respect to the Annual Meeting.

**Time and Place of the Annual Meeting**

The Annual Meeting is being held on Wednesday, June 7, 2006 at 9:00 a.m. local time at our corporate headquarters 46421 Landing Parkway, Fremont, California 94538.

All stockholders who owned shares of our common stock as of April 10, 2006, the record date, may attend the Annual Meeting.

**Purpose of the Proxy Statement and Proxy Card**

You are receiving a Proxy Statement and proxy card from us because you owned shares of our common stock on April 10, 2006, the record date. This Proxy Statement describes proposals on which we would like you, as a stockholder, to vote. It also gives you information on these proposals so that you can make an informed decision.

When you sign the proxy card, you appoint Joseph DeVivo and Michael Angel as your representatives at the Annual Meeting. Joseph DeVivo and Michael Angel will vote your shares at the Annual Meeting as you have instructed them on the proxy card. This way, your shares will be voted whether or not you attend the Annual Meeting. Even if you plan to attend the Annual Meeting it is a good idea to complete, sign and return your proxy card in advance of the Annual Meeting just in case your plans change. If you attend the Annual Meeting and decide to vote your shares in person, you may still do so. Your proxy is revocable in accordance with the procedures described below.

**Proposals to be Voted on at This Year's Annual Meeting**

You are being asked to vote on:

The election of two directors to serve on our Board of Directors.

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The amendment to the 2005 Stock and Incentive Plan to increase the number of shares of common stock issuable under the plan by an additional 500,000 shares, to an aggregate of 5,876,746 shares.

The ratification of our appointment of Stonefield Josephson, Inc. as our independent registered public accounting firm for the current fiscal year.

Our Board recommends a vote FOR each proposal.

### **Voting Procedure**

*You may vote by mail.*

To vote by mail, please sign your proxy card and return it in the enclosed, prepaid and addressed envelope. If you mark your voting instructions on the proxy card, your shares will be voted as you instruct. If you do not mark any voting instructions on the proxy card, your shares will be voted FOR the director nominees identified in this Proxy Statement, FOR the amendment to the 2005 Stock and Incentive Plan, FOR the ratification of our independent registered public accounting firm identified in this Proxy Statement and as the proxy holders deem desirable for any other matters that may come before the Annual Meeting.

*You may vote in person at the Annual Meeting.*

We will pass out written ballots to anyone who wants to vote at the Annual Meeting. If you hold your shares in street name, you must request a legal proxy from your stockbroker in order to vote at the Annual Meeting. Holding shares in street name means your shares of common stock are held in an account by your stockbroker, bank, or other nominee, and the stock certificates and record ownership are not in your name. If your shares are held in street name and you wish to attend the Annual Meeting, you must notify your broker, bank or other nominee and obtain the proper documentation to vote your shares at the Annual Meeting.

*You may change your mind after you have returned your proxy card.*

If you change your mind after you return your proxy card, you may revoke your proxy at any time before the polls close at the Annual Meeting. You may do this by:

signing another proxy card with a later date, or

voting in person at the Annual Meeting.

### **Multiple Proxy Cards**

If you received more than one proxy card, it means that you hold shares in more than one account. Please sign and return all proxy cards to ensure that all your shares are voted.

### **Quorum Requirement**

Shares are counted as present at the Annual Meeting if the stockholder either:

is present and votes in person at the Annual Meeting, or

has properly submitted a proxy.

A majority of our outstanding shares as of the record date must be present at the Annual Meeting (either in person or by proxy) in order to hold the Annual Meeting and conduct business. This is called a quorum.

### **Consequences of Not Returning Your Proxy; Broker Non-Votes**

If your shares are held in your name, you must return your proxy card (or attend the Annual Meeting in person) in order to vote on the proposals. If your shares are held in street name and you do not vote your proxy card, your brokerage firm may either:

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vote your shares on routine matters, or

leave your shares unvoted.

Under the rules that govern brokers who have record ownership of shares that are held in street name for their clients, brokers may vote such shares on behalf of their clients with respect to routine matters (such as the

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election of directors or the ratification of auditors), but not with respect to non-routine matters (such as proposals authorizing the issuance of stock or options to directors, officers or employees or a proposal submitted by a stockholder). If the proposals to be acted upon at any meeting include both routine and non-routine matters, the broker may turn in a proxy card for uninstructed shares that votes FOR the routine matters, but expressly states that the broker is not voting on non-routine matters. This is called a broker non-vote .

At the Annual Meeting, broker non-votes will be counted for the purpose of determining the presence or absence of a quorum, but will not be counted for the purpose of determining the number of votes cast.

We encourage you to provide instructions to your brokerage firm by voting your proxy card. This ensures that your shares will be voted at the Annual Meeting.

### **Effect Of Abstentions**

Abstentions are counted as shares that are present and entitled to vote for the purposes of determining the presence of a quorum and as votes AGAINST for purposes of determining the approval of any matter submitted to the stockholders for a vote.

### **Required Vote**

Assuming a quorum is present, the two nominees receiving the highest number of yes votes will be elected as directors. The amendment to the 2005 Stock and Incentive Plan and the ratification of our independent registered public accounting firm will require the affirmative vote of a majority of shares of our common stock present in person or represented by proxy and entitled to be voted on the proposal at the Annual Meeting.

### **Vote Solicitation; Use Of Outside Solicitors**

RITA Medical Systems, Inc. is soliciting your proxy to vote your shares at the Annual Meeting. In addition to this solicitation by mail, our directors, officers, and other employees may contact you by telephone, Internet, in person or otherwise to obtain your proxy. These persons will not receive any additional compensation for assisting in the solicitation. We will also request brokerage firms, nominees, custodians and fiduciaries to forward proxy materials to the beneficial owners. We will reimburse these entities and our transfer agent for their reasonable out-of-pocket expenses in forwarding proxy materials. Furthermore, we have retained the services of Georgeson Shareholder Communications, Inc., a proxy solicitor, to assist in the solicitation of votes. In addition to reasonable out-of-pocket expenses, Georgeson Shareholder Communications will receive a customary fee, which we estimate will be approximately \$30,000.

### **Voting Procedures**

Votes cast by proxy or in person at the Annual Meeting will be tabulated by U.S. Stock Transfer, who will act as the Inspector of Election. The Inspector of Election will also determine whether a quorum is present at the Annual Meeting.

The shares represented by the proxy cards received, properly marked, dated, signed and not revoked, will be voted at the Annual Meeting. If a proxy card specifies a choice with respect to any matter to be acted on, the shares will be voted in accordance with that specified choice. Any proxy card which is returned but not marked will be voted FOR the director nominees identified below, FOR the amendment to the 2005 Stock and Incentive Plan, FOR the ratification of the independent registered public accounting firm as discussed in this Proxy Statement, and as the proxy holders deem desirable for any other matters that may come before the Annual Meeting. Broker non-votes will not be considered as voting with respect to any matter for which the broker does not have voting authority.

We believe that the procedures to be used by the Inspector of Election to count the votes are consistent with Delaware law concerning voting of shares and determination of a quorum.

### **Publication Of Voting Results**

We will announce preliminary voting results at the Annual Meeting. We will publish the final results in our quarterly report on Form 10-Q for the second quarter of 2006 which we will file with the SEC. You can get a copy by contacting our Investor Relations Department at (510) 771-0400 or on our website at [www.ritamedical.com](http://www.ritamedical.com), by

contacting the SEC at (800) 732-0330 for the location of the nearest public reference room, or through the EDGAR system at [www.sec.gov](http://www.sec.gov).

**2005 Annual Report**

We have mailed a copy of our Annual Report on Form 10-K for the fiscal year ended December 31, 2005 with this Proxy Statement.

**Other Business**

We do not know of any business to be considered at the Annual Meeting other than the proposals described in this Proxy Statement. However, if any other business is properly presented at the Annual Meeting, your signed proxy card gives authority to Joseph DeVivo and Michael Angel to vote on such matters at their discretion.

**Proposals For 2007 Annual Meeting**

To have your proposal included in our proxy statement for the 2007 Annual Meeting of Stockholders, you must submit your proposal before February 15, 2007 to RITA Medical Systems, Inc., 46421 Landing Parkway, Fremont, California 94538, Attn: Corporate Secretary.

**PROPOSAL NO. 1****ELECTION OF DIRECTORS**

Our Certificate of Incorporation divides our Board of Directors into three classes, with staggered three-year terms. The Class I directors, whose terms expire at the 2007 Annual Meeting of Stockholders, are Vincent Bucci, Scott Halsted and Steve LaPorte; the Class II directors, whose terms expire at the 2008 Annual Meeting of Stockholders, are James E. Brands, Thomas J. Dugan and Wesley E. Johnson, Jr.; and the Class III directors, whose terms expire at the Annual Meeting, are Joseph DeVivo and Randy Lindholm. You only elect one class of directors at each annual meeting. The other classes continue to serve for the remainder of their three-year terms. The Board has determined that a majority of the members of the Board, specifically Messrs. Brands, Bucci, Dugan, Halsted, Johnson and LaPorte, are independent directors under the rules of the NASDAQ Stock Market.

The Class III directors are the nominees for re-election at the Annual Meeting. Each nominee has consented to serve an additional three-year term.

**Vote Required**

If a quorum is present, the two nominees receiving the highest number of affirmative votes of shares entitled to be voted for him or her will be elected as directors for the ensuing three years. Unless marked otherwise, proxies received will be voted FOR the election of the nominees named below. If additional people are nominated for election as a director, the proxy holders intend to vote all proxies received by them in a way that will ensure that the nominees listed below are elected.

**Nominees for the Board of Directors**

The names of each nominee, his age as of April 15, 2006 and certain other information about him is set forth below:

<u>Name of Nominee</u>	<u>Age</u>	<u>Principal Occupation</u>	<u>Director Since</u>
Joseph DeVivo	38	President and Chief Executive Officer of the Company	August 2003
Randy Lindholm (1)	49	Consultant to Life Sciences Companies	April 2003

(1) Member of the Compensation Committee of the Board.

**Joseph DeVivo** has served as our President and Chief Executive Officer and as a member of our Board since August 2003. Prior to joining us, from August 2002 to June 2003, he was President, Director and Chief Operating Officer of ComputerMotion Incorporation (CMI), a medical robotics company. Prior to CMI, Mr. DeVivo held various positions at United States Surgical Corporation, a division of TYCO Healthcare, from May 1993 to August 2002, most recently as Vice President and General Manager of the U.S. Surgical/Davis and Geck Suture division from October 2001 through August 2002. Mr. DeVivo holds a B.S. in Business Administration from the E. Claiborne Robins School of Business at the University of Richmond.

**Randy Lindholm** has served as a member of our Board since April 2003. Mr. Lindholm is currently a consultant to several life sciences companies. Prior to that, Mr. Lindholm held various positions at VidaMed, Inc., a medical device company. From August 1999 to April 2002, at VidaMed, Inc., he served as Chairman, President and Chief Executive Officer and from July 1998 to August 1999, he served as Executive Vice President of Sales and Marketing. Mr. Lindholm is also a director of Omnicell, Inc., a medical supply company, as well as two private companies. Mr. Lindholm holds a B.S. in Electrical Engineering from Michigan Technological University.

The names of the Class I and Class II directors, their ages as of April 15, 2006 and certain other information about them are set forth below:

<u>Name of Nominee</u>	<u>Age</u>	<u>Principal Occupation</u>	<u>Director Since</u>
James E. Brands (3)	68	Principal, Brands & Co.	July 2004

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Vincent Bucci (1)(2)  
Thomas J. Dugan (2)(3)

51 President of Health Policy Associates, Inc.  
48 Senior Vice President, Marketing & Business  
Development at SonoSite, Inc.

March 1999  
November 2004

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Scott Halsted (1)	46	General Partner and Principal at Morgan Stanley, Dean Witter Venture Partners	May 1998
Wesley E. Johnson, Jr. (3)	48	General Manager of Abbot Spine, S.A., a division of Abbott Laboratories	August 2003
Steve LaPorte (2)	55	Retired Medtronic, Inc. Executive	September 2005

- (1) Member of the Compensation Committee of the Board.
- (2) Member of the Nominating/Corporate Governance Committee of the Board.
- (3) Member of the Audit Committee of the Board.

**James E. Brands** has served as a member of our Board since July 2004. Mr. Brands is the founder of Brands & Co., which provides business and financial consulting services, and has been active as Principal in such business from time to time since 1982. From April 2003 to July 2004, Mr. Brands served as a director of Horizon Medical Products, Inc., a medical device company, which merged with us in July 2004. From April 1999 until September 2001, Mr. Brands served as Senior Executive Vice President of Able Telcom Holding Corp., whose principal businesses were development of telecommunications networks and intelligent highway systems throughout the United States and in other parts of the world. Able Telecom merged with Adesta Communications, a wholly owned subsidiary of Able Telecom, and Adesta Communications filed a petition under the federal bankruptcy laws in November 2001. Mr. Brands holds an A.B. from Wesleyan University, an M.B.A. from the University of Chicago and a J.D. from Kennedy-Western University.

**Vincent Bucci** has served as a member of our Board since March 1999 and is currently the Chairman of the Board. Mr. Bucci has held the position of President of Health Policy Associates, Inc., a consulting company, since 1992. Mr. Bucci holds a B.A. from Bates College and a J.D. in Public Law and an M.A. in Government, both from Georgetown University.

**Thomas J. Dugan** has served as a member of our Board since November 2004. Mr. Dugan is Senior Vice President, Marketing & Business Development, of SonoSite, Inc., a medical device company. From October 2002 to November 2004, Mr. Dugan served as President of InterVascular, Inc., a subsidiary of Datascope Corp., a medical device company. From April 2001 to December 2002, Mr. Dugan served as Corporate Vice President, Business Development for Datascope. Prior to joining Datascope, Mr. Dugan was Vice President of Marketing for United States Surgical, a division of Tyco Healthcare, responsible for its Auto Suture and USS/D&G suture businesses from 1999 to 2001.

**Scott Halsted** has served as a member of our Board since May 1998. He has held the positions of General Partner and Principal of Morgan Stanley Dean Witter Venture Partners, a venture capital firm, since February 1997 and prior to that he was Vice President from January 1992 to January 1997. Mr. Halsted is also a director of Intuitive Surgical, Inc., a medical device company, and various private companies. Mr. Halsted holds an A.B. and a B.E. in Biomechanical Engineering from Dartmouth College and an M.M. from the Kellogg Graduate School of Management at Northwestern University.

**Wesley E. Johnson, Jr.** has served as a member of our Board since August 2003. Since October 2005, Mr. Johnson has served as General Manager of Abbott Spine, S.A., a division of Abbott Laboratories. From June 2003 to October 2005, Mr. Johnson served as Division Vice President, Finance for Abbott Spine. From May 1999 to June 2003, he served as Vice President of Operations and Chief Financial Officer for Spinal Concepts. Mr. Johnson holds a B.B.A. in Accounting from Texas A&M University and became a certified public accountant in 1981.

**Steve LaPorte** has served as a member of our Board since September 2005. From 2002 until his retirement in August 2005, Mr. LaPorte served as the Vice President of NeuroVentures and Business Development at Medtronic, Inc., a global leader in medical technology. Prior to this, from 2000 to 2002, Mr. LaPorte served as Vice President and General Manager of Medtronic's Drug Delivery Division; from 1994 to 2000, he held the position of Vice President and General Manager of Medtronic's Electrophysiology Systems Division; and from 1988 to 1994 he was the Vice President of Operations for Medtronic's Neurological Division. He began his career at Medtronic in 1978. Mr. LaPorte received his M.B.A. from the University of Minnesota and a B.S. in mathematics and computer science from the University of Wisconsin Stevens Point.

There are no family relationships among any of our directors or executive officers.

## Director Nomination

In February 2004, our Board established a Nominating/Corporate Governance Committee of the Board (the Nominating Committee). The Nominating Committee is responsible for, among other things, recommending to the Board nominees for possible election to the Board of Directors and providing oversight with respect to corporate governance matters. The information below describes the criteria and process that the Nominating Committee currently uses to evaluate future candidates to the Board of Directors.

*Criteria for Nomination to the Board.* The Nominating Committee considers the appropriate balance of experience, skills and characteristics required of the Board of Directors, and seeks to insure that at least a majority of the directors are independent under the rules of the NASDAQ Stock Market, and that members of the Audit Committee meet the financial literacy requirements under the rules of the NASDAQ Stock Market and at least one of them qualifies as an audit committee financial expert under the rules of the Securities and Exchange Commission. Nominees for director will be selected on the basis of their depth and breadth of experience, wisdom, integrity, ability to make independent analytical inquiries, understanding of the Company's business environment, and willingness to devote adequate time to Board duties.

*Stockholders Proposals for Nominees.* The Nominating Committee will consider written proposals from stockholders for nominees for director. Any such nominations should be submitted to the Nominating Committee c/o the Secretary of the Company and should include (at a minimum) the following information: (a) all information relating to such nominee that is required to be disclosed pursuant to Regulation 14A under the Securities Exchange Act of 1934 (including such person's written consent to being named in the proxy statement as a nominee and to serving as a director if elected); (b) the name(s) and address(es) of the stockholder(s) making the nomination and the number of shares of our common stock which are owned beneficially and of record by such stockholder(s); and (c) appropriate biographical information and a statement as to the qualification of the nominee, and should be submitted in the time frame described in the Bylaws of the Company and under the caption, Proposals for 2007 Annual Meeting above.

*Process for Identifying and Evaluating Nominees.* The process for identifying and evaluating nominees to the Board of Directors will be initiated by identifying a slate of candidates who meet the criteria for selection as a nominee and have the specific qualities or skills being sought based on input from members of the Board and, if the Nominating Committee deems appropriate, a third-party search firm. These candidates will be evaluated by the Nominating Committee by reviewing the candidates' biographical information and qualification and checking the candidates' references, and qualified nominees will be interviewed by at least one member of the Nominating Committee. Serious candidates will meet with all members of the Board, and using the input from such interviews and the information obtained by the Nominating Committee, the Nominating Committee will evaluate which of the prospective candidates is qualified to serve as a director and whether the committee should recommend to the Board that the Board nominate, or elect to fill a vacancy, with one of these final prospective candidates. Candidates recommended by the Nominating Committee will be presented to the Board for selection as nominees to be presented for the approval of the stockholders or for election to fill a vacancy.

The Nominating Committee expects that a similar process will be used to evaluate nominees recommended by stockholders. However, to date, the Company has not received any stockholder's proposal to nominate a director.

*Board Nominees for the 2006 Annual Meeting.* The nominees for this Annual Meeting were elected as follows:

Joseph DeVivo: elected by the Board in August 2003.

Randy Lindholm: elected by the Board in April 2003.

## Committees of the Board of Directors

Our Board has standing audit, compensation and nominating/corporate governance committees.

*Audit Committee.* Jim Brands, Tom Dugan and Wes Johnson (Chairman) are the current members of the Audit Committee. The Board has determined that all current members of the Audit Committee are independent directors under the rules of the NASDAQ Stock Market and each of them is able to read and understand fundamental financial statements. The Board has determined that Mr. Johnson qualifies as an audit committee financial expert as defined by the rules of the SEC. The purpose of the Audit Committee is to oversee the accounting and financial

reporting processes of the Company and audits of its financial statements. The responsibilities of the Audit Committee include, among other things, appointing and providing the compensation of our independent registered public accounting firm to conduct the annual audit of our accounts, reviewing the scope and results of the independent audits, reviewing and discussing annual and quarterly financial statements of the Company and approving all professional services to be provided to the Company by its independent registered public accounting firm. The Audit Committee has a written charter, which was adopted in February 2004. The Audit Committee's charter can be found on our website at [www.ritamedical.com](http://www.ritamedical.com).

*Compensation Committee.* Vin Bucci, Scott Halsted (Chairman) and Randy Lindholm are the current members of the Compensation Committee. The Board has determined that Messrs. Bucci and Halsted are independent directors under the rules of the NASDAQ Stock Market. In April 2005, the Board approved Mr. Lindholm's appointment to the Compensation Committee. The Board has not been able to determine if Mr. Lindholm is independent under applicable Nasdaq rules as a result of Mr. Lindholm's consulting relationship with the Company from 2003 to 2004. The Board has determined that Mr. Lindholm's participation on the Compensation Committee and his ongoing involvement in Company compensation matters is in the best interests of the Company and its stockholders and that he will serve on the Compensation Committee under an exception from the requirement that compensation committees be comprised solely of independent directors under applicable Nasdaq rules. The purpose of the Compensation Committee is to discharge the responsibilities of the Board with respect to compensation matters for our executive officers and other employees and consultants, report annually to our stockholders on executive compensation matters and administer our equity and other compensation plans. The responsibilities of the Compensation Committee include, among other things, establishing and administering our policies regarding annual executive salaries and cash incentives and long-term equity incentives and administering our 2000 Employee Stock Purchase Plan, our 2000 Directors' Stock Option Plan and the 2005 Stock and Incentive Plan. The Compensation Committee's charter can be found on our website at [www.ritamedical.com](http://www.ritamedical.com).

*Nominating/Corporate Governance Committee.* Vin Bucci, Tom Dugan and Steve LaPorte are the current members of the Nominating Committee. At the beginning of fiscal 2005, the Nominating Committee consisted of Tom Dugan, Scott Halsted and Robert Tucker. In July 2005, Mr. Tucker resigned from the Nominating Committee and the Board. In August 2005, the Nominating Committee was reconstituted to include Vin Bucci and Tom Dugan, with one vacancy. In September 2005, the Board approved Mr. LaPorte's appointment to the Board and the Nominating Committee. The Board has determined that all members of the Nominating Committee are independent directors under the rules of the NASDAQ Stock Market. The purpose of the Nominating Committee is to recommend nominees for election as directors of the Company, evaluate the Board's performance, develop and recommend to the Board corporate governance guidelines and provide oversight with respect to corporate governance and ethical conduct. The responsibilities of the Nominating Committee include, among other things, recommending to the Board nominees for possible election to the Board and providing oversight with respect to corporate governance matters. The Nominating Committee's charter can be found on our website at [www.ritamedical.com](http://www.ritamedical.com).

#### **Compensation Committee Interlocks and Insider Participation**

No member of the Compensation Committee or executive officer of the Company has, or in the past fiscal year had, a relationship that would constitute an interlocking relationship with executive officers or directors of another entity.

#### **Meetings of the Board and Committees of the Board**

During the last fiscal year (the period from January 1, 2005 through December 31, 2005), the Board met eight times, the Audit Committee met 19 times, the Compensation Committee met two times and the Nominating Committee met one time. Last year, each director attended at least 75% of all eligible Board and applicable committee meetings on which he served. Furthermore, the Compensation Committee and the Nominating Committee met informally many times either in person or by telephone throughout the year.

#### **Director Compensation**

To date, nonemployee directors have not been compensated for attendance at meetings of the Board or any committee but are reimbursed for reasonable and customary travel expenses. Commencing in the third quarter of 2006, however, the Company will pay its nonemployee directors a quarterly retainer as compensation for attendance

at meetings of the Board or any committee. The amount of any such retainer may be based on such factors as earnings, revenue, income and operating profit. For 2006, the Board has determined that the retainer will be \$5,000 per quarter, payable in cash or stock, for each nonemployee director other than the Chairman of the Board, who will be entitled to receive a retainer of \$10,000 per quarter, payable in cash or stock. The Board will consider adjusting the amount of the quarterly retainer payment in 2007.

All nonemployee directors are eligible to participate in the 2000 Directors' Stock Option Plan (the "Directors' Plan"). Employee directors and nonemployee directors are eligible to participate in the 2005 Stock and Incentive Plan. Employee directors are eligible to participate in the 2000 Employee Stock Purchase Plan. Employee directors receive no additional compensation for serving on the Board.

Under the Directors' Plan, when a nonemployee director first becomes a director, he or she receives a nonstatutory stock option to purchase 36,050 shares of our common stock. This option vests at a rate of 1/36th of the total number of shares subject to such option per month. Thereafter, on the date of each annual meeting of the Company's stockholders, each nonemployee director who has been a member for at least six months will be automatically granted a nonstatutory stock option to purchase 20,600 shares of our common stock, provided that a nonemployee director who is serving as Chairman of the Company will be granted a nonstatutory stock option to purchase 30,900 shares of our common stock (in lieu of the 20,600 share annual option grant that other nonemployee directors will receive). In addition, on the date of each annual meeting of the Company's stockholders, each nonemployee director who is at that time serving on a committee of the Board will be automatically granted a nonstatutory stock option to purchase 5,150 shares of our common stock. Finally, on the date of each annual meeting of the Company's stockholders, each nonemployee director who is at that time serving as a chairperson on a committee of the Board will be automatically granted a nonstatutory stock option to purchase 2,060 shares of our common stock. All options granted to nonemployee directors as of the date of each annual meeting of the Company's stockholders vest and become exercisable, assuming continued service on the Board throughout such period, as of the earlier of (a) the one year anniversary of the date of the option and (b) the date immediately preceding the date of the annual meeting of the Company's stockholders for the year following the year of grant of the option. The number of shares to be granted subject to each automatic option grant automatically increases each year by 3% of the number of shares subject to that type of automatic option grant for the previous year. The increase for 2006 is reflected in the summary above. All options granted under the Directors' Plan are for a ten-year term and shall be adjusted to reflect any stock splits, stock dividends, combinations or similar transactions. The exercise price of the options must be at least 100% of the fair market value of the common stock on the NASDAQ National Market on the date the option was granted. The options may be exercised only (1) while the individual is serving as a director on the Board, (2) within 6 months after termination by death or disability, or (3) within 3 months after the individual's term as director ends. Therefore, assuming that each of our nonemployee directors continues to hold his respective position(s) on the various committees of the Board, on the date of the Annual Meeting, our nonemployee directors, Messrs. Brands, Bucci, Dugan, Halsted, Johnson, Lindholm and LaPorte, will receive the following option grants: (1) Messrs. Brands, Dugan, LaPorte and Lindholm will each be granted options to purchase an aggregate of 25,750 shares of our common stock for their respective service as a director and as a member of one or more committees of the Board, (2) Messrs. Halsted and Johnson will each be granted options to purchase an aggregate of 27,810 shares of our common stock for their respective service as a director, a member of one or more committees of the Board and a chairperson of a committee and (3) Mr. Bucci will be granted options to purchase an aggregate of 36,050 shares of our common stock for his service as Chairman of the Board and as a member of one or more committees of the Board.

In April 2005, the Board granted options to purchase shares of our common stock to the nonemployee directors under our 2000 Stock Plan. The Audit Committee approved such grants. Mr. Bucci received an option grant to purchase 20,000 shares of our common stock in recognition of his services as Chairman of the Board during fiscal 2004, and Messrs. Brands, Bucci, Dugan, Halsted, Johnson, Lindholm and Tucker each received an option grant for 5,000 shares of our common stock in recognition of their services on one or more committees of the Board during fiscal 2004. All such options had an exercise price equal to \$3.07 per share (the closing price on the Nasdaq National Market for a share of our common stock on the date of grant) and were fully vested and immediately exercisable.

On June 8, 2005, the date of the Company's 2005 Annual Meeting of the Stockholders, our nonemployee directors, Messrs. Brands, Bucci, Dugan, Halsted, Johnson, Lindholm and Robert Tucker, received the following option grants under the Directors' Plan: (1) Messrs. Brands, Dugan and Lindholm were each granted options to purchase an aggregate of 25,000 shares of our common stock for their respective service as a director and as a member of one or more committees of the Board, (2) Messrs. Halsted, Johnson and Tucker were each granted options to purchase an aggregate of 27,000 shares of our common stock for their respective service as a director, a



member of one or more committees of the Board and a chairperson of a committee and (3) Mr. Bucci was granted options to purchase an aggregate of 35,000 shares of our common stock for his service as Chairman of the Board and as a member of one or more committees of the Board.

In September 2005, Mr. LaPorte was elected to the Board as a nonemployee director and received an automatic option grant for 35,000 shares of our common stock under the Directors' Plan.

#### **Communications with Directors**

Stockholders who wish to communicate with our directors to report complaints or concerns related to accounting, internal accounting controls or auditing may do so using the Company's Whistleblower Policy adopted by the Audit Committee in February 2004. The Company's Whistleblower Policy can be found on our website at [www.ritamedical.com](http://www.ritamedical.com).

The Company does not have a policy with regard to directors' attendance at annual meetings of stockholders. One director attended our 2005 Annual Meeting of Stockholders.

#### **Recommendation of the Board:**

**THE BOARD RECOMMENDS A VOTE *FOR* PROPOSAL NO. 1.**

#### **PROPOSAL NO. 2**

#### **APPROVAL OF AMENDMENT TO THE 2005 STOCK AND INCENTIVE PLAN**

At the Annual Meeting, you are being asked to approve an amendment to the RITA Medical Systems, Inc. 2005 Stock and Incentive Plan (the Stock Plan) to increase the number of shares of common stock reserved for issuance under the Stock Plan by 500,000 shares (representing less than 5% of the Company's outstanding common stock) from 5,376,746 shares to 5,876,746 shares. Stockholder approval of this amendment is being sought (i) for the purpose of qualifying options as incentive stock options, as defined in Section 422 of the Internal Revenue Code of 1986, as amended (the Code), and (ii) in accordance with the rules of the Nasdaq National Market, to permit the listing of shares purchased by officers, directors or key employees whether or not the Company could otherwise obtain listing without such approval.

The Stock Plan was adopted by the Board in April 2005, and it became effective on June 8, 2005 after approval of the stockholders at the 2005 Annual Meeting of Stockholders. In March 2006, the Board approved an amendment of the Stock Plan, subject to stockholder approval, to increase the number of shares of common stock issuable under the plan by an additional 500,000 shares to a total of 5,876,746 shares. The Board adopted this amendment because it believes that:

additional shares are necessary to attract new employees and executives;

additional shares are needed to further the goal of retaining and motivating existing personnel; and

the issuance of options and other stock awards to our employees is an integral component of the Company's compensation policy.

As of March 10, 2006, awards (net of canceled awards) covering an aggregate of 1,847,469 shares of common stock had been issued under the Stock Plan. An additional 2,889,809 shares issued under our 2000 Stock Plan remained outstanding. A total of 639,468 shares of common stock (plus up to 4,737,278 shares that might in the future be returned to the Stock Plan as a result of cancellations or expiration of awards) remained available for future grant under the Stock Plan. As of March 10, 2006, options outstanding under the Stock Plan and the Company's 2000 Stock Plan have per share exercise prices ranging from \$2.52 to \$11.63 or a weighted average per share exercise price of \$3.53.

As proposed to be amended, the Stock Plan will provide that an aggregate of up to 5,876,746 shares of our common stock will be reserved and available to be issued pursuant to awards granted under the Stock Plan. As of March 10, 2006, this maximum number of shares includes:

500,000 shares being reserved in connection with the amendment of the Stock Plan;

639,468 shares that are available for grant pursuant to awards that may be made under the Stock Plan; and

up to 4,737,278 shares that are subject to outstanding options granted under the Stock Plan or the 2000 Stock Plan which shares might be returned to the Stock Plan if and to the extent the options to which they are subject terminate or expire or become unexercisable for any reason without having been exercised in full.

The material terms of the Stock Plan include the following:

the types of awards that may be granted under the Stock Plan are stock options (including incentive stock options and nonstatutory stock options), restricted stock grants, restricted stock units, stock appreciation rights, stock purchase rights, and other similar types of awards (including other awards under which recipients are not required to pay any purchase or exercise price such as phantom stock rights), as well as cash awards;

the maximum number of shares subject to awards that may be granted to any one participant under the Stock Plan during any single fiscal year of the Company is 1,000,000 shares (the 162(m) Share Limit );

the maximum value of any cash award granted under the Stock Plan is \$500,000;

up to 400,000 shares of common stock may be granted under the Stock Plan as restricted stock grants, stock purchase rights and restricted stock units or any similar type of award that does not require the participant to pay the Company an amount equal to the fair market value of the common stock as of the award grant date in order to acquire the award shares, such as phantom stock rights (the Restricted Stock Limit );

stock-settled stock appreciation rights shall not be counted against the Restricted Stock Limit; provided however that the total number of shares to which a stock appreciation right applies (rather than the net number issued upon settlement) shall be deducted against the number of shares of common stock reserved for issuance under the Stock Plan upon settlement of the stock appreciation right;

the Company may not reprice or otherwise reduce the exercise price of outstanding options granted under the Stock Plan (other than in connection with certain corporate transactions such as stock splits, stock dividends or similar transactions) without the approval of our stockholders;

the number of shares reserved for issuance under the Stock Plan and subject to outstanding awards, the exercise or purchase price per share applicable to outstanding awards and the 162(m) Share Limit and the Restricted Stock Limit will each be adjusted to proportionately reflect the terms of certain corporate transactions including stock splits, stock dividends, and certain other transactions affecting the capital stock of the Company;

the maximum number of shares reserved for issuance under the Stock Plan is as described above;

shares subject to awards that expire or become unexercisable for any reason without having been exercised in full or without the shares subject thereto having been issued in full will become available for re-issuance under the Stock Plan;

shares of common stock which are retained by the Company upon exercise of an award in order to satisfy the exercise or purchase price of an award or any withholding taxes due with respect to the exercise or purchase shall not continue to be available for issuance under the Stock Plan; and

the Stock Plan will expire in 2015 (unless it expires or is terminated earlier pursuant to its terms).

Brokers do not have discretion to vote on this proposal without your instruction. If you do not instruct your broker how to vote on this proposal, your broker will deliver a non-vote on this proposal. Broker non-votes, if any, will have no effect on the outcome of the vote on this proposal. Abstentions will have the effect of a vote AGAINST the proposal.

### Summary of the Stock Plan

A copy of the Stock Plan is attached to this proxy statement as Appendix A. The following description of the Stock Plan is only a summary and so is qualified by reference to the complete text of the Stock Plan.

### General

The purpose of the Stock Plan is to offer incentives to attract and retain the best available personnel for positions of substantial responsibility and by providing additional incentive to employees and consultants to promote the success of the Company's business. Stock options, stock purchase rights, restricted stock, restricted stock units, stock appreciation rights and other similar types of awards (including other awards under which recipients are not required to pay any purchase or exercise price such as phantom stock rights), as well as cash awards may be granted under the Stock Plan (each an "Award"). Options granted under the Stock Plan may be either incentive stock options, as defined in section 422 of the Code, or non-statutory stock options.

*Administration.* The Stock Plan is administered by the Board and the Compensation Committee (the "Administrator").

*Eligibility.* Non-statutory stock options and stock awards may be granted under the Stock Plan to employees, directors (including nonemployee directors) and consultants of the Company, its parent and subsidiaries. Incentive stock options and cash awards may be granted only to employees of the Company or its subsidiaries. The Administrator, in its discretion, selects the employees to whom stock options and other stock awards, as well as cash awards, may be granted, the time or times at which such awards are granted, and the terms of such awards to be granted under the Stock Plan. As of March 10, 2006, the Company had approximately 225 officers, employees and consultants and seven nonemployee directors who would be eligible to participate in the Stock Plan.

*Nontransferability of Awards.* Unless otherwise determined by the Administrator, options and stock awards granted under the Stock Plan are not transferable other than by will or the laws of descent and distribution and may be exercised during the lifetime of the holder of the option or stock award only by the holder; provided that non-statutory stock options and stock awards may be transferred by gift to immediate family members of the participant or to a trust in which non-statutory stock options or stock awards are to be passed to a beneficiary of the participant upon the death of the participant.

### Stock Options

*Exercise Price.* The Administrator determines the exercise price of options at the time the options are granted. The exercise price of options granted under the Stock Plan may not be less than 100% of the fair market value of our common stock on the date of grant of such option, provided that the exercise price of an incentive stock option to an employee who is also a 10% stockholder must have an exercise price at least equal to 110% of the fair market value of our common stock on the date of grant of such option. The Company may grant options with exercise prices equal to less than 100% of the fair market value of our common stock on the date of grant in connection with an acquisition by the Company of another company. The fair market value of our common stock is generally the closing sales price as quoted on the Nasdaq National Market on the date of grant. No option may be repriced to reduce the exercise price of such option without stockholder approval (except in connection with a change in our capitalization, such as a stock split or a recapitalization).

*Exercise of Option; Form of Consideration.* The Administrator determines when options vest and become exercisable, and in its discretion may accelerate the vesting and/or exercisability of any outstanding option. The Company's standard vesting schedule applicable to options granted to new employees is 12.5% of the total number of shares vest on the six month anniversary of the vesting commencement date and 1/48th of the total number of shares vest on each subsequent monthly anniversary of the vesting commencement date. The means of payment for shares issued upon exercise of an option are specified in each option agreement. The Stock Plan permits payment to

be made by cash, check, promissory note, cancellation of indebtedness, other shares of common stock of the Company (with some restrictions), broker assisted same-day sale, withholding of shares subject to the option (with some restrictions) or any other means of consideration permitted by applicable law.

*Term of Option.* The term of an option may be no more than ten years from the date of grant; provided that the term of an incentive stock option may not be more than five years from the date of grant for an optionee who is also a 10% stockholder. No option may be exercised after the expiration of its term.

*Termination of Options.* Generally, if an optionee's services to the Company as an employee, consultant or director terminate other than for death or disability, vested options will generally remain exercisable for a period of three months following the optionee's termination. Unless otherwise provided for in the option agreement, generally if an optionee becomes disabled while an employee, consultant or director, the optionee's vested options shall be exercisable for six months following the optionee's termination as a result of disability, or if earlier, the expiration of the term of such option. Unless otherwise provided for in the option agreement, if an optionee dies during optionee's employment with the Company or within 30 days following termination of optionee's employment, optionee's vested options shall be exercisable for 12 months following the optionee's death, or if earlier, the expiration of the term of such option. The Administrator has the authority to extend the period of time for which an option is to remain exercisable following optionee's termination; provided that in no event will an option be exercisable later than the expiration of the term of the option.

### **Stock Awards**

Stock awards may be stock grants, stock purchase rights, stock units, stock appreciation rights or other similar types of awards (including phantom stock rights). A total of 400,000 shares may be granted under the Stock Plan pursuant to stock grants, stock purchase rights and stock units or any similar type of award that does not require the participant to pay the Company an amount equal to the fair market value of the stock award as of the award grant date in order to acquire the award shares, such as phantom stock rights. Stock grants are awards of a specific number of shares of our common stock. Stock purchase rights are rights to purchase our common stock. Stock units represent a promise to deliver shares of our common stock, or an amount of cash or property equal to the value of the underlying shares, at a future date. Stock appreciation rights are rights to receive cash and/or shares of our common stock based on a change in the fair market value of a specific number of shares of our common stock. Each stock award is evidenced by a stock award agreement between the Company and the participant. The Stock Plan allows the Administrator broad discretion to determine the terms of individual awards, including the number of shares that such participant shall be entitled to purchase or receive and the price (if any) to be paid by the recipient in connection with the issuance of the shares. Each stock award agreement will contain provisions regarding (i) the number of shares subject to such stock award or a formula for determining such number, (ii) the purchase price of the shares, if any, and the means of payment for the shares, (iii) the performance criteria (including the Qualifying Performance Criteria), if any, and level of achievement versus these criteria that will determine the number of shares granted, issued, retainable and vested, as applicable, (iv) such terms and conditions on the grant, issuance, vesting and forfeiture of the shares, as applicable, as may be determined from time to time by the Administrator, (v) restrictions on the transferability of the stock award, and (vi) such further terms and conditions, in each case not inconsistent with the Stock Plan, as may be determined from time to time by the Administrator. Shares may be granted under the Stock Plan as stock awards without requiring the participant to pay the Company an amount equal to the fair market value of our common stock as of the Award grant date in order to acquire the Award shares.

### **Cash Awards**

Cash awards granted under the Stock Plan will generally be made to individuals who are, or who the Company anticipates may be, one of our five most highly compensated officers (such individuals being those employees whose compensation may not be fully deductible by the Company under Code Section 162(m) if it exceeds with respect to a given year the limits imposed by that section). Each cash award granted under the Stock Plan will be subject to Qualifying Performance Criteria and will be reflected in an agreement containing provisions regarding (1) the target and maximum amount payable to the participant as a cash award, (2) the Qualifying Performance Criteria and level of achievement versus the criteria that will determine the amount of such payment, (3) the period as to which performance shall be measured for establishing the amount of any payment, (4) the timing of any payment earned by virtue of performance, (5) restrictions on the alienation or transfer of the cash award prior to actual payment, (6) forfeiture provisions, and (7) such further terms and conditions, in each case not inconsistent with the Stock Plan, as may be determined from time to time by the Administrator. The maximum amount payable as

a cash award may be a multiple of the target amount payable. The maximum amount payable pursuant to a cash award granted under the Stock Plan for any fiscal year may not exceed \$500,000. Nothing in the Stock Plan prevents the Company from granting cash awards outside of the Stock Plan to any individual.

#### **Adjustments on Changes in Capitalization, Merger or Change of Control**

In the event of any stock dividend, stock split, reverse stock split, recapitalization, combination, reclassification or similar change to the capital structure of the Company without receipt of consideration by the Company, appropriate adjustments will be made to (i) the number of shares subject to the Stock Plan, (ii) the 162(m) Share Limit, (iii) the exercise price and number of shares under each outstanding Award, and (iv) the Restricted Stock Limit. Any such adjustments shall be made by the Administrator, and the decision of the Administrator shall be final, binding and conclusive.

In the event of a change in control of the Company, as defined in the Stock Plan and determined by the Administrator, the Administrator, in its discretion, may provide for the assumption, substitution, or adjustment of each outstanding Award, accelerate the vesting of options and terminate any restrictions on stock awards or cash awards, or terminate Awards on such terms and conditions as the Administrator determines, including for a cash payment to the awardee.

In the event of a proposed dissolution or liquidation of the Company, each Award will terminate immediately prior to the consummation of the dissolution or liquidation, unless otherwise determined by the Administrator.

#### **Amendment and Termination of the Stock Plan**

The Board may amend, alter, suspend or discontinue the Stock Plan. However, the Company shall obtain stockholder approval for any amendment to the Stock Plan to the extent necessary and desirable to comply with applicable laws and Nasdaq National Market listing requirements. Generally, no such action by the Board or stockholders may alter or impair any outstanding Award under the Stock Plan without the written consent of the holder. In addition, no amendment shall be made that would reduce the exercise price of outstanding options without the written consent of the stockholders. The Stock Plan will terminate in June 2015 unless it expires or is terminated earlier pursuant to its terms.

#### **Federal Income Tax Consequences of Options under the Stock Plan**

THE FOLLOWING IS A GENERAL SUMMARY OF THE TYPICAL FEDERAL INCOME TAX CONSEQUENCES OF THE ISSUANCE AND EXERCISE OF OPTIONS OR AWARDS OF RESTRICTED STOCK UNDER THE STOCK PLAN. IT DOES NOT DESCRIBE STATE OR OTHER TAX CONSEQUENCES OF THE ISSUANCE AND EXERCISE OF OPTIONS OR OF GRANT OF RESTRICTED STOCK.

*Options.* The grant of an incentive stock option has no federal income tax effect on the optionee. Upon exercise the optionee does not recognize income for regular tax purposes. However, the excess of the fair market value of the stock subject to an option over the exercise price of such option (the option spread) is includible in the optionee's alternative minimum taxable income for purposes of the alternative minimum tax. If the optionee does not dispose of the stock acquired upon exercise of an incentive stock option until more than two years after the option grant date and more than one year after exercise of the option, any gain (or loss) upon sale of the shares will be a long-term capital gain (or loss). If shares are sold or otherwise disposed of before both of these periods have expired (a disqualifying disposition), the option spread at the time of exercise of the option (but not more than the amount of the gain on the sale or other disposition) is ordinary income in the year of such sale or other disposition. If gain on a disqualifying disposition exceeds the amount treated as ordinary income, the excess is taxable as capital gain (which will be long-term capital gain if the shares have been held more than one year after the date of exercise of the option). The Company is not entitled to a federal income tax deduction in connection with incentive stock options, except to the extent that the optionee has taxable ordinary income on a disqualifying disposition (unless limited by Section 162(m) of the Code).

The grant of a non-statutory option has no federal income tax effect on the optionee. Upon the exercise of a non-statutory option, the optionee has taxable ordinary income (and unless limited by Section 162(m) of the Code the Company is entitled to a corresponding deduction) equal to the option spread on the date of exercise. Upon the disposition of stock acquired upon exercise of a non-statutory stock option, the optionee recognizes either long-term

or short-term capital gain or loss, depending on how long such stock was held, on any difference between the sale price and the exercise price, to the extent not recognized as taxable income on the date of exercise. The Company may allow non-statutory stock options to be transferred subject to conditions and restrictions imposed by the Administrator; special tax rules may apply on such a transfer.

In the case of both incentive stock options and non-statutory stock options, special federal income tax rules apply if Company common stock is used to pay all or part of the option price, and different rules than those described above will apply if unvested shares are purchased on exercise of the option.

*Stock Awards.* Stock awards will generally be taxed in the same manner as non-statutory stock options. However, shares issued under a restricted stock award are subject to a substantial risk of forfeiture within the meaning of Section 83 of the Code to the extent the shares will be forfeited in the event that the participant ceases to provide services to the Company and are not transferable. As a result of this substantial risk of forfeiture, the participant will not recognize ordinary income at the time the award shares are issued. Instead, the participant will recognize ordinary income on the dates when the stock is no longer subject to a substantial risk of forfeiture, or when the stock becomes transferable, if earlier. The participant's ordinary income is measured as the difference between the amount paid for the stock, if any, and the fair market value of the stock on the date the stock is no longer subject to forfeiture.

The employee may accelerate his or her recognition of ordinary income, if any, and begin his or her capital gains holding period by timely filing (i.e., within thirty days of the share issuance date) an election pursuant to Section 83(b) of the Code. In such event, the ordinary income recognized, if any, is measured as the difference between the amount paid for the stock, if any, and the fair market value of the stock on the date of such issuance, and the capital gain holding period commences on such date. The ordinary income recognized by an employee will be subject to tax withholding by the Company. Unless limited by Section 162(m) of the Code, the Company is entitled to a deduction in the same amount as and at the time the employee recognizes ordinary income.

*Cash Awards.* Upon receipt of cash, the recipient will have taxable ordinary income, in the year of receipt, equal to the cash received. Any cash received will be subject to tax withholding by the Company. Unless limited by Section 162(m) of the Code, the Company will be entitled to a tax deduction in the amount and at the time the recipient recognizes compensation income.

#### **Accounting Treatment**

Beginning with the first quarter of fiscal 2006, the Company is generally required to recognize compensation expense in an amount equal to the fair value on the date of grant of all stock options under the Stock Plan. The fair value of an option will be based on the number of shares subject to the option. The Company uses a Black-Scholes valuation model to measure fair value of option grants. In addition, the Company is required to recognize compensation expense for other Awards under the Stock Plan. In general, the expense associated with each Award will be recognized over the requisite employee service period, generally the vesting period.

#### **Plan Benefits**

The number of Awards that an employee, officer, director and consultant may receive under the Stock Plan is in the discretion of the Administrator and therefore cannot be determined in advance. As of the date of this proxy statement, there has been no determination by the Administrator with respect to future Awards under the Stock Plan.

The following table shows the number of shares of common stock issuable upon exercise of options granted to the Named Executive Officers and named groups under the Stock Plan during the fiscal year ended December 31, 2005:

<u>Name and Position</u>	<u>Number of Shares (1)</u>
Joseph DeVivo, President, Chief Executive Officer and Director	200,000
Trent Reutiman, Former Vice President, U.S. Sales and Marketing	
Darrin Uecker, Chief Technology Officer	
John Soto, Vice President International Sales	60,000
Donald Stewart, Former Chief Financial Officer and Vice President, Finance and Administration	
All executive officers, as a group	260,000
All directors who are not executive officers, as a group	
All employees who are not executive officers, as a group	944,900

(1) All options granted at fair market value as of the date of grant.

**Recommendation of the Board:**

**THE BOARD OF DIRECTORS RECOMMENDS A VOTE *FOR* PROPOSAL NO. 2.**

**PROPOSAL NO. 3**

**RATIFICATION OF APPOINTMENT OF  
INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Audit Committee has approved the appointment of Stonefield Josephson, Inc. as our independent registered public accounting firm for the current fiscal year ending December 31, 2006. Stonefield Josephson, Inc. has served as our independent registered public accounting firm since 2005. In the event that ratification of this selection of accountants is not approved by a majority of the shares of common stock voting at the Annual Meeting in person or by proxy, the Audit Committee will review its future selection of auditors.

A representative of Stonefield Josephson, Inc. is expected to be present at the Annual Meeting. This representative will have an opportunity to make a statement and will be available to respond to appropriate questions.

**Recommendation of the Board:**

**THE BOARD OF DIRECTORS RECOMMENDS A VOTE *FOR* PROPOSAL NO. 3.**

**CODE OF ETHICS**

Our Board has adopted a code of ethics that applies to all officers and employees, including our principal executive officer, principal financial officer and controller. This code of ethics can be found on our website at [www.ritamedical.com](http://www.ritamedical.com). We will post any waivers from our code of ethics at that location.

**COMMON STOCK OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT**

The following table sets forth information known to the Company with respect to the beneficial ownership of the Company's common stock, as to (i) each person who is known to the Company to beneficially own more than 5% of our common stock, (ii) each of our directors, (iii) each of our Named Executive Officers (as defined below), and (iv) all directors and executive officers as a group. The percentages set forth below are based on shares of our common stock outstanding as of March 10, 2006. Unless otherwise noted below, the address of each person listed below is the Company's principal executive offices.

<b>5% Stockholders, Directors, Executive Officers and Directors and Executive Officers as a Group</b>	<b>Amount and Nature of Beneficial Ownership (1)</b>	<b>Percent of Common Stock (1)(2)</b>
Entities Affiliated with Atlas Master Fund, Ltd (3) c/o Walkers SPV Limited, Walker House P.O.Box 908 GT, George Town Grand Cayman, Cayman Islands, British West Indies	3,919,433	8.6 %
Entities Affiliated with SF Capital Partners, Ltd. (4) 3600 South Lake Drive St. Francis, WI 53235	2,380,238	5.5 %
Tocqueville Asset Management, L.P. (5) 1675 Broadway New York, New York 10019	2,172,930	5.0 %
Scott Halsted (6)	1,678,362	3.9%
Joseph DeVivo (7)	601,866	1.4%
Vincent Bucci (8)	228,000	*
Darrin Uecker (9)	142,000	*
Randy Lindholm (10)	111,875	*
John Soto (11)	81,666	*
Donald Stewart (12)	30,600	*
Wesley Johnson (13)	44,062	*
James Brands (14)	30,272	*
Thomas Dugan (15)	17,395	*
Steve LaPorte (16)	6,805	*
Trent Reutiman (17)	4,436	*
All directors and executive officers as a group (12 persons) (18)	2,977,339	6.7%
* Less than 1%		

- (1) The persons named in this table have sole voting and investment power with respect to all shares of common stock shown as beneficially owned by them, subject to community property laws where applicable and except as indicated in the other footnotes to this table.
- (2) In computing the number of shares beneficially owned by a person and the percentage ownership of that person, shares of common stock subject to options or warrants held by that person that are currently exercisable or exercisable within 60 days after March 10, 2006 are deemed outstanding. Such shares, however, are not deemed outstanding for the purpose of computing the percentage ownership of any other person. Beneficial ownership calculations for 5% stockholders are based on publicly filed Schedules 13D or 13G, which 5% stockholders are required to file with the SEC, and which generally set forth ownership interests as of December 31, 2005.



- (3) Includes 2,406,948 shares issuable upon conversion of subordinated senior convertible notes. Atlas Global, LLC, a Delaware limited liability company ( AG ), owns 19.1% of the equity interests in the selling stockholder and may be deemed to beneficially own all shares of our common stock shown as beneficially owned by the selling securityholder. Atlas Global Investments, Ltd., a Cayman Islands corporation ( AGI1 ), owns 73.4% of the equity interests in the selling stockholder and may be deemed to beneficially own all shares of our common stock shown as beneficially owned by the selling securityholder. Atlas Global Investments II, Ltd., a Cayman Islands corporation ( AGI2 ), owns 7.5% of the equity interests in the selling stockholder and may be deemed to beneficially own all shares of our common stock shown as beneficially owned by the selling securityholder. Balyasny Asset Management L.P., a Delaware limited partnership ( BAM ), is the sole managing member of AG and is the investment manager to each of AG, AGI1 and AGI2. By virtue of its position as investment manager of each of AG, AGI1 and AGI2 and its role as sole managing member of AG, BAM may be deemed to beneficially own all shares of our common stock shown as beneficially owned by the selling securityholder. Dmitry Balyasny is the sole managing member of the general partner of BAM and as such, Mr. Balyasny may be deemed to beneficially own all shares of our common stock shown as beneficially owned by the selling securityholder.
- (4) Represents the combined indirect holdings of Michael A. Roth and Brian J. Stark, as joint filers. All of the shares are held directly by SF Capital Partners, Ltd., a British Virgin Islands company. Messrs. Roth and Stark are the founding members and direct the management of Staro Asset Management, L.L.C., a Wisconsin limited liability company, which (i) acts as investment manager and has sole power to direct the management of Shepherd Investments International, Ltd., a British Virgin Islands corporation, and (ii) acts as general partner and has sole power to direct the management of Stark Investments Limited Partnership, a Wisconsin limited partnership, which serves as the general partner of Stark Trading, a Wisconsin general partnership. Shepherd Investments International, Ltd. and Stark Trading are the controlling owners of SF Capital Partners, Ltd. Through Staro, Messrs. Roth and Stark possess sole voting and dispositive power over all of the foregoing shares.
- (5) Tocqueville Asset Management, L.P. filed a Schedule 13G Statement with the SEC stating that as of December 31, 2005, it may be deemed to have sole voting power with respect to 2,099,990 shares of our common stock, and sole dispositive power over 2,172,930 shares of our common stock.
- (6) Includes 1,435,988 shares, 137,874 shares and 62,500 shares held by Morgan Stanley Venture Partners III, L.P., Morgan Stanley Venture Investors III, L.P. and The Morgan Stanley Venture Partners Entrepreneur Fund L.P., respectively. Mr. Halsted, a director of the Company, is a general partner of Morgan Stanley Venture Partners. Mr. Halsted disclaims beneficial ownership of the shares held by these entities except to the extent of his proportional interest in the entities. The figure shown further includes 42,000 shares issuable upon exercise of options exercisable within 60 days after March 10, 2006.
- (7) Includes 561,866 shares issuable upon exercise of options exercisable within 60 days after March 10, 2006.
- (8) Includes 113,876 shares issuable upon exercise of options exercisable within 60 days after March 10, 2006.
- (9) Includes 136,500 shares issuable upon exercise of options exercisable within 60 days after March 10, 2006.
- (10) Includes 91,875 shares issuable upon exercise of options exercisable within 60 days after March 10, 2006.
- (11) Includes 81,666 shares issuable upon exercise of options exercisable within 60 days after March 10, 2006.
- (12) Mr. Stewart's employment with the Company terminated on October 19, 2005.
- (13) Includes 39,062 shares issuable upon exercise of options exercisable within 60 days after March 10, 2006.
- (14) Includes 30,272 shares issuable upon exercise of options exercisable within 60 days after March 10, 2006.
- (15) Includes 17,395 shares issuable upon exercise of options exercisable within 60 days after March 10, 2006.
- (16) Includes 6,805 shares issuable upon exercise of options exercisable within 60 days after March 10, 2006.
- (17) Mr. Reutiman's employment with the Company terminated on January 9, 2006.
- (18) Includes 1,121,317 shares issuable upon exercise of options exercisable within 60 days after March 10, 2006.

### COMPENSATION OF EXECUTIVE OFFICERS

The following table shows the compensation paid by the Company for services rendered during the Company's three preceding fiscal years to (a) the individual who served as our Chief Executive Officer during the fiscal year ended December 31, 2005, (b) the three other most highly compensated individuals who served as executive officers of the Company as of December 31, 2005, and (c) an additional individual who would have been included in the three most highly compensated individuals, except that he was not serving as an executive officer on December 31, 2005 (the Named Executive Officers).

#### Summary Compensation Table

Name and Principal Position	Fiscal Year	Annual Compensation			Long-Term Compensation		All Other Compensation
		Salary (\$)(1)	Bonus (\$)	Other Annual Compensation (\$)	Restricted Securities Awards (\$)	Underlying Options (#)	
<b>Joseph DeVivo</b>	2005	263,033				200,000	
President, Chief Executive Officer and Director	2004	263,218	52,607			190,000	
	2003	97,500		42,079	(2)	692,175	100,000(3)
<b>Trent Reutiman</b>	2005	200,000	21,185	6,000	(5)		
Former Vice President, U.S.Sales and Marketing (4)	2004	103,561	126,820	6,000	(5)	60,000	24,500(6)
	2003	100,000	91,281	6,000	(5)	25,200	23,000(6)
<b>Darrin Uecker</b>	2005	215,000					
Chief Technology Officer	2004	209,520	29,563	75,000(7)		247,000	10,000(8)
	2003						
<b>John Soto</b>	2005	186,926	159,603			60,000	
Vice President, International Sales	2004	191,181	57,347			15,000	
	2003	56,491	13,750			100,000	
<b>Donald Stewart</b>	2005	164,354					228,239 (10)
Former Chief Financial Officer and Vice President, Finance and Administration (9)	2004	204,932	28,142			15,000	
	2003	196,381	27,500			61,250	

- (1) Includes amounts deferred under our 401(k) plan.
- (2) Mr. DeVivo received \$9,367 in reimbursed moving expenses in 2003. An additional \$32,712 related to relocation expenses incurred in 2004 was accrued in 2003.
- (3) Mr. DeVivo received a \$100,000 signing bonus in 2003.
- (4) Mr. Reutiman's employment with the Company terminated on January 9, 2006.
- (5) Mr. Reutiman received a \$6,000 auto allowance in 2005, 2004 and 2003.
- (6) Mr. Reutiman received housing allowance payments of \$24,500 in 2004 and \$23,000 in 2003.

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- (7) Mr. Uecker received \$75,000 in reimbursed moving expenses in 2004.
- (8) Mr. Uecker received a \$10,000 signing bonus in 2004.
- (9) Mr. Stewart also served as our Acting Chief Executive Officer from May 2003 to August 2003. Mr. Stewart's employment with the Company terminated on October 19, 2005.

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- (10) Mr. Stewart's severance, paid vacation and retention bonus totaled \$156,018. He further recognized ordinary income related to disqualifying dispositions of stock options in the amount of \$72,221.

**OPTION GRANTS IN LAST FISCAL YEAR**

The following table provides certain information with respect to stock options granted to Named Executive Officers in the last fiscal year out of our 2005 Stock and Incentive Plan. In addition, as required by SEC rules, the table sets forth the hypothetical gains that would exist for the options based on assumed rates of annual compound stock price appreciation during the option term.

Individual Grants (1)						
Name	Number of Securities Underlying Options Granted	Percent of Total Options Granted to Employees in Fiscal Year 2005(3)	Exercise Price (\$/sh)(4)	Expiration Date	Potential Realizable Value at Assumed Annual Rates of Stock Price Appreciation for Option Term (2)	
					5%	10%
<b>Joseph DeVivo</b>	200,000	11.1%	\$ 4.18	12/2/2015	\$ 525,756	\$ 1,332,369
<b>Trent Reutiman</b>						
<b>Darrin Uecker</b>						
<b>John Soto</b>	60,000	3.3%	\$ 4.18	12/2/2015	\$ 157,727	\$ 399,711
<b>Donald Stewart</b>						

- (1) No stock appreciation rights were granted to the Named Executive Officers in the last fiscal year. The options granted have a 10-year term. Options granted to the Named Executive Officers vest at the rate of 2.0833% on each monthly anniversary of the grant date. All of the granted options are subject to earlier termination in connection with termination of employment.
- (2) The potential realizable value illustrates the value that might be realized upon the exercise of the options immediately prior to the expiration of their terms, assuming the specified compounded rates of appreciation of the market price on the date of grant through the option term, less the exercise price. Actual gains, if any, on stock option exercise are dependent upon a number of factors, including the future performance of the common stock and the timing of option exercises, as well as the optionees' continued employment throughout the vesting period. There can be no assurance that the amounts reflected in this table will be achieved.
- (3) The Company granted 1,805,900 options to purchase common stock to employees in the last fiscal year.
- (4) The exercise price may be paid in cash, in shares of common stock valued at fair market value on the exercise date or through a cashless exercise procedure involving a same-day sale of the purchased shares.

**Equity Compensation Plan Information**

The following table provides information as of March 10, 2006 with respect to the shares of our common stock that may be issued under our existing equity compensation plans.

Plan Category	Number of Securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in Column (a))
	(a)	(b)	(c)

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Equity compensation plans approved by security holders: (1)	5,397,682	\$	3.49 (2)	1,224,178(3)
Equity compensation plans not approved by security holders: (4)	2,373,659	\$	1.63	
<b>Total</b>	<b>7,771,341</b>	<b>\$</b>	<b>2.92</b>	<b>1,224,178</b>

- (1) Consists of the following equity compensation plans:

2005 Stock and Incentive Plan  
 2000 Stock Plan  
 2000 Directors Stock Option Plan  
 2000 Employee Stock Purchase Plan  
 1994 Incentive Stock Plan

- (2) Assumes that employees will purchase the remaining 197,165 shares of common stock available for issuance under the 2000 Employee Stock Purchase Plan in August 2006 at a purchase price of \$3.4425 per share. Under the terms of the 2000 Employee Stock Purchase Plan, shares are purchased at 85% of the fair market value of our common stock on either the first day of an offering period or the last day of a purchase period, whichever is lower. Therefore, the purchase price is not fixed until the August 2006 purchase date, and employees may purchase the shares at a lower price per share, affecting the weighted-average exercise price.
- (3) The 2000 Employee Stock Purchase Plan incorporates an evergreen provision pursuant to which, on the first day of each of our fiscal years (through fiscal 2010), the number of shares available for future issuance under the 2000 Employee Stock Purchase Plan automatically increases by the lesser of (i) 650,000 shares; (ii) 4% of our outstanding common stock on the last day of the immediately preceding fiscal year; or (iii) such lesser number of shares as the Board of Directors determines. In April 2006, the Board of Directors determined that the number of shares available for future issuance under the 2000 Employee Stock Purchase Plan would not be increased for fiscal 2006.
- (4) Consists of the Horizon Medical Products 1998 Incentive Stock Plan.

**AGGREGATED OPTION EXERCISES IN LAST FISCAL YEAR AND FISCAL YEAR-END OPTION VALUES**

The following table sets forth certain information with respect to stock options exercised by the Named Executive Officers during the fiscal year ended December 31, 2005. In addition, the table sets forth the number of shares covered by stock options as of the fiscal year ended December 31, 2005, and the value of in-the-money stock options, which represents the positive spread between the exercise price of a stock option and the market price of the shares subject to such option at the end of the fiscal year ended December 31, 2005.

Name	Shares Acquired on Exercise	Value Realized	Number of Securities Underlying Unexercised Options at 12/31/2005 (1)		Value of Unexercised In-the-Money Options at December 31, 2005 (2)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
Joseph DeVivo		\$	455,226	626,949	\$ 613,210	\$ 540,813
Trent Reutiman			136,553	59,335	114,167	58,851
Darrin Uecker			108,562	138,438	12,856	34,614
John Soto			60,311	114,689	48,539	45,611
Donald Stewart	76,250	\$ 72,221	156,250			

- (1) No stock appreciation rights (SARs) were outstanding during fiscal 2005.
- (2) Based on the \$3.91 closing price of our common stock on the Nasdaq Stock Market on December 30, 2005, less the exercise price of the options.



## Employment Agreements

*Joseph DeVivo.* We have an employment agreement with Joseph DeVivo, our President and Chief Executive Officer, which among other things provides for the payment of severance or the acceleration of unvested options in certain circumstances. Mr. DeVivo's employment agreement provides that he will have up to 18 months to exercise his initial option grant, to the extent vested, if his employment is terminated after a change of control transaction. Mr. DeVivo's agreement also provides that if his employment with us is terminated without cause (including as a result of constructive termination), and provided that he executes our standard form or release agreement releasing any claims he may have against us, Mr. DeVivo will receive monthly severance payments, equal to 1/12th of his annual base salary and reimbursement for his continued medical coverage until the earlier of (i) 12 months after his termination date or (ii) such time as he accepts an offer of employment or consulting relationship which constitutes the equivalent of a full-time position or which compensates him at a level equal to the level of compensation provided by the Company on the date of termination of his employment. Mr. DeVivo is also a party to our standard form of change of control agreement that is described in more detail below.

*Michael Angel.* We have an employment agreement with Michael Angel, our Chief Financial Officer, which among other things provides for the payment of severance in certain circumstances. Mr. Angel's agreement provides that if his employment with us is terminated without cause, and provided that he executes our standard form or release agreement releasing any claims he may have against us, Mr. Angel will receive monthly severance payments, equal to 1/12th of his annual base salary and reimbursement for his continued medical coverage until the earlier of (i) 12 months after his termination date or (ii) such time as he accepts an offer of employment or consulting relationship which constitutes the equivalent of a full-time position. Mr. Angel is also a party to our standard form of change of control agreement that is described in more detail below.

*John J. Soto.* We have an employment agreement with John J. Soto, our Vice President, International, which among other things provides for the payment of severance in certain circumstances. Mr. Soto's agreement provides that if his employment with us is terminated without cause, Mr. Soto will receive monthly severance payments, equal to 1/12th of his annual base salary until the earlier of (i) six months after his termination date or (ii) such time as he obtains alternative full-time employment. Mr. Soto is also a party to our standard form of change of control agreement that is described in more detail below.

*Darrin Uecker.* We have an employment agreement with Darrin Uecker, our Chief Technology Officer, which among other things provides for the payment of severance in certain circumstances. Mr. Uecker's agreement provides that if his employment with us is terminated without cause, and provided that he executes our standard form or release agreement releasing any claims he may have against us, Mr. Uecker will receive monthly severance payments, equal to 1/12th of his annual base salary and reimbursement for his continued medical coverage until the earlier of (i) six months after his termination date or (ii) such time as he accepts an offer of employment or consulting relationship which constitutes the equivalent of a full-time position.

*Mario Martinez.* We have an employment agreement with Mario Martinez, our Vice President of Operations and General Manager, which among other things provides for the payment of severance in certain circumstances. Mr. Angel's agreement provides that if his employment with us is terminated without cause, and provided that he executes our standard form or release agreement releasing any claims he may have against us, Mr. Angel will receive monthly severance payments, equal to 1/12th of his annual base salary and reimbursement for his continued medical coverage until the earlier of (i) six months after his termination date or (ii) such time as he accepts an offer of employment or consulting relationship which constitutes the equivalent of a full-time position. Mr. Angel is also a party to our standard form of change of control agreement that is described in more detail below.

## Transactions with Security Holders

On August 5, 2005, we completed a private placement of subordinated Senior Convertible Notes (the "New Notes") with an aggregate principal amount of \$9.7 million. The New Notes were issued pursuant to a Securities Purchase Agreement (the "Purchase Agreement") among the Company and Atlas Master Fund, Ltd., which is not related to us. No warrants or other securities were issued in conjunction with the Purchase Agreement and we incurred no financing costs other than normal and customary legal and other professional expenses. The New Notes are convertible into shares of our common stock at an initial conversion price of \$4.03 per share of common stock which was greater than the per share fair market value of our common stock on the date of issuance of the New Notes. The conversion price is subject to adjustment in certain circumstances including common stock splits or other standard anti-dilution provisions. Until conversion or maturity, the New Notes bear interest at the rate of 6.5% per annum, payable semiannually in cash. Absent conversion, the New Notes mature on August 5, 2008 (the "Maturity



Date ). If on the Maturity Date the closing price of the common stock has been at or above 102% of the then current conversion price for at least 10 consecutive business days immediately preceding the Maturity Date, then any remaining principal outstanding under the New Notes shall automatically be converted into common stock, subject to certain conditions. The issuance of the New Notes was deemed to be exempt from registration under the Securities Act of 1933 in reliance upon Section 4(2) thereof as transactions by an issuer not involving any public offering.

As of the issuance date of the New Notes, we also owed \$8.3 million plus accrued interest to holders of our Senior Subordinated Convertible Notes (the Senior Notes ) and \$1.4 million plus accrued interest to the holder of our Junior Promissory Note (the Junior Note ). Pursuant to the terms of the New Notes, the Company was required to repay the Senior Notes and the Junior Note within 21 days of the issuance of the New Notes, or August 26, 2005. The Senior Notes were repaid on August 9, 2005 and the Junior Note was repaid on August 11, 2005.

### **Change of Control Agreements**

We have entered into change of control agreements with our officers that provide the following benefits upon the sale or merger of the Company. In the event that we consummate a change of control transaction, 50% of any unvested options held by our officers shall become fully vested and immediately exercisable and repurchase rights retained by us with respect to 50% of the restricted stock held by our officers shall immediately lapse. In addition, on each one month anniversary following the effective date of a change of control transaction, 1/12th of the remaining unvested options held by our officers shall become fully vested and immediately exercisable and repurchase rights retained by us with respect to 1/12th of any remaining restricted stock held by our officers shall immediately lapse.

If the officer is involuntarily terminated within 12 months after the change of control transaction, all unvested options held by our officers shall become fully vested and immediately exercisable and all repurchase rights retained by us with respect to the restricted stock held by our officers shall immediately lapse. If the officer voluntarily resigns or is terminated for cause after the change of control, then the officer is not entitled to any acceleration of the vesting of options or lapse of repurchase rights with respect to restricted stock.

### **Separation Agreements**

During the year ended December 31, 2005, we entered into a separation agreement with Donald Stewart, our former Chief Financial Officer.

### **Indemnification of Directors and Executive Officers**

We have entered into indemnification agreements with our officers and directors containing provisions which may require us, among other things, to indemnify our officers and directors against a number of liabilities that may arise by reason of their status or service as officers or directors (other than liabilities arising from willful misconduct of a culpable nature) and to advance their expenses incurred as a result of any proceeding against them as to which they could be indemnified. Insofar as indemnification for liabilities arising under the Securities Act of 1933 may be permitted to directors, officers or persons controlling us pursuant to the foregoing provisions, we have been informed that in the opinion of the SEC such indemnification is against public policy as expressed in the Securities Act and is therefore unenforceable.

### **Other Relationships**

Vincent Bucci, a member of our Board, is the President of Health Policy Associates, Inc. In 2004, Health Policy Associates, Inc. provided consulting services to us in a variety of areas related to U.S. Food and Drug Administration regulations including clinical studies, regulatory affairs and quality assurance and was paid approximately \$14,000.

Randy Lindholm, a member of our Board, began providing consulting services to us in April 2003 pursuant to a consulting agreement which was amended in August 2003. During 2004, in connection with these consulting services, Mr. Lindholm was granted an option to purchase 10,000 shares of our common stock. These options have an exercise price of \$3.50 per share and vest at a rate of 1/24th per month from August 5, 2004.

*Notwithstanding anything to the contrary set forth in any of the Company's filings under the Securities Act of 1933 or the Securities Exchange Act of 1934 that might incorporate future filings, including this Proxy Statement, in whole or in part, the Compensation Committee Report, the Audit Committee Report and the Stock Performance Graph shall not be deemed to be incorporated by reference into any such filings.*

## COMPENSATION COMMITTEE REPORT ON EXECUTIVE COMPENSATION

The following is a report of the Compensation Committee of the Board of Directors of RITA Medical Systems, Inc. (the "Compensation Committee") describing the compensation policies applicable to the Company's executive officers during the fiscal year that ended December 31, 2005. Vincent Bucci, Scott Halsted (Chairman) and Randy Lindholm are the current members of the Compensation Committee. Messrs. Bucci and Halsted have been determined to be independent directors under the rules of the NASDAQ Stock Market. In April 2005, the Board approved Mr. Lindholm's appointment to the Compensation Committee. The Board has not been able to determine if Mr. Lindholm is independent under applicable NASDAQ rules as a result of Mr. Lindholm's prior consulting relationship with the Company. The Board has determined that Mr. Lindholm's participation on the Compensation Committee and his ongoing involvement in Company compensation matters is in the best interests of the Company and its stockholders and that he will continue to serve on the Compensation Committee under an exception from the requirement that compensation committees be comprised solely of independent directors under applicable NASDAQ rules. Messrs. Bucci and Halsted are each a nonemployee director within the meaning of Section 16 of the Securities and Exchange Act and an outside director within the meaning of Section 162(m) of the Internal Revenue Code. The purpose of the Compensation Committee is to discharge the responsibilities of the Board with respect to compensation matters for our executive officers and other employees and consultants, report annually to our stockholders on executive compensation matters and administer our equity and other compensation plans. The responsibilities of the Compensation Committee include, among other things, establishing and administering our policies regarding annual executive salaries and cash incentives and long-term equity incentives and administering our 2005 Stock and Incentive Plan, 2000 Employee Stock Purchase Plan and 2000 Directors Stock Option Plan.

### General Compensation Policy

Under the supervision of the Board of Directors, our compensation policy is designed to attract and retain qualified key executives critical to our growth and long term success. It is the objective of the Board of Directors to have a portion of each executive's compensation contingent upon our performance as well as upon the individual's personal performance. Accordingly, each executive officer's compensation package is comprised of three elements: (i) base salary which reflects individual performance and expertise, (ii) variable bonus awards payable in cash and tied to the achievement of certain performance goals that the Board of Directors establishes from time to time for the Company, and (iii) long term stock-based incentive awards which are designed to strengthen the mutuality of interests between the executive officers and our stockholders.

The summary below describes in more detail the factors which the Board of Directors considers in establishing each of the three primary components of the compensation package provided to the executive officers.

### Base Salary

The level of base salary is established primarily on the basis of the individual's qualifications and relevant experience, the strategic goals for which he or she has responsibility, the compensation levels at similar companies and the incentives necessary to attract and retain qualified management. Base salary is adjusted each year to take into account the individual's performance and to maintain a competitive salary structure. Company performance does not play a significant role in the determination of base salary.

During fiscal 2005, the Compensation Committee reviewed and adjusted the base salaries for the Company's executive officers by evaluating the factors described above and considering the recommendations of the Company's Chief Executive Officer.

### Cash-Based Incentive Compensation

Cash bonuses are awarded on a discretionary basis to executive officers and other managers on the basis of their success in achieving designated individual goals and our success in achieving specific company-wide goals, such as revenue growth and earnings. For fiscal 2005, the Company adopted its Performance Incentive Plan, which

set maximum targeted cash bonuses for participating executive officers ranging from 27.5% to 40.0% of their base salaries, and lesser amounts for other participating managers. In 2005, nothing was earned under this plan, and no payments have been or will be made.

In addition, the Company maintains a sales incentive program for its sales force that pays commissions based on the performance of the sales team toward the Company's revenue targets. In 2005, Mr. Soto, our Vice President, International Sales, participated in this sales incentive program, earning commissions of \$151,749. His participation in the sales incentive program is in lieu of participating in the Performance Incentive Program.

### **Long-Term Incentive Compensation**

We have utilized our stock option plans to provide executives and other key employees with incentives to maximize long-term stockholder values. Awards under this plan by the Board of Directors take the form of stock options designed to give the recipient a significant equity stake and thereby closely align his or her interests with those of our stockholders. Factors considered in making such awards include the individual's position, his or her performance and responsibilities, and internal comparability considerations. In addition, the Board of Directors has established certain general guidelines in making option grants to the executive officers in an attempt to target a fixed number of unvested option shares based upon each individual's position and his or her existing holdings of unvested options. However, the Board of Directors is not required to adhere strictly to these guidelines and may vary the size of the option grant made to each executive officer as it determines the circumstances warrant. Each option grant allows the executive officer to acquire shares of common stock at a fixed price per share (the fair market value on the date of grant) over a specified period of time (up to 10 years). The options typically vest in periodic installments over a four year period, contingent upon the executive officer's continued employment with us. Accordingly, the option will provide a return to the executive officer only if he or she remains in our service, and then only if the market price of the common stock appreciates over the option term.

In accordance with this policy, during fiscal 2005, the existing equity-based compensation of the executive officers was reviewed and the Compensation Committee made new grants of stock options to executive officers under the Company's 2005 Stock and Incentive Plan. In the aggregate, these options provided our executive officers with rights to purchase 260,000 shares of our common stock at a price of \$4.18 per share.

In addition to participating in the Company's 2005 Stock and Incentive Plan, the Company's executive officers may also participate in the Company's 2000 Employee Stock Purchase Plan on the same basis as other employees who meet eligibility criteria. This plan is qualified under Section 423 of the Internal Revenue Code, and it allows participants to purchase, through payroll deductions, shares of our common stock at a price equal to 85% of its fair market value on the enrollment date or the purchase date, whichever is lower.

### **Compensation of the Chief Executive Officer**

Joseph DeVivo has served as the Company's President and Chief Executive Officer since August 2003. His annual base salary for the fiscal year ended December 31, 2005 was \$263,033, which was determined based on the factors described above. For fiscal 2005, Mr. DeVivo was eligible to participate in the Performance Incentive Plan with a targeted cash bonus of up to 40% of his base salary, but he earned and was paid no bonus under this plan. Also during 2005, in accordance with the policy described above in Long-Term Incentive Compensation, Mr. DeVivo was granted options to purchase 200,000 shares of our common stock. These options have an exercise price of \$4.18 per shares and vest at the rate of 1/48th per month from December 2, 2005.

In connection with his joining the Company in August 2003, Mr. DeVivo was paid a \$100,000 signing bonus. In addition, Mr. DeVivo was granted an option to purchase 692,175 shares of our common stock, which vests at the rate of 25% of the total number of shares on August 18, 2004 and 1/48th of the total number of shares each month thereafter. The factors discussed above in Base Salary, Cash-Based Incentive Compensation and Long-Term Incentive Compensation were considered in establishing the amount of Mr. DeVivo's base salary, cash bonus and stock option grant at the time of his hiring.

### **Deductibility of Executive Compensation**

The Compensation Committee has considered the impact of Section 162(m) of the Internal Revenue Code adopted under the Omnibus Budget Reconciliation Act of 1993, which section disallows a deduction for any publicly held corporation for individual compensation exceeding \$1 million in any taxable year for the Chief Executive

Officer and four other most highly compensated executive officers, respectively, unless such compensation meets the requirements for the performance-based exception to Section 162(m). As the cash compensation paid by the Company to each of its executive officers is expected to be below \$1 million and the committee believes that options granted under the 2000 Stock Plan and the 2005 Stock and Incentive Plan to such officers will meet the requirements for qualifying as performance-based, the committee believes that Section 162(m) will not affect the tax deductions available to the Company with respect to the compensation of its executive officers. It is the Compensation Committee's policy to qualify, to the extent reasonable, its executive officers' compensation for deductibility under applicable tax law. However, the Company may from time to time pay compensation to its executive officers that may not be deductible.

*The Compensation Committee of the Board of Directors of RITA Medical Systems, Inc.:*

Vincent Bucci  
Scott Halsted  
Randy Lindholm

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### AUDIT COMMITTEE REPORT

The Audit Committee of the Board of Directors of RITA Medical Systems, Inc. (the "Audit Committee") is composed of three independent directors and operates under a written charter originally adopted by the Board of Directors in May 2000 and most recently amended in February 2004. Jim Brands, Tom Dugan and Wes Johnson (Chairman) are the current members of the Audit Committee. The Company's Board of Directors has determined that all members of the Audit Committee are independent directors under the rules of the NASDAQ Stock Market and each of them is able to read and understand fundamental financial statements. The Company's Board of Directors has determined that Mr. Johnson qualifies as an "audit committee financial expert" as defined by the rules of the SEC.

The purpose of the Audit Committee is to oversee the accounting and financial reporting processes of the Company and audits of its financial statements. The Audit Committee selects, subject to stockholder ratification, an accounting firm to be engaged as the Company's independent registered public accounting firm. The independent registered public accounting firm is responsible for performing an independent audit of the Company's financial statements in accordance with generally accepted auditing standards and to issue a report thereon. Management is responsible for the Company's internal controls and the financial reporting process. The Audit Committee is responsible for, among other things, monitoring and overseeing these processes, reviewing and discussing annual and quarterly financial statements of the Company and approving all professional services to be provided to the Company by its independent registered public accounting firm.

The Audit Committee held 19 meetings during the fiscal year 2005. The Audit Committee had a year end meeting in March 2006 with management and the Company's independent registered public accounting firm, Stonefield Josephson, Inc. Management represented to the Audit Committee that the Company's financial statements were prepared in accordance with generally accepted accounting principles. The Audit Committee reviewed and discussed the audited financial statements for fiscal year 2005 with management and the independent registered public accounting firm.

The Audit Committee discussed with the independent registered public accounting firm the matters required to be discussed by Statement on Auditing Standards No. 61, Communication with Audit Committees.

The Audit Committee has received and reviewed the written disclosures and the letter from the independent registered public accounting firm, Stonefield Josephson, Inc. as required by Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees. Additionally, the Audit Committee has discussed with Stonefield Josephson, Inc. the issue of its independence from the Company.

Based on its review of the audited financial statements and the various discussions noted above, the Audit Committee recommended to the Board of Directors that the audited financial statements be included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2005.

*The Audit Committee of the Board of Directors of RITA Medical Systems, Inc.:*

James Brands  
Thomas J. Dugan  
Wesley E. Johnson, Jr.

**FEES BILLED FOR SERVICES RENDERED BY PRINCIPAL ACCOUNTANT**

PricewaterhouseCoopers LLP ( PwC ) was engaged as our independent registered public accounting firm for the fiscal year ending December 31, 2004. On May 23, 2005, PwC resigned as our independent registered public accounting firm. On June 30, 2005, we engaged Stonefield Josephson, Inc. ( Stonefield ) to serve as our independent registered public accounting firm for the fiscal year ending December 31, 2005. The following table lists the aggregate fees and costs billed by Stonefield and PwC to us for professional services rendered for the fiscal years ended December 31, 2004 and December 31, 2005, respectively.

Fee Category	Year ended December 31,	
	2005	2004
Audit fees	\$ 490,027	\$ 816,777
Audit-related fees	21,007	415,155
Tax fees		
All other fees		
	<u>\$ 511,034</u>	<u>\$ 1,231,932</u>

*Audit fees.* Audit fees consist of fees billed for professional services rendered for the audit of our consolidated financial statements and review of the interim consolidated financial statements included in quarterly reports and services that are normally provided by our independent registered public accounting firm in connection with statutory and regulatory filings or engagements. Audit fees also include the audit of management's report on the effectiveness of the Company's internal control over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act of 2002.

*Audit-related fees.* Audit-related fees consists of fees billed for assurance and related services that are reasonably related to the performance of the audit or review of our consolidated financial statements and are not reported under Audit Fees. These services include employee benefit plan audits, attest services that are not required by statute or regulation, audits in connection with acquisitions and consultations concerning financial accounting and reporting standards.

**STOCK PERFORMANCE GRAPH**

The following graph compares the cumulative total shareholder return data for the Company's stock since December 31, 2000 to the cumulative return over such period of (i) the Nasdaq Stock Market (U.S.) Index and (ii) the Nasdaq Medical Equipment Index. The graph assumes that \$100 was invested on December 31, 2000 in the common stock of the Company and in each of the comparative indexes. The graph further assumes that such amount was initially invested in the common stock of the Company at a per share price of \$12.00 and reinvestment of any dividends. The stock price performance on the following graph is not necessarily indicative of future stock price performance.

**COMPARISON OF 5 YEAR CUMULATIVE RETURN\***  
 AMONG RITA MEDICAL SYSTEMS, INC., THE NASDAQ STOCK MARKET (U.S.) INDEX  
 AND THE NASDAQ MEDICAL EQUIPMENT INDEX

0  
 20  
 40  
 60  
 80  
 100  
 120  
 140  
 160  
 180  
 12/31/00  
 12/31/01  
 12/31/02  
 12/31/03  
 12/31/04  
 12/31/05

RITA MEDICAL SYSTEMS, INC.  
 NASDAQ STOCK MARKET (U.S.)  
 NASDAQ MEDICAL EQUIPMENT

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\* \$100 invested on 12/31/00 in stock market or index, including reinvestment of dividends. Fiscal year ended December 31.

	<u>12/31/00</u>	<u>12/31/01</u>	<b>Cumulative Total Return</b>		<u>12/31/04</u>	<u>12/31/05</u>
			<u>12/31/02</u>	<u>12/31/03</u>		
RITA MEDICAL SYSTEMS, INC.	70.83	55.58	42.08	37.08	32.25	46.00
NASDAQ STOCK MARKET (U.S.)	65.16	49.6	28.53	41.45	43.78	93.72
NASDAQ MEDICAL EQUIPMENT	100.63	111.27	91.42	133.95	156.01	168.11

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**Section 16 Beneficial Ownership Reporting Compliance**

Section 16(a) of the Exchange Act requires our directors, our executive officers and persons who own more than 10% of the common stock (collectively, Reporting Persons ) to file initial reports of ownership and changes in ownership of our common stock. Reporting Persons are required by SEC regulations to furnish us with copies of all Section 16(a) reports they file. To our knowledge, based solely on our review of the copies of such reports received or written representations from certain Reporting Persons that no other reports were required, we believe that during our fiscal year ended December 31, 2005, all Reporting Persons complied with all applicable filing requirements.

**Other Matters**

The Board knows of no other business that will be presented to the Annual Meeting. If any other business is properly brought before the Annual Meeting, proxies in the enclosed form will be voted in respect thereof as the proxy holders deem advisable. It is important that the proxies are returned promptly and that your shares are represented. Stockholders are urged to mark, date, execute and promptly return the accompanying proxy card in the enclosed envelope.

By Order of the Board of Directors,

/s/ Joseph DeVivo

Joseph DeVivo, President and Chief Executive Officer

Fremont, California  
April 28, 2006

**RITA MEDICAL SYSTEMS, INC.**

**2005 STOCK AND INCENTIVE PLAN, AS AMENDED**

**Adopted June 8, 2005**

**Amended \_\_\_\_\_, 2006**

1. **Purposes of the Plan.** The purposes of this 2005 Stock and Incentive Plan are to attract and retain the best available personnel for positions of substantial responsibility, to provide additional incentive to Employees and Consultants of the Company and its Subsidiaries and to promote the success of the Company's business. Options granted under the Plan may be Incentive Stock Options (as defined under Section 422 of the Code) or Nonstatutory Stock Options, as determined by the Administrator at the time of grant of an Option and subject to the applicable provisions of Section 422 of the Code and the regulations promulgated thereunder. Stock Awards (including Stock Grants, Stock Units, Stock Appreciation Rights and Stock Purchase Rights) and Cash Awards may also be granted under the Plan.

2. **Definitions.** As used herein, the following definitions shall apply:

(a) **Administrator** means the Board or any of its Committees appointed pursuant to Section 4 of the Plan.

(b) **Applicable Laws** means the legal requirements relating to the administration of stock option and restricted stock plans under applicable U.S. state corporate laws, U.S. federal and applicable state securities laws, the Code, any Nasdaq National Market or stock exchange rules or regulations and the applicable laws of any other country or jurisdiction where Options or Stock Awards are granted under the Plan, as such laws, rules, regulations and requirements shall be in place from time to time.

(c) **Award** means a Stock Award, a Cash Award or an Option granted in accordance with the terms of the Plan.

(d) **Award Agreement** means a Stock Award Agreement, Cash Award Agreement and/or Option Agreement, which may be in written or electronic format, in such form and with such terms and conditions as may be specified by the Administrator, evidencing the terms and conditions of an individual Award. Each Award Agreement is subject to the terms and conditions of the Plan.

(e) **Board** means the Board of Directors of the Company.

(f) **Cash Award** means a bonus opportunity awarded under Section 14 pursuant to which a Participant may become entitled to receive an amount based on the satisfaction of such performance criteria as are specified in the agreement or other documents evidencing the Award (the **Cash Award Agreement**).

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(g) **Change in Control** means any of the following, unless the Administrator provides otherwise:

(i) any merger or consolidation in which the Company shall not be the surviving entity (or survives only as a subsidiary of another entity whose stockholders did not own all or substantially all of the Common Stock in substantially the same proportions as immediately prior to such transaction),

(ii) the sale of all or substantially all of the Company's assets to any other person or entity (other than a wholly-owned subsidiary),

(iii) the acquisition of beneficial ownership of a controlling interest (including, without limitation, power to vote) the outstanding shares of Common Stock by any person or entity (including a group as defined by or under Section 13(d)(3) of the Exchange Act),

(iv) a contested election of Directors, as a result of which or in connection with which the persons who were Directors before such election or their nominees (the **Incumbent Directors**) cease to constitute a majority of the Board; provided however that if the election, or nomination for election by the Company's stockholders, of any new director was approved by a vote of at least fifty percent (50%) of the Incumbent Directors, such new Director shall be considered as an Incumbent Director, or

(v) any other event specified by the Board or a Committee, regardless of whether at the time an Award is granted or thereafter.

(h) **Code** means the Internal Revenue Code of 1986, as amended.

(i) **Committee** means one or more committees or subcommittees appointed by the Board of Directors to administer the Plan in accordance with Section 4 below.

(j) **Common Stock** means the Common Stock of the Company.

(k) **Company** means RITA Medical Systems, Inc., a Delaware corporation.

(l) **Consultant** means any person, including an advisor, who is engaged by the Company or any Parent or Subsidiary to render services and is compensated for such services, and any Director of the Company whether compensated for such services or not.

(m) **Continuous Service Status** means the absence of any interruption or termination of service as an Employee or Consultant. Continuous Service Status shall not be considered interrupted in the case of: (i) sick leave; (ii) military leave; (iii) any other leave of absence approved by the Administrator, provided that such leave is for a period of not more than 90 days, unless reemployment upon the expiration of such leave is guaranteed by contract or statute, or unless provided otherwise pursuant to Company policy adopted from time to time; or (iv) in the case of transfers between locations of the Company or between the Company, its Subsidiaries or their respective successors. For purposes of this Plan, a change in status from an

Employee to a Consultant or from a Consultant to an Employee will not constitute an interruption of Continuous Service Status.

(n) **Director** means a member of the Board of Directors of the Company.

(o) **Employee** means any person employed by the Company or any Parent or Subsidiary of the Company, with the status of employment determined based upon such minimum number of hours or periods worked as shall be determined by the Administrator in its discretion, subject to any requirements of the Code or the Applicable Laws. The payment by the Company of a director's fee to a Director shall not be sufficient to constitute employment of such Director by the Company.

(p) **Exchange Act** means the Securities Exchange Act of 1934, as amended.

(q) **Fair Market Value** means, as of any date, the Fair Market Value of the Common Stock as determined by the Administrator in good faith on such basis as it deems appropriate and applied consistently with respect to Participants. Whenever possible, the determination of Fair Market Value shall be based upon the closing price for the Shares as reported in the **Wall Street Journal** for the applicable date.

(r) **Incentive Stock Option** means an Option intended to qualify as an incentive stock option within the meaning of Section 422 of the Code, as designated in the applicable written Option Agreement.

(s) **Named Executive** means any individual who, on the last day of the Company's fiscal year, is the chief executive officer of the Company (or is acting in such capacity) or among the four most highly compensated officers of the Company (other than the chief executive officer). Such officer status shall be determined pursuant to the executive compensation disclosure rules under the Exchange Act.

(t) **Nonstatutory Stock Option** means an Option not intended to qualify as an Incentive Stock Option, as designated in the applicable written Option Agreement.

(u) **Officer** means a person who is an officer of the Company within the meaning of Section 16(a) of the Exchange Act and the rules and regulations promulgated thereunder.

(v) **Option** means a stock option granted pursuant to the Plan.

(w) **Option Agreement** means a written agreement between an Optionee and the Company reflecting the terms of an Option granted under the Plan and includes any documents attached to such Option Agreement, including, but not limited to, a notice of stock option grant and a form of exercise notice.

(x) **Optioned Stock** means the Common Stock subject to an Option.

(y) **Optionee** means an Employee or Consultant who receives an Option.

(z) **Parent** means a parent corporation, whether now or hereafter existing, as defined in Section 424(e) of the Code, or any successor provision.

(aa) **Participant** means any holder of one or more Options or Stock Awards, or the Shares issuable or issued upon exercise of such Awards, under the Plan.

(bb) **Plan** means this 2005 Stock and Incentive Plan.

(cc) **Qualifying Performance Criteria** means any one or more of the following performance criteria, either individually, alternatively or in any combination, applied to either the Company as a whole or to a business unit, Parent, Subsidiary or business segment, either individually, alternatively or in any combination, and measured either annually or cumulatively over a period of years, on an absolute basis or relative to a pre-established target, to previous years' results or to a designated comparison group, in each case as specified by the Committee in the Award: (i) cash flow; (ii) earnings (including gross margin, earnings before interest and taxes, earnings before taxes, and net earnings); (iii) earnings per share; (iv) growth in earnings or earnings per share; (v) stock price; (vi) return on equity or average stockholders equity; (vii) total stockholder return; (viii) return on capital; (ix) return on assets or net assets; (x) return on investment; (xi) revenue; (xii) income or net income; (xiii) operating income or net operating income; (xiv) operating profit or net operating profit; (xv) operating margin; (xvi) return on operating revenue; (xvii) market share; (xviii) contract awards or backlog; (xix) overhead or other expense reduction; (xx) growth in stockholder value relative to the moving average of the S&P 500 Index or a peer group index; (xxi) credit rating; (xxii) strategic plan development and implementation (including individual performance objectives that relate to achievement of the Company's or any business unit's strategic plan); (xxiii) improvement in workforce diversity, and (xxiv) any other similar criteria as may be determined by the Administrator. The Committee may appropriately adjust any evaluation of performance under a Qualifying Performance Criteria to exclude any of the following events that occurs during a performance period: (A) asset write-downs; (B) litigation or claim judgments or settlements; (C) the effect of changes in tax law, accounting principles or other such laws or provisions affecting reported results; (D) accruals for reorganization and restructuring programs; and (E) any gains or losses classified as extraordinary or as discontinued operations in the Company's financial statements.

(dd) **Reporting Person** means an Officer, Director, or greater than 10% stockholder of the Company within the meaning of Rule 16a-2 under the Exchange Act, who is required to file reports pursuant to Rule 16a-3 under the Exchange Act.

(ee) **Restricted Stock** means shares of Common Stock acquired pursuant to a grant of a Stock Award under Sections 11, 12 or 13 below.

(ff) **Rule 16b-3** means Rule 16b-3 promulgated under the Exchange Act, as the same may be amended from time to time, or any successor provision.

(gg) **Share** means a share of the Common Stock, as adjusted in accordance with Section 17 of the Plan.

(hh) **Stock Appreciation Right** means a right to receive cash and/or shares of Common Stock based on a change in the Fair Market Value of a specific number of shares of Common Stock granted under Section 13.

(ii) **Stock Award** means a Stock Grant, a Stock Unit, a Stock Appreciation Right or a Stock Purchase Right granted under Sections 11, 12 or 13 below or other similar awards granted under the Plan (including phantom stock rights).

(jj) **Stock Award Agreement** means a written agreement, the form(s) of which shall be approved from time to time by the Administrator, between the Company and a holder of a Stock Award evidencing the terms and conditions of an individual Stock Award grant. Each Stock Award Agreement shall be subject to the terms and conditions of the Plan.

(kk) **Stock Exchange** means any stock exchange or consolidated stock price reporting system on which prices for the Common Stock are quoted at any given time.

(ll) **Stock Grant** means the award of a certain number of shares of Common Stock granted under Section 11 below.

(mm) **Stock Purchase Right** means the right to purchase Common Stock pursuant to Section 12 below.

(nn) **Stock Unit** means a bookkeeping entry representing an amount equivalent to the Fair Market Value of one Share, payable in cash, property or Shares. Stock Units represent an unfunded and unsecured obligation of the Company, except as otherwise provided for by the Administrator.

(oo) **Subsidiary** means a subsidiary corporation, whether now or hereafter existing, as defined in Section 424(f) of the Code, or any successor provision.

(pp) **Ten Percent Holder** means a person who owns stock representing more than ten percent (10%) of the voting power of all classes of stock of the Company or any Parent or Subsidiary.

(qq) **2000 Stock Plan** means the 2000 Stock Plan, as amended, of the Company.

### 3. **Stock Subject to the Plan.**

(a) Subject to the provisions of Section 17 of the Plan, the maximum aggregate number of Shares that may be sold or issued under the Plan is 5,876,746 shares of Common Stock. This maximum number of shares includes:

(i) 500,000 Shares being reserved in connection with the April \_\_\_\_, 2006 amendment of the Stock Plan;

(ii) 639,468 Shares that are available for grant pursuant to awards that may be made under the Plan on or after March 10, 2006; and

(iii) up to 4,737,278 Shares reserved for issuance under the Plan or the 2000 Stock Plan that as of March 10, 2006 are subject to outstanding options granted under the Plan or the 2000 Stock Plan which Shares might be returned to the Plan if and to the extent the options to which they are subject terminate or expire or become unexercisable for any reason without having been exercised in full.

(b) If an Award should expire or become unexercisable for any reason without having been exercised in full or without the Shares subject thereto having been issued in full, the unpurchased or unissued Shares that were subject thereto shall, unless the Plan shall have been terminated, become available for future grant under the Plan. Any Shares of Common Stock which are retained by the Company upon exercise of an Award whether issued under the Plan or the 2000 Stock Plan in order to satisfy the exercise or purchase price for such Award or any withholding taxes due with respect to such exercise, purchase or issuance shall not continue to be available under the Plan. Shares issued under the Plan and later repurchased by the Company pursuant to any repurchase right which the Company may have shall not be available for future grant under the Plan.

(c) Notwithstanding anything to the contrary in the Plan and subject to the provisions of Section 17 of the Plan, the maximum aggregate number of Shares that may be granted under the Plan subject to Stock Grants, Stock Purchase Rights and Stock Units (or any other similar Award having an exercise or purchase price that is less than the Fair Market Value of the Common Stock measured as of the date of grant of the Award, such as phantom stock rights) is 400,000 Shares. Stock-settled Stock Appreciation Rights shall not be counted against this limit; provided however that the total number of Shares to which a Stock Appreciation Right applies (rather than the net number issued upon settlement) shall be deducted against the number of Shares set forth in Section 3(a) above upon settlement of such Award.

#### 4. **Administration of the Plan.**

(a) **General.** The Plan shall be administered by the Board or a Committee, or a combination thereof, as determined by the Board. The Plan may be administered by different administrative bodies with respect to different classes of Participants and, if permitted by the Applicable Laws, the Board may authorize one or more officers to grant Options, Stock Awards and Cash Awards under the Plan.

(b) **Administration With Respect to Reporting Persons.** With respect to Options, Stock Awards and Cash Awards granted to Reporting Persons and Named Executives, the Plan may (but need not) be administered so as to permit such Options, Stock Awards and Cash Awards to qualify for the exemption set forth in Rule 16b-3 and to qualify as performance-based compensation under Section 162(m) of the Code.

(c) **Committee Composition.** If a Committee has been appointed pursuant to this Section 4, such Committee shall continue to serve in its designated capacity until otherwise

directed by the Board. From time to time the Board may increase the size of any Committee and appoint additional members thereof, remove members (with or without cause) and appoint new members in substitution therefor, fill vacancies (however caused) and remove all members of a Committee and thereafter directly administer the Plan, all to the extent permitted by the Applicable Laws and, in the case of a Committee administering the Plan pursuant to Section 4(c) above, to the extent permitted or required by Rule 16b-3 and Section 162(m) of the Code.

(d) **Powers of the Administrator.** Subject to the provisions of the Plan and in the case of a Committee, the specific duties delegated by the Board to such Committee, the Administrator shall have the authority, in its discretion:

(i) to determine the Fair Market Value of the Common Stock, in accordance with Section 2(q) of the Plan;

(ii) to select the Consultants and Employees to whom Options, Stock Awards and Cash Awards or any combination thereof may from time to time be granted hereunder;

(iii) to determine whether and to what extent Options, Stock Awards and Cash Awards or any combination thereof are granted hereunder;

(iv) to determine the number of shares of Common Stock or amount of cash to be covered by each Award granted hereunder;

(v) to approve forms of agreement for use under the Plan;

(vi) to determine the terms and conditions, not inconsistent with the terms of the Plan, of any Award granted hereunder. Such terms and conditions include, but are not limited to, the exercise and/or purchase price (if applicable), the time or times when an Award may be exercised (which may or may not be based on performance criteria), the vesting schedule, any vesting and/or exercisability acceleration or waiver of forfeiture restrictions, the acceptable forms of consideration, the term, and any restriction or limitation regarding any Award or the Shares relating thereto, based in each case on such factors as the Administrator, in its sole discretion, shall determine and may be established at the time an Award is granted or thereafter;

(vii) to determine the terms and restrictions applicable to Stock Awards and the Restricted Stock purchased or issued on exercise or settlement of such Stock Awards;

(viii) to construe and interpret the terms of the Plan and Awards granted pursuant to the Plan;

(ix) in order to fulfill the purposes of the Plan and without amending the Plan, to modify grants of Options, Stock Awards or Cash Awards to Participants who are foreign nationals or employed outside of the United States in order to recognize differences in local law, tax policies or customs;



(x) to allow Participants to satisfy withholding tax amounts by electing to have the Company withhold from the Shares to be issued upon exercise of a Nonstatutory Stock Option or vesting of a Stock Award that number of Shares having a Fair Market Value equal to the amount required to be withheld. The Fair Market Value of the Shares to be withheld shall be determined in such manner and on such date that the Administrator shall determine or, in the absence of provision otherwise, on the date that the amount of tax to be withheld is to be determined. All elections by a Participant to have Shares withheld for this purpose shall be made in such form and under such conditions as the Administrator may provide;

(xi) to correct administrative errors;

(xii) to modify or amend each Award, including, but not limited to, the acceleration of vesting and/or exercisability, provided, however, that any such amendment is subject to Section 20 of the Plan and except as set forth in that Section, may not impair any outstanding Award unless agreed to in writing by the Participant;

(xiii) to authorize conversion or substitution under the Plan of any or all options, stock appreciation rights or stock awards held by service providers of an entity acquired by the Company (the **Conversion Awards** ). Any conversion or substitution shall be effective as of the close of the merger, acquisition or other transaction. The Conversion Awards may be Nonstatutory Stock Options or Incentive Stock Options, as determined by the Administrator, with respect to options granted by the acquired entity; provided, however, that with respect to the conversion of stock appreciation rights in the acquired entity, the Conversion Awards shall be Nonstatutory Stock Options. Unless otherwise determined by the Administrator at the time of conversion or substitution, all Conversion Awards shall have the same terms and conditions as Awards generally granted by the Company under the Plan;

(xiv) to authorize any person to execute on behalf of the Company any instrument required to effect the grant of an Award previously granted by the Administrator;

(xv) to impose such restrictions, conditions or limitations as it determines appropriate as to the timing and manner of any resales by a Participant or other subsequent transfers by the Participant of any Shares issued as a result of or under an Award, including without limitation, (A) restrictions under an insider trading policy and (B) restrictions as to the use of a specified brokerage firm for such resales or other transfers;

(xvi) to provide, either at the time an Award is granted or by subsequent action, that an Award shall contain as a term thereof, a right, either in tandem with the other rights under the Award or as an alternative thereto, of the Participant to receive, without payment to the Company, a number of Shares, cash or a combination thereof, the amount of which is determined by reference to the value of the Award; and

(xvii) to make all other determinations deemed necessary or advisable for administering the Plan and any Award granted hereunder.

(e) **Effect of Administrator's Decision.** All decisions, determinations and interpretations of the Administrator shall be final and binding on all holders of Options, Stock Awards or Cash Awards.

5. **Eligibility.**

(a) **Recipients of Grants.** Nonstatutory Stock Options and Stock Awards may be granted to Employees and Consultants. Incentive Stock Options and Cash Awards may be granted only to Employees. An Employee or Consultant who has been granted an Option, Stock Award or Cash Award may, if he or she is otherwise eligible, be granted additional Options, Stock Awards or Cash Awards.

(b) **Type of Option.** Each Option shall be designated in the Option Agreement as either an Incentive Stock Option or a Nonstatutory Stock Option.

(c) **\$100,000 Limitation.** Notwithstanding any designation under Section 5(b), to the extent that the aggregate Fair Market Value of Shares with respect to which Options designated as Incentive Stock Options are exercisable for the first time by any Optionee during any calendar year (under all plans of the Company or any Parent or Subsidiary) exceeds \$100,000, such excess Options shall be treated as Nonstatutory Stock Options. For purposes of this Section 5(c), Incentive Stock Options shall be taken into account in the order in which they were granted, and the Fair Market Value of the Shares subject to an Incentive Stock Option shall be determined as of the date of the grant of such Option.

(d) **Employment Relationship.** The Plan shall not confer upon the holder of any Award any right with respect to continuation of an employment or consulting relationship with the Company, nor shall it interfere in any way with such holder's right or the Company's right to terminate his or her employment or consulting relationship at any time, with or without cause.

6. **Term of Plan.** The Plan shall become effective upon its approval by the stockholders of the Company as described in Section 24 of the Plan. It shall continue in effect for a term of ten (10) years from the date the Plan is approved by the stockholders of the Company unless sooner terminated under Section 20 of the Plan.

7. **Term of Option.** The term of each Option shall be the term stated in the Option Agreement; provided, however, that the term shall be no more than ten years from the date of grant thereof or such shorter term as may be provided in the Option Agreement and provided further that, in the case of an Incentive Stock Option granted to an Optionee who, at the time the Option is granted, is a Ten Percent Holder, the term of the Option shall be five years from the date of grant thereof or such shorter term as may be provided in the Option Agreement.

8. **Limitation on Grants to Employees.** Subject to adjustment as provided in Section 17 below, the maximum number of Shares which may be subject to Options and Stock Awards granted to any one Employee under this Plan for any fiscal year of the Company shall be 1,000,000 Shares.

9. **Option Exercise Price and Consideration.**

(a) **Exercise Price.** The per Share exercise price for the Shares to be issued pursuant to exercise of an Option shall be such price as is determined by the Board and set forth in the Option Agreement, but shall be subject to the following:

(i) In the case of an Incentive Stock Option that is:

(A) granted to an Employee who, at the time of the grant of such Incentive Stock Option, is a Ten Percent Holder, the per Share exercise price shall be no less than 110% of the Fair Market Value per Share on the date of grant; or

(B) granted to any other Employee, the per Share exercise price shall be no less than 100% of the Fair Market Value per Share on the date of grant.

(ii) In the case of a Nonstatutory Stock Option the per Share exercise price shall be no less than 100% of the Fair Market Value per Share on the date of grant.

(iii) Notwithstanding the foregoing, Options may be granted with a per Share exercise price other than as required above pursuant to a merger or other corporate transaction.

(b) **No Option Repricings.** Other than in connection with a change in the Company's capitalization (as described in Section 17(a) of the Plan), the exercise price of an Option may not be reduced without stockholder approval.

(c) **Permissible Consideration.** The consideration to be paid for the Shares to be issued upon exercise of an Option, including the method of payment, shall be determined by the Administrator (and, in the case of an Incentive Stock Option, shall be determined at the time of grant) and may consist entirely of (1) cash, (2) check, (3) promissory note (subject to the provisions of Section 153 of the Delaware General Corporation Law), (4) cancellation of indebtedness, (5) other Shares that (x) in the case of Shares acquired upon exercise of an Option, have been owned by the Optionee for more than six months on the date of surrender or such other period as may be required to avoid a charge to the Company's earnings, and (y) have a Fair Market Value on the date of surrender equal to the aggregate exercise price of the Shares as to which such Option shall be exercised, (6) if as of the date of exercise of an Option the Company then is permitting optionees to engage in a same-day sale cashless-brokered exercise program involving one or more brokers, through such a program that complies with the Applicable Laws (including without limitation the requirements of Regulation T and other applicable regulations promulgated by the Federal Reserve Board) and that ensures prompt delivery to the Company of the amount required to pay the exercise price and any applicable withholding taxes, (7) provided that the Company's allowing the optionee to do so does not result in adverse accounting treatment to the Company relative to the treatment the Option would have if it did not include such provision either at the time of grant or while the Option remains outstanding, by the Company's withholding from the Shares subject to the Option that number of Shares having as of the date of exercise an aggregate fair market value equal to the aggregate exercise price for the

Shares being exercised, (8) any combination of the foregoing methods of payment, or (9) such other consideration and method of payment for the issuance of Shares to the extent permitted under the Applicable Laws. In making its determination as to the type of consideration to accept, the Administrator shall consider if acceptance of such consideration may be reasonably expected to benefit the Company and the Administrator may, in its sole discretion, refuse to accept a particular form of consideration at the time of any Option exercise.

10. **Exercise of Option.**

(a) **Procedure for Exercise; Rights as a Stockholder.** Any Option granted hereunder shall be exercisable at such times and under such conditions as determined by the Administrator, including performance criteria with respect to the Company and/or the Optionee, and as shall be permissible under the terms of the Plan. The Administrator shall have the discretion to determine whether and to what extent the vesting of Options shall be tolled during any unpaid leave of absence; provided, however, that in the absence of such determination, vesting of Options shall be tolled during any leave that is not a leave required to be provided to the Participant under Applicable Law. In the event of military leave, vesting shall toll during any unpaid portion of such leave, provided that, upon a Participant's returning from military leave (under conditions that would entitle him or her to protection upon such return under the Uniform Services Employment and Reemployment Rights Act), he or she shall be given vesting credit with respect to Options to the same extent as would have applied had the Participant continued to provide services to the Company throughout the leave on the same terms as he or she was providing services immediately prior to such leave.

An Option may not be exercised for a fraction of a Share.

An Option shall be deemed to be exercised when written (including electronic) notice of such exercise has been given to the Company in accordance with the terms of the Option by the person entitled to exercise the Option and the Company has received full payment for the Shares with respect to which the Option is exercised. Full payment may, as authorized by the Board, consist of any consideration and method of payment allowable under Section 9(c) of the Plan. Until the issuance (as evidenced by the appropriate entry on the books of the Company or of a duly authorized transfer agent of the Company) of the stock certificate evidencing such Shares, no right to vote or receive dividends or any other rights as a stockholder shall exist with respect to the Optioned Stock, notwithstanding the exercise of the Option. The Company shall issue (or cause to be issued) such stock certificate promptly upon exercise of the Option. No adjustment will be made for a dividend or other right for which the record date is prior to the date the stock certificate is issued, except as provided in Section 17 of the Plan.

Exercise of an Option in any manner shall result in a decrease in the number of Shares that thereafter may be available, both for purposes of the Plan and for sale under the Option, by the number of Shares as to which the Option is exercised.

(b) **Termination of Employment or Consulting Relationship.** Subject to Section 10(c) below, in the event of termination of an Optionee's Continuous Service Status, such Optionee may, but only within three months (or such other period of time as is determined

by the Administrator) after the date of such termination (but in no event later than the expiration date of the term of such Option as set forth in the Option Agreement), exercise his or her Option to the extent that the Optionee is vested in the Optioned Stock at the date of such termination. To the extent that the Optioned Stock is not vested at the date of such termination, or if the Optionee does not exercise such Option to the extent the Optioned Stock is vested within the time specified herein, the Option shall terminate. No termination shall be deemed to occur and this Section 10(b) shall not apply if (i) the Optionee is a Consultant who becomes an Employee, or (ii) the Optionee is an Employee who becomes a Consultant.

**(c) Disability of Optionee.**

(i) Notwithstanding Section 10(b) above, in the event of termination of an Optionee's Continuous Service Status as a result of his or her total and permanent disability (within the meaning of Section 22(e)(3) of the Code), such Optionee may, but only within six months from the date of such termination (but in no event later than the expiration date of the term of such Option as set forth in the Option Agreement), exercise the Option to the extent the Optioned Stock is vested at the date of such termination. To the extent that the Optioned Stock is not vested at the date of termination, or if the Optionee does not exercise such Option to the extent the Optioned Stock is vested within the time specified herein, the Option shall terminate.

(ii) In the event of termination of an Optionee's Continuous Service Status as a result of a disability which does not fall within the meaning of total and permanent disability (as set forth in Section 22(e)(3) of the Code), such Optionee may, but only within six months from the date of such termination (but in no event later than the expiration date of the term of such Option as set forth in the Option Agreement), exercise the Option to the extent the Optioned Stock is vested at the date of such termination. However, to the extent that such Optionee fails to exercise an Option which is an Incentive Stock Option (ISO) (within the meaning of Section 422 of the Code) within three months of the date of such termination, the Option will not qualify for ISO treatment under the Code. To the extent that the Optioned Stock is not vested at the date of termination, or if the Optionee does not exercise such Option to the extent the Optioned Stock is vested within six months from the date of termination, the Option shall terminate.

(d) **Death of Optionee.** In the event of the death of an Optionee during the period of Continuous Service Status since the date of grant of the Option, or within 30 days following termination of the Optionee's Continuous Service Status, the Option may be exercised, at any time within twelve months following the date of death (but in no event later than the expiration date of the term of such Option as set forth in the Option Agreement), by such Optionee's estate or by a person who acquired the right to exercise the Option by bequest or inheritance, but only to the extent the Optioned Stock is vested at the date of death or, if earlier, the date of termination of the Optionee's Continuous Status as an Employee or Consultant. To the extent that the Optioned Stock is not vested at the date of death or termination, as the case may be, or if the Optionee does not exercise such Option to the extent the Optioned Stock is vested within the time specified herein, the Option shall terminate.

(e) **Extension of Exercise Period.** The Administrator shall have full power and authority to extend the period of time for which an Option is to remain exercisable following termination of an Optionee's Continuous Service Status from the periods set forth in Sections 10(b), 10(c) and 10(d) above or in the Option Agreement to such greater time as the Board shall deem appropriate, provided that in no event shall such Option be exercisable later than the date of expiration of the term of such Option as set forth in the Option Agreement.

(f) **Rule 16b-3.** Options granted to Reporting Persons shall comply with Rule 16b-3 and shall contain such additional conditions or restrictions as may be required thereunder to qualify for the maximum exemption for Plan transactions.

11. **Stock Grants and Stock Unit Awards.** Each Stock Award Agreement reflecting the issuance of a Stock Grant or Stock Unit shall be in such form and shall contain such terms and conditions as the Administrator shall deem appropriate. The terms and conditions of such agreements may change from time to time, and the terms and conditions of separate agreements need not be identical, but each such agreement shall include (through incorporation of provisions hereof by reference in the agreement or otherwise) the substance of each of the following provisions:

(a) **Consideration.** A Stock Grant or Stock Unit may be awarded in consideration for such property or services as is permitted under Applicable Law, including for past services actually rendered to the Company or a Subsidiary for its benefit.

(b) **Vesting.** Shares of Common Stock awarded under an agreement reflecting a Stock Grant and a Stock Unit award may, but need not, be subject to a share repurchase option, forfeiture restriction or other conditions in favor of the Company in accordance with a vesting or lapse schedule to be determined by the Administrator.

(c) **Termination of Participant's Continuous Service.** In the event a Participant's Continuous Service terminates, the Company may reacquire any or all of the Shares held by the Participant which have not vested or which are otherwise subject to forfeiture or other conditions as of the date of termination under the terms of the agreement.

(d) **Transferability.** Rights to acquire Shares under a Stock Grant or a Stock Unit agreement shall be transferable by the Participant only by will or by the laws of descent and distribution.

12. **Stock Purchase Rights.**

(a) **Rights to Purchase.** Stock Purchase Rights may be issued either alone, in addition to, or in tandem with other Awards granted under the Plan and/or cash awards made outside of the Plan. After the Administrator determines that it will offer Stock Purchase Rights under the Plan, it shall advise the offeree in writing of the terms, conditions and restrictions related to the offer, including the number of Shares that such person shall be entitled to purchase, the price to be paid, and the time within which such person must accept such offer, which shall in no event exceed 30 days from the date upon which the Administrator made the determination to

grant the Stock Purchase Right. The purchase price of Shares subject to Stock Purchase Rights shall be as determined by the Administrator. The offer to purchase Shares subject to Stock Purchase Rights shall be accepted by execution of a Stock Award Agreement in the form determined by the Administrator.

(b) **Repurchase Option.** Unless the Administrator determines otherwise, the Stock Award Agreement shall grant the Company a repurchase option exercisable upon the voluntary or involuntary termination of the purchaser's employment with the Company for any reason (including death or disability). The purchase price for Shares repurchased pursuant to the Stock Award Agreement shall be the original purchase price paid by the purchaser or such other price as the Administrator determines and may be paid by cancellation of any indebtedness of the purchaser to the Company. The repurchase option shall lapse at such rate as the Administrator may determine.

(c) **Other Provisions.** The Stock Award Agreement shall contain such other terms, provisions and conditions not inconsistent with the Plan as may be determined by the Administrator in its sole discretion. In addition, the provisions of Stock Award Agreements need not be the same with respect to each purchaser.

(d) **Rights as a Stockholder.** Once the Stock Purchase Right is exercised, the purchaser shall have the rights equivalent to those of a stockholder, and shall be a stockholder when his or her purchase is entered upon the records of the duly authorized transfer agent of the Company. No adjustment will be made for a dividend or other right for which the record date is prior to the date the Stock Purchase Right is exercised, except as provided in Section 17 of the Plan.

### 13. **Stock Appreciation Rights.**

(a) **General.** Stock Appreciation Rights may be granted either alone, in addition to, or in tandem with other Awards granted under the Plan. The Administrator may grant Stock Appreciation Rights to eligible Participants subject to terms and conditions not inconsistent with this Plan and determined by the Administrator. The specific terms and conditions applicable to the Participant shall be provided for in the Stock Award Agreement. Stock Appreciation Rights shall be exercisable, in whole or in part, at such times as the Administrator shall specify in the Stock Award Agreement. Stock Appreciation Rights shall be subject to the final sentence of Section 3(c) above.

(b) **Exercise of Stock Appreciation Right.** Upon the exercise of a Stock Appreciation Right, in whole or in part, the Participant shall be entitled to a payment in an amount equal to the excess of the Fair Market Value on the date of exercise of a fixed number of Shares covered by the exercised portion of the Stock Appreciation Right, over the Fair Market Value on the grant date of the Shares covered by the exercised portion of the Stock Appreciation Right (or such other amount calculated with respect to Shares subject to the award as the Administrator may determine). The amount due to the Participant upon the exercise of a Stock Appreciation Right shall be paid in such form of consideration as determined by the Administrator and may be in cash, Shares or a combination thereof, over the period or periods, in

each case as specified in the Stock Award Agreement. A Stock Award Agreement may place limits on the amount that may be paid over any specified period or periods upon the exercise of a Stock Appreciation Right, on an aggregate basis or as to any Participant. A Stock Appreciation Right shall be considered exercised when the Company receives written notice of exercise in accordance with the terms of the Stock Award Agreement from the person entitled to exercise the Stock Appreciation Right.

(c) **Nonassignability of Stock Appreciation Rights.** Except as determined by the Board, no Stock Appreciation Right shall be assignable or otherwise transferable by the Participant except by will or by the laws of descent and distribution.

14. **Cash Awards.** Each Cash Award will confer upon the Participant the opportunity to earn a future payment tied to the level of achievement with respect to one or more performance criteria established for a performance period of not less than one (1) year.

(a) **Cash Award.** Each Cash Award shall contain provisions regarding (i) the target and maximum amount payable to the Participant as a Cash Award, (ii) the Qualifying Performance Criteria and level of achievement versus these criteria which shall determine the amount of such payment, (iii) the period as to which performance shall be measured for establishing the amount of any payment, (iv) the timing of any payment earned by virtue of performance, (v) restrictions on the alienation or transfer of the Cash Award prior to actual payment, (vi) forfeiture provisions, and (vii) such further terms and conditions, in each case not inconsistent with the Plan, as may be determined from time to time by the Administrator. The maximum amount payable as a Cash Award may be a multiple of the target amount payable, but the maximum amount payable pursuant to that portion of a Cash Award granted under this Plan for any fiscal year to any Participant shall not exceed U.S. \$500,000.

(b) **Performance Criteria.** The Administrator shall establish the Qualifying Performance Criteria and level of achievement versus these criteria which shall determine the target and the minimum and maximum amount payable under a Cash Award. The Administrator may specify the percentage of the target Cash Award that is intended to satisfy the requirements for performance-based compensation under Section 162(m) of the Code. Notwithstanding anything to the contrary herein, the performance criteria for any portion of a Cash Award that is intended to satisfy the requirements for performance-based compensation under Section 162(m) of the Code shall be a measure established by the Administrator based on one or more Qualifying Performance Criteria selected by the Administrator and specified in writing not later than 90 days after the commencement of the period of service to which the performance goals relates, provided that the outcome is substantially uncertain at that time (or in such other manner that complies with Section 162(m)).

(c) **Timing and Form of Payment.** The Administrator shall determine the timing of payment of any Cash Award. The Administrator may provide for or, subject to such terms and conditions as the Administrator may specify and Applicable Law, may permit a Participant to elect for the payment of any Cash Award to be deferred to a specified date or event. The Administrator may specify the form of payment of Cash Awards, which may be cash or other property, or may provide for a Participant to have the option for his or her Cash Award, or such



portion thereof as the Administrator may specify, to be paid in whole or in part in cash or other property.

(d) **Termination of Employment.** The Administrator shall have the discretion to determine the effect a Termination of Employment due to (i) disability, (ii) death or (iii) otherwise shall have on any Cash Award.

15. **Section 162(m) Compliance.** Any Stock Award (other than an Option or any other Stock Award having a purchase price equal to 100% of the Fair Market Value on the date such award is made) or Cash Award that is intended as qualified performance-based compensation within the meaning of Section 162(m) of the Code must vest or become exercisable contingent on the achievement of one or more Qualifying Performance Criteria. Notwithstanding anything to the contrary herein, the Committee shall have the discretion to determine the time and manner of compliance with Section 162(m) of the Code as required under applicable regulations and to conform the procedures related to the Award to the requirements of Section 162(m) and may reduce the number of Shares granted or amount of cash or other property to which a Participant may otherwise have been entitled with respect to an Award designed to qualify as performance-based compensation under Section 162(m).

16. **Taxes.**

(a) As a condition of the grant, vesting or exercise of an Option, Stock Award or Cash Award granted under the Plan or issuance of Shares under the Plan, the Participant (or in the case of the Participant's death, the person exercising the Option or Stock Award) shall make such arrangements as the Administrator may require for the satisfaction of any applicable federal, state, local or foreign withholding tax obligations that may arise in connection with such grant, vesting or exercise of the Option, Stock Award or Cash Award and the issuance of Shares. The Company shall not be required to issue any Shares or pay any cash under the Plan until such obligations are satisfied.

(b) In the case of an Employee and in the absence of any other arrangement, the Employee shall be deemed to have directed the Company to withhold or collect from his or her compensation an amount sufficient to satisfy such tax obligations from the next payroll payment otherwise payable after the date of an exercise of the Option or Stock Award.

(c) In the case of Participant other than an Employee (or in the case of an Employee where the next payroll payment is not sufficient to satisfy such tax obligations, with respect to any remaining tax obligations), in the absence of any other arrangement and to the extent permitted under the Applicable Laws, the Participant shall be deemed to have elected to have the Company withhold from the Shares to be issued upon exercise of the Option or Stock Award that number of Shares having a Fair Market Value determined as of the applicable Tax Date (as defined below) or that amount of cash to be paid pursuant to a Cash Award equal to the minimum statutory amounts required to be withheld. For purposes of this Section 16, the Fair Market Value of the Shares to be withheld shall be determined on the date that the amount of tax to be withheld is to be determined under the Applicable Laws (the Tax Date ).

(d) If permitted by the Administrator, in its discretion, a Participant may satisfy his or her tax withholding obligations upon exercise of an Option or Stock Award by surrendering to the Company Shares that (i) in the case of Shares previously acquired from the Company, have been owned by the Participant for more than six (6) months on the date of surrender, and (ii) have a Fair Market Value determined as of the applicable Tax Date equal to the minimum statutory amounts required to be withheld.

(e) Any election or deemed election by a Participant to have Shares or cash withheld to satisfy tax withholding obligations under Section 16(c) or (d) above shall be irrevocable as to the particular Shares or cash as to which the election is made and shall be subject to the consent or disapproval of the Administrator. Any election by a Participant under Section 16(d) above must be made on or prior to the applicable Tax Date.

(f) In the event an election to have Shares withheld is made by a Participant and the Tax Date is deferred under Section 83 of the Code because no election is filed under Section 83(b) of the Code, the Participant shall receive the full number of Shares with respect to which the Option or Stock Award is exercised but such Participant shall be unconditionally obligated to tender back to the Company the proper number of Shares on the applicable Tax Date.

17. **Adjustments Upon Changes in Capitalization, Merger or Certain Other Transactions.**

(a) **Changes in Capitalization.** Subject to any required action by the stockholders of the Company, the number of shares of Common Stock covered by each outstanding Option or Stock Award, the number of shares of Common Stock that have been authorized for issuance under the Plan but as to which no Options or Stock Awards have yet been granted or that have been returned to the Plan upon cancellation or expiration of an Option or Stock Award, and the number of shares set forth in Sections 3(c) and 8 above, as well as the price per share of Common Stock covered by each such outstanding Option or Stock Award, shall be proportionately adjusted for any increase or decrease in the number of issued shares of Common Stock resulting from a stock split, reverse stock split, stock dividend, combination, recapitalization or reclassification of the Common Stock, or any other increase or decrease in the number of issued shares of Common Stock effected without receipt of consideration by the Company; provided, however, that conversion of any convertible securities of the Company shall not be deemed to have been effected without receipt of consideration. Such adjustment shall be made by the Administrator, whose determination in that respect shall be final, binding and conclusive. Except as expressly provided herein, no issuance by the Company of shares of stock of any class, or securities convertible into shares of stock of any class, shall affect, and no adjustment by reason thereof shall be made with respect to, the number or price of shares of Common Stock subject to an Option or Stock Award.

(b) **Dissolution or Liquidation.** In the event of the proposed dissolution or liquidation of the Company, the Board shall notify the Participant at least 15 days prior to such proposed action. To the extent it has not been previously exercised, the Option or Stock Award

will terminate immediately prior to the consummation of such proposed action unless otherwise determined by the Administrator.

(c) **Change in Control.** In the event there is a Change in Control of the Company, as determined by the Board or a Committee, the Board or Committee may, in its discretion, (i) provide for the assumption or substitution of, or adjustment to, each outstanding Award; (ii) accelerate the vesting of Options and terminate any restrictions on Cash Awards or Stock Awards; and/or (iii) provide for termination of Awards as a result of the Change in Control on such terms and conditions as it deems appropriate, including providing for the cancellation of Awards for a cash payment to the Participant. For purposes of this Section 17(c), an Option or a Stock Award shall be considered assumed, without limitation, if, at the time of issuance of the stock or other consideration upon such merger or sale of assets, each holder of an Option or a Stock Award would be entitled to receive upon exercise of the Option or Stock Award the same number and kind of shares of stock or the same amount of property, cash or securities as such holder would have been entitled to receive upon the occurrence of such transaction if the holder had been, immediately prior to such transaction, the holder of the number of Shares of Common Stock covered by the Option or the Stock Award at such time (after giving effect to any adjustments in the number of Shares covered by the Option or Stock Award as provided for in this Section 17).

(d) **Certain Distributions.** In the event of any distribution to the Company's stockholders of securities of any other entity or other assets (other than dividends payable in cash or stock of the Company) without receipt of consideration by the Company, the Administrator may, in its discretion, appropriately adjust the price per share of Common Stock covered by each outstanding Option or Stock Award to reflect the effect of such distribution.

18. **Non-Transferability of Awards.** Except as set forth in this Section 18, Awards may not be sold, pledged, assigned, hypothecated, transferred or disposed of in any manner other than by will or by the laws of descent or distribution; provided however that Awards may be transferred by instrument to an inter vivos or testamentary trust in which the Awards are to be passed to beneficiaries upon the death of the trustor (settlor) or by gift or pursuant to domestic relations orders to Immediate Family Members (as defined below) of the Participant. Immediate Family means any child, stepchild, grandchild, parent, stepparent, grandparent, spouse, former spouse, sibling, niece, nephew, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law (including adoptive relationships), a trust in which these persons have more than fifty percent of the beneficial interest, a foundation in which these persons (or the Participant) control the management of assets, and any other entity in which these persons (or the Participant) own more than fifty percent of the voting interests. The designation of a beneficiary by a Participant will not constitute a transfer. An Option or Stock Award may be exercised, during the lifetime of the holder of an Option or Stock Award, only by such holder or a transferee permitted by this Section 18.

19. **Time of Granting Awards.** The date of grant of an Award shall, for all purposes, be the date on which the Administrator makes the determination granting such Award, or such other date as is determined by the Board; provided, however, that in the case of any Incentive Stock Option, the grant date shall be the later of the date on which the Administrator makes the

determination granting such Incentive Stock Option or the date of commencement of the Optionee's employment relationship with the Company. Notice of the determination shall be given to each Employee or Consultant to whom an Award is so granted within a reasonable time after the date of such grant.

20. **Amendment and Termination of the Plan.**

(a) **Authority to Amend or Terminate.** The Board may at any time amend, alter, suspend or discontinue the Plan, but no amendment, alteration, suspension or discontinuation shall be made that would impair the rights of any Optionee or holder of Stock Awards or Cash Awards under any grant theretofore made, without his or her consent. In addition, to the extent necessary and desirable to comply with the Applicable Laws, the Company shall obtain stockholder approval of any Plan amendment in such a manner and to such a degree as required. In addition, unless approved by the stockholders of the Company, no amendment shall be made that would result in a repricing of Options by (x) reducing the exercise price of outstanding Options or (y) canceling an outstanding Option held by a Participant and re-granting to the Participant a new Option with a lower exercise price, in either case other than in connection with a change in the Company's capitalization pursuant to Section 17(a) of the Plan.

(b) **Effect of Amendment or Termination.** No amendment or termination of the Plan shall adversely affect Options, Stock Awards or Cash Awards already granted, unless mutually agreed otherwise between the Optionee or holder of Stock Awards or Cash Awards and the Board, which agreement must be in writing and signed by the Optionee or holder of Stock Awards or Cash Awards and the Company.

21. **Conditions upon Issuance of Shares.** Shares shall not be issued pursuant to the exercise of an Option or Stock Award unless the exercise of such Option or Stock Award and the issuance and delivery of such Shares pursuant thereto shall comply with all relevant provisions of law, including, without limitation, the Securities Act of 1933, as amended, the Exchange Act, the rules and regulations promulgated thereunder, and the requirements of any Stock Exchange. Notwithstanding any other provision of the Plan or any agreement entered into by the Company pursuant to the Plan, the Company shall not be obligated, and shall have no liability for failure, to issue or deliver any Shares under the Plan unless such issuance or delivery would comply with the Applicable Laws, with such compliance determined by the Company in consultation with its legal counsel.

As a condition to the exercise of an Option or Stock Award, the Company may require the person exercising such Award to represent and warrant at the time of any such exercise that the Shares are being purchased only for investment and without any present intention to sell or distribute such Shares if, in the opinion of counsel for the Company, such a representation is required by law.

22. **Reservation of Shares.** The Company, during the term of this Plan, will at all times reserve and keep available such number of Shares as shall be sufficient to satisfy the requirements of the Plan. The inability of the Company to obtain authority from any regulatory body having jurisdiction, which authority is deemed by the Company's counsel to be necessary to

the lawful issuance and sale of any Shares hereunder, shall relieve the Company of any liability in respect of the failure to issue or sell such Shares as to which such requisite authority shall not have been obtained.

23. **Agreements.** Options, Stock Awards and Cash Awards shall be evidenced by written Option Agreements, Stock Award Agreements and Cash Award Agreements, respectively, in such form(s) as the Administrator shall approve from time to time.

24. **Stockholder Approval.** If required by Applicable Laws, continuance of the Plan shall be subject to approval by the stockholders of the Company within twelve months before or after the date the Plan is adopted. Such stockholder approval shall be obtained in the degree and manner required under the Applicable Laws. All Options, Stock Awards and Cash Awards issued under the Plan shall become void in the event such approval is not obtained.

25. **Governing Law.** The Plan and all determinations made and actions taken pursuant hereto shall be governed by the substantive laws, but not the choice of law rules, of the state of Delaware.

**RITA MEDICAL SYSTEMS, INC.**

**PROXY SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS**

The undersigned hereby appoints Joseph DeVivo and Michael Angel, and each of them individually, each with full power of substitution, as attorney, agent and proxy to represent the undersigned at the 2006 Annual Meeting of Stockholders (the Annual Meeting ) of RITA Medical Systems, Inc. (the Company ) to be held at its corporate headquarters located at 46421 Landing Parkway, Fremont, CA 94538 at 9:00 a.m. local time, on Wednesday, June 7, 2006, or at any adjournment thereof, with all power which the undersigned would possess if personally present, and to vote all shares of stock of the Company which the undersigned may be entitled to vote at said Annual Meeting in the manner set forth below. The Board of Directors unanimously recommends your vote FOR all matters set forth below.

1. ELECTION OF DIRECTORS:

Nominees: Joseph DeVivo  
Randy Lindholm

- FOR Joseph DeVivo  WITHHOLD AUTHORITY
- FOR Randy Lindholm  WITHHOLD AUTHORITY

2. AMENDMENT to the 2005 Stock and Incentive Plan to increase the number of shares of common stock issuable under the plan by an additional 500,000 shares, to an aggregate of 5,876,746 shares.

- FOR  AGAINST  ABSTAIN

3. RATIFICATION of the selection Stonefield Josephson, Inc. as our independent registered public accounting firm for the fiscal year ending December 31, 2006.

- FOR  AGAINST  ABSTAIN

4. IN THEIR DISCRETION, ON SUCH OTHER MATTERS AS MAY PROPERLY COME BEFORE THE MEETING AND ANY ADJOURNMENT(S) THEREOF. (continued and to be signed on reverse side)

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(continued from other side)

THIS PROXY WHEN PROPERLY EXECUTED WILL BE VOTED IN THE MANNER DIRECTED HEREIN BY THE UNDERSIGNED STOCKHOLDER. IF NO DIRECTION IS MADE, THIS PROXY WILL BE VOTED FOR THE ELECTION OF ALL NOMINEES FOR DIRECTOR NAMED IN PROPOSAL (1) AND FOR PROPOSALS (2) AND (3) AS DESCRIBED HEREIN, AND WILL CONFER THE AUTHORITY SET FORTH IN PARAGRAPH 4.

Receipt is hereby acknowledged of the Notice of Meeting and Proxy Statement dated April 28, 2006, as well as a copy of the Company's Annual Report for the fiscal year ended December 31, 2005.

Dated: \_\_\_\_\_, 2006

\_\_\_\_\_

\_\_\_\_\_

(signature of stockholder)

Please sign your name exactly as it appears hereon. When signing as attorney, executor, administrator, trustee or guardian, please give title. Each joint owner is requested to sign. If a corporation, partnership or other entity, please sign by an authorized officer or partner.

Whether or not you plan to attend the Annual Meeting, please complete, date, sign and return this proxy in the envelope provided.