

UNITED STATES  
 SECURITIES AND EXCHANGE COMMISSION  
 WASHINGTON, DC 20549

FORM 10-Q

(MARK ONE)

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

FOR THE QUARTERLY PERIOD ENDED: JUNE 30, 2000

OR

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

FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_

COMMISSION FILE NUMBER: 0-24531

COSTAR GROUP, INC.

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE  
 (STATE OR OTHER JURISDICTION OF  
 INCORPORATION OR ORGANIZATION)

52-2091509  
 (IRS EMPLOYER  
 IDENTIFICATION NUMBER)

2 BETHESDA METRO CENTER  
 BETHESDA, MD 20814  
 (301) 215-8300

(ADDRESS, INCLUDING ZIP CODE, AND TELEPHONE NUMBER, INCLUDING AREA CODE, OF  
 REGISTRANT'S PRINCIPAL EXECUTIVE OFFICES)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  - No

As of July 2, 2000, there were 15,401,567 shares outstanding of the Registrant's Common Stock, par value \$.01.

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## PART 1 FINANCIAL INFORMATION

## ITEM 1 FINANCIAL STATEMENTS

CoStar Group, Inc.  
 Condensed Consolidated Statements of Operations  
 (in thousands, except per share data)  
 (unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2000	1999	2000	1999
Revenues	\$ 14,572	\$ 7,178	\$ 25,944	\$ 13,305
Cost of revenues	7,730	3,068	13,707	5,662
Gross margin	6,842	4,110	12,237	7,643
Operating expenses:				
Selling and marketing	11,168	3,923	19,570	7,006
Software development	1,004	309	1,722	549
General and administrative	6,660	2,572	12,081	4,508
Purchase amortization	2,739	548	4,476	1,048
Acquired in-process development	-	-	5,812	-
	21,571	7,352	43,661	13,111
Loss from operations	(14,729)	(3,242)	(31,424)	(5,468)
Loss on disposal of assets	(182)	-	(182)	-
Other income, net	933	616	1,959	678
Net loss before income taxes	(13,978)	(2,626)	(29,647)	(4,790)
Income tax benefit	845	-	1,410	-
Net loss	\$ (13,133)	\$ (2,626)	\$ (28,237)	\$ (4,790)
Basic and diluted net loss per share	\$ (0.85)	\$ (0.23)	\$ (1.91)	\$ (0.45)
Weighted average common shares	15,391	11,510	14,822	10,572

See accompanying notes.

CoStar Group, Inc.  
Condensed Consolidated Balance Sheets  
(in thousands)

	June 30, 2000	December 31, 1999
-----		
ASSETS	(unaudited)	
Current assets:		
Cash and cash equivalents	\$ 64,258	\$ 94,074
Accounts receivable, less allowance for doubtful accounts of \$1,482 and \$756 as of June 30, 2000 and December 31, 1999	7,612	2,841
Prepaid expenses and other current assets	1,660	2,458
-----		
Total current assets	73,530	99,373
Property and equipment	20,517	8,259
Accumulated depreciation	(3,371)	(2,377)
-----		
	17,146	5,882
Intangible and other assets	90,292	31,222
Deposits	587	428
-----		
Total assets	\$181,555	\$136,905
=====		
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	\$ 13,710	\$ 7,585
Deferred revenue	8,503	2,635
-----		
Total current liabilities	22,213	10,220
Long term liabilities	1,906	-
Deferred taxes	11,100	6,988
Stockholders' equity	146,336	119,697
-----		
Total liabilities and stockholders' equity	\$181,555	\$136,905
=====		

See accompanying notes.

CoStar Group, Inc.  
Condensed Consolidated Statements of Cash Flows  
(in thousands)  
(unaudited)

	For the Six Months Ended June 30,	
	----- 2000	1999 -----
Operating activities:		
Net loss	\$ (28,237)	\$ (4,790)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation	994	480
Amortization	6,835	1,732
Acquired in-process development	5,812	-
Loss on disposal of assets	182	-
Provision for losses on accounts receivable	726	274
Income tax benefit	(1,410)	-
Non-cash charges	-	9
Changes in operating assets and liabilities	589	411
	-----	-----
Net cash used in operating activities	(14,509)	(1,884)
Investing activities:		
Net purchases of property and equipment	(8,391)	(2,100)
Intangible and other assets	(2,976)	( 677)
Acquisitions (net of acquired cash)	(2,407)	(9,993)
	-----	-----
Net cash used in investing activities	(13,774)	(12,770)
Financing activities:		
Payment of long term liability	(2,625)	-
Net proceeds from exercise of stock options	1,092	-
Net proceeds from public offering	-	97,411
	-----	-----
Net cash (used in) provided by financing activities	(1,533)	97,411
Net (decrease)/increase in cash and cash equivalents	(29,816)	82,757
Cash and cash equivalents at beginning of period	94,074	19,667
	-----	-----
Cash and cash equivalents at end of period	\$ 64,258	\$102,424
	=====	=====

See accompanying notes.

COSTAR GROUP, INC.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION

CoStar Group, Inc. (the "Company") has created a comprehensive, proprietary, national database of commercial real estate information for metropolitan areas throughout the United States. Based on its unique database, the Company provides information to the commercial real estate and related business community and operates within one reportable business segment. The information is distributed to its clients under license agreements, which are typically one to three years in duration.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

CoStar Group, Inc. is a Delaware corporation and was incorporated in February 1998 to succeed its predecessors, Realty Information Group L.P. ("RIGLP") and OLD RIG, Inc. ("RIGINC"). RIGLP was an operating entity, while RIGINC was a shell holding entity. In connection with the Company's Initial Public Offering on July 1, 1998 ("the Offering"), RIGLP and RIGINC merged with the Company pursuant to the RIG Contribution Agreement dated March 5, 1998. The limited partners of RIGLP (other than RIGINC) and all of the stockholders of RIGINC received 3.03 shares of Common Stock of the Company per each limited partnership unit or share of common stock exchanged, for a total of 5,754,017 shares. As a result of the reorganization of these entities, the Company owned (directly or indirectly) all of the capital stock of RIGINC and all the equity of RIGLP.

The merger has been accounted for as a reorganization of entities under common control similar to a pooling of interests. Following the merger, each shareholder of the Company maintained their exact same ownership of the operating entity, RIGLP, as before the merger. The transfer of assets and liabilities of RIGLP and RIGINC have been recorded at the historical carrying values. The financial statements are presented as if the Company was in existence throughout all periods presented, as one operating entity. All share amounts have been restated to reflect the conversion of partnership units to common stock of the Company. On January 1, 1999, RIGLP and RIGINC were merged into a newly formed corporation, CoStar Realty Information, Inc. ("CoStar Realty"), a wholly owned subsidiary of the Company.

Additionally, the consolidated financial statements of the Company include the accounts of New Market Systems ("NMS") acquired on March 1, 1997, C Data Services, Inc. ("CDS") acquired on August 14, 1998, LeaseTrend, Inc. ("LeaseTrend") acquired on January 8, 1999, Jamison Research, Inc. ("Jamison") acquired on January 22, 1999, ARES Development Group, LLC ("ARES") acquired on September 15, 1999, and COMPS.COM, Inc. ("Comps") acquired on February 10, 2000. CDS was merged into CoStar Realty on January 1, 1999, and LeaseTrend and Jamison were merged into CoStar Realty on December 31, 1999.

CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its subsidiaries after elimination of all significant intercompany transactions.

USE OF ESTIMATES

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

RECLASSIFICATIONS

Certain previously reported amounts have been reclassified to conform to the Company's current presentation.

## 3. ACQUISITIONS

On August 14, 1998, the Company acquired Houston-based commercial real estate information provider, C Data Services, Inc. CDS was acquired in a transaction in which the former stockholders of CDS received 93,530 shares of common stock of the Company and approximately \$9,000 in cash. The transaction was accounted for as a purchase and the consideration was valued for accounting purposes at approximately \$617,000 including acquisition expenses.

On January 8, 1999, the Company acquired all of the common stock of LeaseTrend, Inc., a Cincinnati based provider of commercial real estate information, for \$4,500,000 in cash and 566,671 shares of the Company's common stock. The transaction was accounted for as a purchase and the consideration was valued for accounting purposes at approximately \$9,200,000 including acquisition expenses.

On January 22, 1999, the Company acquired all of the common stock of Jamison Research, Inc., an Atlanta based provider of commercial real estate information, for \$5,284,000 in cash and 446,637 shares of the Company's common stock. The transaction was accounted for as a purchase and the consideration was valued for accounting purposes at approximately \$10,300,000 including acquisition expenses.

On September 15, 1999, the Company acquired all of the membership interests of ARES Development Group, LLC, Los Angeles based developers and distributors of ARES for ACT!, for \$250,000 in cash and 33,208 shares of the Company's common stock. The transaction was accounted for as a purchase and the consideration was valued for accounting purposes at approximately \$1,265,000 including acquisition expenses. In addition, the acquisition agreement provides for \$1,000,000 of additional consideration (in a combination of cash and stock) that may be paid by the Company upon the achievement of certain operating goals by the members of ARES. In February 2000, the Company issued 2,140 shares of its common stock and paid \$437,500 in cash to the members of ARES for the achievement of the first operating goal by the members of ARES.

On February 10, 2000, the Company completed the acquisition of Comps under a merger agreement, dated as of November 3, 1999, among the Company, Comps and Acq Sub, Inc. ("Acq Sub"), a wholly owned subsidiary of the Company. Comps' primary asset is a database of commercial real estate sales information. In connection with the transaction, Comps was merged with and into Acq Sub, which was the surviving corporation in the merger. Immediately after the merger, Acq Sub changed its name to Comps, Inc. The aggregate consideration included \$49,015,905 in cash paid to former holders of Comps common stock (excluding cash paid for fractional shares), and 2,258,738 shares of the Company's common stock (including shares issued to former warrant holders of Comps). The transaction was accounted for as a purchase and the consideration was valued for accounting purposes at approximately \$101,379,000 including acquisition expenses. The purchase price has been allocated on a preliminary basis to the assets and liabilities acquired based on the estimated fair values of the assets acquired and liabilities assumed.

The operations of all acquired businesses were included in the Company's statement of operations after the respective date of acquisitions. Except for the portion of the purchase price of acquisitions acquired with cash, these transactions have been excluded from the statements of cash flows.

The Company's unaudited pro forma condensed consolidated statements of operations for the six month periods ended June 30, 2000 and 1999, assuming the acquisition of LeaseTrend, Jamison, ARES and Comps had been consummated as of January 1 of each period, is summarized as follows (in thousands, except per share data):

	For the Six Month Period Ended June 30,	
	2000	1999
	-----	-----
Revenues	\$ 27,619	\$ 13,617
	-----	-----
Net loss	\$(33,053)	\$( 4,934)
	=====	=====
Weighted average shares	15,331	10,652
	=====	=====
Net loss per share - basic and diluted	\$ (2.16)	\$ (0.46)
	=====	=====

## 4. INTANGIBLE AND OTHER ASSETS

Intangible and other assets consists of the following (in thousands):

	June 30, 2000	December 31, 1999
	-----	-----
Capitalized product development costs	\$ 1,489	\$ 1,435
Accumulated amortization	(760)	(617)
	-----	-----
	729	818
	-----	-----
Building photography	4,000	3,118
Acquired technology	19,708	3,552
Customer base	31,600	19,347
Tradename	4,198	-
Goodwill	42,256	9,894
Accumulated amortization	(12,199)	(5,507)
	-----	-----
	89,563	30,404
	-----	-----
Intangible and other assets	\$90,292	\$ 31,222
	=====	=====

## ITEM 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements, which involve risks and uncertainties. Our actual results could differ materially from those in such forward-looking statements as a result of certain factors, including those set forth in the Company's Annual Report on Form 10-K for the year ended December 31, 1999, the Company's registration on Form S-3 filed June 16, 2000, and the Company's other filings with the Securities and Exchange Commission. The following discussion should be read in conjunction with the Company's filings with the Securities and Exchange Commission and the unaudited condensed consolidated financial statements included herein.

### OVERVIEW

The Company is the leading provider of information services to the U.S. commercial real estate industry. We are creating a digital marketplace where the members of the commercial real estate and related business community can continuously interact and facilitate transactions by efficiently exchanging accurate and standardized information. Our wide array of digital service offerings includes a leasing marketplace, a selling marketplace, comparable sales information, decision support, tenant information, property marketing, and industry news. Substantially all of our current services are digitally delivered over the Internet.

We completed our initial public offering in July 1998 and received net proceeds of approximately \$22.7 million. We primarily used those net proceeds to fund the geographic and service expansion of our business, including three strategic acquisitions, and to expand our sales and marketing organization. In May 1999, we completed a follow-on public offering and received net proceeds of approximately \$97.4 million. We used a portion of those net proceeds to fund the acquisition of Comps, and we expect to use the remainder of the proceeds primarily for development and distribution of new services, expansion of all existing services across our current markets, geographic expansion in the U.S. and international markets, strategic acquisitions and working capital and general corporate purposes.

From 1994 through June 2000, we expanded the geographical coverage of our existing services and developed new services. In addition to internal growth, this expansion included the acquisitions of Chicago ReSource, Inc. in Chicago in 1996 and New Market Systems, Inc. in San Francisco in 1997. In August 1998, we expanded into the Houston region through the acquisition of Houston-based real estate information provider C Data Services, Inc. In January 1999, we expanded further into the Midwest and Florida by acquiring LeaseTrend, and into Atlanta and Dallas/Fort Worth by acquiring Jamison. In September 1999, we acquired ARES, a Los Angeles based developer and distributor of ARES for ACT!. In February 2000, we acquired Comps.

We consider regions that have had ongoing operations for at least 18 months to be established, and we currently generate positive cash flow from our operations in established regions. As of June 30, 2000, the following regions are those that have been in operation for more than 18 months and that we consider to be established: Washington, New York, Los Angeles, Chicago, San Francisco, Philadelphia, Boston and Houston. These regions provide us with substantial cash flow, which we reinvest into the business. Since our inception, the development of our business has required substantial investments for the expansion of services and the establishment of operating regions, which has resulted in substantial net losses on an overall basis.

The incremental cost of introducing new services in an established region in the future may reduce the profitability of a region or cause it to incur losses. We expect continued development and distribution of new services, expansion of all existing services across current markets and geographic expansion in the United States and international markets. Therefore, while we expect operations in existing established regions to remain profitable and provide substantial funding, we expect our overall expansion activities to generate significant losses and negative cash flow from operations during the next 18 months.

Although our services are expanding rapidly, our CoStar Property, CoStar Tenant and CoStar COMPS services currently generate the largest portion of our revenue. The CoStar Property, CoStar Tenant and CoStar COMPS contracts range from terms of one to three years and generally renew automatically. Upon renewal, many of the contract rates increase automatically in accordance with contract provisions or as a result of renegotiations. To encourage clients to use our services regularly, we generally charge fixed amounts rather than fees based on actual system usage. We charge our clients based on the number of sites, organization size, the company's business focus, and the number of services to which a client subscribes. Our contract renewal rate currently exceeds 90% on an annual basis. Our clients pay contract fees on an annual, quarterly, or monthly basis. We recognize this revenue over the life of the

contract on a straight-line basis beginning with the installation or renewal date. Annual and quarterly advance payments result in deferred revenue, substantially reducing the working capital requirements generated by the growth in our accounts receivable.

THREE MONTHS ENDED JUNE 30, 1999 COMPARED TO  
THREE MONTHS ENDED JUNE 30, 2000

**REVENUES.** Revenues increased 103% from \$7,178,000 for the three months ended June 30, 1999 to \$14,572,000 for the three months ended June 30, 2000. The increase resulted primarily from growth in the Company's client base in established regions, expansion of emerging regions entered during 1999 and revenues from Comps. Our Comps Division contributed \$4.3 million to revenues for the three months ended June 30, 2000.

**GROSS MARGINS.** Gross margins increased 66% from \$4,110,000 for the three months ended June 30, 1999 to \$6,842,000 for the three months ended June 30, 2000, while gross margin percentages were 57% and 47% of revenue, respectively. The increase in gross margins resulted principally from significant revenue growth from established regions. The decline in gross margin percentages resulted primarily from investments in research for the expansion in both emerging and acquired regions and from lower gross margins in the recently acquired Comps business. Furthermore, cost of revenues for the three months ended June 30, 2000 includes purchase price amortization from the LeaseTrend, Jamison, ARES and Comps acquisitions of approximately \$1,277,000 compared to approximately \$187,000 for the same period in 1999.

**SELLING AND MARKETING EXPENSES.** Selling and marketing expenses increased 185% from \$3,923,000 for the three months ended June 30, 1999 to \$11,168,000 for the three months ended June 30, 2000. Selling and marketing expenses increased primarily as a result of the continued expansion of the sales force and marketing efforts required for growth, particularly in emerging regions, and for the marketing surrounding the launch of our CoStar Exchange product.

**SOFTWARE DEVELOPMENT.** Software development expenses increased 225% from \$309,000 for three months ended June 30, 1999 to \$1,004,000 for the three months ended June 30, 2000 reflecting development costs for the increased number of products we now support including CoStar COMPS and CoStar Exchange.

**GENERAL AND ADMINISTRATIVE EXPENSES.** General and administrative expenses increased 159% from \$2,572,000 for the three months ended June 30, 1999 to \$6,660,000 for the three months ended June 30, 2000. General and administrative expenses primarily increased due to the hiring of new employees to support the expanding scope of our operations and client base and also the increase in employees due to Comps.

**PURCHASE AMORTIZATION.** Purchase amortization increased 400% from \$548,000 for the three months ended June 30, 1999 to \$2,739,000 for the three months ended June 30, 2000. Purchase amortization increased primarily due to the acquisition of Comps.

**OTHER INCOME, NET.** Interest and other income increased from \$616,000 for the three months ended June 30, 1999 to \$933,000 for the three months ended June 30, 2000. This increase was a direct result of interest earned on the proceeds from the follow-on public offering.

**INCOME TAX BENEFIT.** An income tax benefit of \$845,000 for the three months ended June 30, 2000 is a result of the impact of the reversal of the deferred tax liability in connection with the amortization of identified intangible assets established during recent acquisitions.

SIX MONTHS ENDED JUNE 30, 1999 COMPARED TO  
SIX MONTHS ENDED JUNE 30, 2000

**REVENUES.** Revenues increased 95% from \$13,305,000 for the six months ended June 30, 1999 to \$25,944,000 for the six months ended June 30, 2000. The increase resulted primarily from growth in the Company's client base in established regions, expansion of emerging regions entered during 1999 and revenues from Comps. Our Comps Division contributed \$6.2 million to revenues for the six months ended June 30, 2000.

**GROSS MARGINS.** Gross margins increased 60% from \$7,643,000 for the six months ended June 30, 1999 to \$12,237,000 for the six months ended June 30, 2000, while gross margin percentages were 57% and 47% of revenue, respectively. The increase in gross margins resulted principally from significant revenue growth from established regions. The decline in gross margin percentages resulted primarily from investments in research for the expansion in both emerging and acquired regions and from lower gross margins in the recently acquired Comps business. Furthermore, cost of revenues for the six months ended June 30, 2000 includes purchase price amortization from the LeaseTrend, Jamison, ARES and Comps acquisitions of approximately \$2,121,000 compared to approximately \$390,000 for the same period in 1999.

**SELLING AND MARKETING EXPENSES.** Selling and marketing expenses increased 179% from \$7,006,000 for the six months ended June 30, 1999 to \$19,570,000 for the six months ended June 30, 2000. Selling and marketing expenses increased primarily as a result of the continued expansion of the sales force and marketing efforts required for growth, particularly in emerging regions, and for the marketing surrounding the launch of our CoStar Exchange product.

**SOFTWARE DEVELOPMENT.** Software development expenses increased 214% from \$549,000 for six months ended June 30, 1999 to \$1,722,000 for the six months ended June 30, 2000 reflecting development costs for the increased number of products we now support including CoStar COMPS and CoStar Exchange.

**GENERAL AND ADMINISTRATIVE EXPENSES.** General and administrative expenses increased 168% from \$4,508,000 for the six months ended June 30, 1999 to \$12,081,000 for the six months ended June 30, 2000. General and administrative expenses increased due to the hiring of new employees to support the expanding scope of our operations and client base and also the increase in employees due to Comps.

**PURCHASE AMORTIZATION.** Purchase amortization increased 327% from \$1,048,000 for the six months ended June 30, 1999 to \$4,476,000 for the six months ended June 30, 2000. Purchase amortization increased primarily due to the acquisition of Comps.

**ACQUIRED IN-PROCESS DEVELOPMENT.** Acquired in-process development costs of \$5,812,000 for the six months ended June 30, 2000 consist of in-process development costs written off as part of the Comps acquisition.

**OTHER INCOME, NET.** Interest and other income increased from \$678,000 for the six months ended June 30, 1999 to \$1,959,000 for the six months ended June 30, 2000. This increase was a direct result of interest earned on the proceeds from the follow-on public offering.

**INCOME TAX BENEFIT.** An income tax benefit of \$1,410,000 for the six months ended June 30, 2000 is a result of the impact of the reversal of the deferred tax liability in connection with the amortization of identified intangible assets established during recent acquisitions.

## LIQUIDITY AND CAPITAL RESOURCES

Our cash and cash equivalents balance was \$64,258,000 at June 30, 2000, a decrease of \$29,816,000 from \$94,074,000 at December 31, 1999. This decrease was due principally to the \$2,407,000 (net of acquired cash) used for the acquisition of Comps on February 10, 2000, cash used in operating activities, \$8,391,000 in purchases of property and equipment, debt repayments of \$2,625,000, and \$882,000 in purchased building photography. During the second quarter of 2000, we financed our operations and growth through cash flow from the established regions and the proceeds of the follow-on offering. Net cash used in operations for the six months ended June 30, 2000 was \$14,509,000 compared to net cash used by operating activities of \$1,884,000 for the six months ended June 30, 1999. This was a direct result of investments in research for the expansion in both emerging and acquired regions, the development and launch of new services and the acquisition of Comps. Additionally, we received advance payments from clients on a number of contracts, resulting in the generation of cash as reflected in the increased deferred revenue balances of \$8,503,000 and \$2,635,000 as of June 30, 2000 and December 31, 1999, respectively. This increase in deferred revenues was a result of the acquisition of Comps as well as a large number of annual contracts billed in the first half of 2000. We continue to experience overall operating losses as a result of our recent expansion into emerging and acquired regions and development of new services, while established regions continue to generate substantial cash flow from operations.

Net cash used in investing activities amounted to \$13,774,000 for the six months ended June 30, 2000, including \$2,407,000 (net of acquired cash) for the acquisition of Comps. Additional investing activities included purchased building photography and purchase of property and equipment, consisting principally of leasehold improvements, computers and office equipment. As a result of our expansion, we have entered into numerous operating leases for office space throughout the country, including the Company's and Comps' headquarters and have commitments for rent payments ranging from \$2,436,000 to \$4,405,000 annually over the next ten years. Other than these leases and related commitments for leasehold improvements, we currently have no material commitments for capital expenditures.

To date, we have grown in part by acquiring other companies, and we may continue to make acquisitions. Our acquisitions may vary in size and could be material to our current operations. We expect to use cash, stock, or other means of funding to make these acquisitions.

During the first six months of 2000, we experienced significant losses and negative operating cash flow as a result of expansion in emerging regions, expansion of services in established regions, costs for the introduction of new products and the acquisition of Comps. Some of these costs are non recurring, and many are fixed operating costs, which will not directly increase as a result of the related expected growth in revenue. Based on current plans we believe that our available cash combined with positive cash flow from our established regions should be sufficient to fund our operations for at least the next two years.

Through June 30, 1998, we operated as either a Subchapter S corporation or a limited partnership, and we were not subject to corporate income taxes. After June 30, 1998, we became a taxable entity. Although we have experienced losses to date, future profits, to the extent not offset by the benefits of loss carryforwards, would result in income tax liabilities. Further, the reversal of deferred taxes of approximately \$11.1 million at June 30, 2000, recorded in connection with the purchase of identifiable intangibles, will result in a non-cash income tax benefit in future periods. These accounts are subject to ongoing evaluation of our future tax liabilities. During the second quarter of 2000, we recorded a purchase price adjustment of approximately \$7.0 million related to our acquisition of Comps. This adjustment resulted in a decrease of the deferred tax liability and related goodwill.

We do not believe the impact of inflation has significantly affected our operations.

## ITEM 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company does not have significant exposure to market risks associated with the changes in interest rates related to its cash equivalent securities held as of June 30, 2000.

## PART II. OTHER INFORMATION

## ITEM 1 LEGAL PROCEEDINGS

On November 5, 1999, a suit was filed in the Court of Chancery of the State of Delaware in and for New Castle County under the caption Morris v. Avis, et al (C.A. 197554). The suit alleged breaches of fiduciary duties by the former members of the board of directors of Comps and Summit Partners. On November 8, 1999, a suit was filed in the Superior Court of the State of California of and for the County of San Diego captioned Berghoff v. Comps.com et al (case no. GIC 738362). The allegations in the California lawsuit were similar to the allegations in the Delaware suit. The plaintiffs in both of these lawsuits had requested monetary damages and injunctive relief to prevent the consummation of the merger between Comps and the Company. On January 6, 2000, the Delaware suit was voluntarily dismissed by the plaintiff. On February 4, 2000, the parties to the California lawsuit entered into a Memorandum of Understanding that sets forth their agreement to settle the lawsuit. The parties subsequently negotiated and executed a more detailed Joint Stipulation and Agreement of Compromise, Settlement and Release ("Joint Stipulation"). On April 7, 2000, the Court entered an Order of Preliminary Class Action Settlement, consistent with the terms of the Joint Stipulation. The Court scheduled a final settlement hearing for September 15, 2000, following appropriate notice to the class members.

## ITEM 2 CHANGES IN SECURITIES

None

## ITEM 3 DEFAULTS UPON SENIOR SECURITIES

None

## ITEM 4 SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Annual Meeting of the Company's stockholders was held on June 21, 2000. The following people were elected to the Board of Directors of the Company for a one-year term: Michael Klein, Andrew Florance, Warren Haber, David Bonderman, Josiah Low III, and John Simon. The vote was as follows: For, 14,068,388 shares; and withheld, 100,748 shares.

Amendments to the Company's 1998 Stock Incentive Plan, as amended, were approved upon the following vote: For, 11,805,941 shares; against, 1,743,375 shares; and abstain, 32,650 shares.

The appointment of Ernst & Young, LLP as independent public accountants of the Company for the fiscal year ending December 31, 2000 was approved upon the following vote: For 14,156,672 shares; against, 11,823 shares; and abstain 641 shares.

ITEM 5 OTHER INFORMATION

None

ITEM 6 EXHIBITS AND REPORTS ON FORM 8-K

A current report on Form 8-K was filed by the Company on August 2, 2000 with respect to the press release announcing the Company's second quarter earnings.

EXHIBIT NUMBER: EXHIBIT DESCRIPTION:

10.1 CoStar Group, Inc. 1998 Stock Incentive Plan, as amended.

10.2 Employment Agreement for John Place.

27 Financial Data Schedule

SIGNATURES

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

COSTAR GROUP, INC.

Date: August 14, 2000

By: /s/ Frank A. Carchedi

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Frank A. Carchedi  
Chief Financial Officer  
(Principal Financial and Accounting Officer  
and Duly Authorized Officer)

COSTAR GROUP, INC.  
1998 STOCK INCENTIVE PLAN  
(AS AMENDED ON JUNE 21, 2000)

## PURPOSE

CoStar Group, Inc., a Delaware corporation "CoStar" or the "Company"), wishes to recruit, reward, and retain employees and outside directors. To further these objectives, the Company hereby sets forth the CoStar Group, Inc. 1998 Stock Incentive Plan (the "Plan") to provide options ("Options") or direct grants ("Stock Grants" and, together with the Options, "Awards") to employees and outside directors with respect to shares of the Company's common stock (the "Common Stock"). The Plan is effective as of the effective date (the "Effective Date") of the Company's registration under Section 12 of the Securities Exchange Act of 1934 (the "Exchange Act") with respect to its initial public offering ("IPO").

## PARTICIPANTS

All Employees of CoStar and any Eligible Subsidiaries are eligible for Options and Stock Grants under this Plan, as are the directors of CoStar and the Eligible Subsidiaries who are not employees ("Eligible Directors"). Eligible employees and directors become "optionees" when the Administrator grants them an option under this Plan or "recipients" when they receive a direct grant of Common Stock. (Optionees and recipients are referred to collectively as "participants." The term participant also includes, where appropriate, a person authorized to exercise an Award in place of the original optionee.) The Administrator may also grant Options or make Stock Grants to certain other service providers.

Employee means any person employed as a common law employee of the Company or an Eligible Subsidiary.

## ADMINISTRATOR

The Administrator will be the Compensation Committee of the Board of Directors of CoStar (the "Compensation Committee"), unless the Board specifies another committee. The Board may also act under the Plan as though it were the Compensation Committee.

The Administrator is responsible for the general operation and administration of the Plan and for carrying out its provisions and has full discretion in interpreting and administering the provisions of the Plan. Subject to the express provisions of the Plan, the Administrator may exercise such powers and authority of the Board as the Administrator may find necessary or appropriate to carry out its functions. The Administrator may delegate its

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functions (other than those described in the GRANTING OF AWARDS section) to officers or employees of CoStar.

The Administrator's powers will include, but not be limited to, the power to amend, waive, or extend any provision or limitation of any Award. The Administrator may act through meetings of a majority of its members or by unanimous consent.

GRANTING OF AWARDS Subject to the terms of the Plan, the Administrator will, in its sole discretion, determine

the participants who receive Awards,

the terms of such Awards,

the schedule for exercisability or nonforfeitability (including any requirements that the participant or the Company satisfy performance criteria),

the time and conditions for expiration of the Award, and

the form of payment due upon exercise, if any.

The Administrator's determinations under the Plan need not be uniform and need not consider whether possible participants are similarly situated.

Options granted to employees may be nonqualified stock options ("NQSOs") or "incentive stock options" ("ISOs") within the meaning of Section 422 of the Internal Revenue Code of 1986, as amended from time to time (the "Code"), or the corresponding provision of any subsequently enacted tax statute. Options granted to Eligible Directors must be NQSOs. The Administrator will not grant ISOs unless the stockholders have approved the Plan.

The Administrator may impose such conditions on or charge such price for the Stock Grants as it deems appropriate.

SUBSTITUTIONS

The Administrator may also grant Awards in substitution for options or other equity interests held by individuals (i) as a result of their employment by or services to CoStar Group, L.P. or (ii) who become Employees of the Company or of an Eligible Subsidiary as a result of the Company's acquiring or merging with the individual's employer or acquiring its assets. If necessary to conform the Awards to the interests for which they are substitutes, the Administrator may grant substitute Awards under terms and conditions that vary from those the Plan otherwise requires.

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DIRECTOR FORMULA OPTIONS	Each Eligible Director of the Company shall be entitled to receive at the first meeting of the Board of Directors immediately following each of the Company's Annual Meeting of Stockholders an Option to purchase 1,000 shares of the Company's Common Stock at an exercise price equal to the Fair Market Value (as defined below) on such date of grant. Such Options shall vest in full on the first anniversary of the date of grant, provided that such Director is still a Director of the Company.
DATE OF GRANT	The Date of Grant will be the date as of which this Plan or the Administrator grants an Award to a participant, as specified in the Plan or in the Administrator's minutes.
EXERCISE PRICE	<p>The Exercise Price is the value of the consideration that a participant must provide in exchange for one share of Common Stock. The Administrator will determine the Exercise Price under each Award and may set the Exercise Price without regard to the Exercise Price of any other Awards granted at the same or any other time. The Company may use the consideration it receives from the participant for general corporate purposes.</p> <p>The Exercise Price per share for NQSOs may not be less than 100% of the Fair Market Value of a share on the Date of Grant. If an Option is intended to be an ISO, the Exercise Price per share may not be less than 100% of the Fair Market Value (on the Date of Grant) of a share of Common Stock covered by the Option; provided, however, that if the Administrator decides to grant an ISO to someone covered by Sections 422(b)(6) and 424(d) (as a more-than-10%-stock-owner), the Exercise Price of the Option must be at least 110% of the Fair Market Value (on the Date of Grant).</p> <p>The Administrator may satisfy any state law requirements regarding adequate consideration for Stock Grants by (i) issuing Common Stock held as treasury stock or (ii) charging the recipients at least the par value for the shares covered by the Stock Grant. The Administrator may designate that a recipient may satisfy (ii) either by direct payments or by the Administrator's withholding from other payments due to the recipient.</p>
FAIR MARKET VALUE	<p>Fair Market Value of a share of Common Stock for purposes of the Plan will be determined as follows:</p> <ul style="list-style-type: none"> <li>if the Common Stock is traded on a national securities exchange, the closing sale price on that date;</li> <li>if the Common Stock is not traded on any such exchange, the closing sale price as reported by the National Association of Securities Dealers, Inc. Automated Quotation System ("Nasdaq") for such date;</li> </ul>

if no such closing sale price information is available, the average of the closing bid and asked prices as reported by Nasdaq for such date; or

if there are no such closing bid and asked prices, the average of the closing bid and asked prices as reported by any other commercial service for such date.

For any date that is not a trading day, the Fair Market Value of a share of Common Stock for such date shall be determined by using the closing sale price or the average of the closing bid and asked prices, as appropriate, for the immediately preceding trading day.

The Fair Market Value will be deemed equal to the IPO price for any Options granted as of the date on which the IPO's underwriters price the IPO.

#### EXERCISABILITY

The Administrator will determine the times and conditions for exercise of or purchase under each Award but may not extend the period for exercise beyond the tenth anniversary of its Date of Grant (or five years for ISOs granted to 10% owners covered by Code Sections 422(b)(6) and 424(d)).

Awards will become exercisable at such times and in such manner as the Administrator determines and the Award Agreement, if any, indicates; provided, however, that the Administrator may, on such terms and conditions as it determines appropriate, accelerate the time at which the participant may exercise any portion of an Award or at which restrictions on Stock Grants lapse. For Stock Grants, "exercise" refers to acceptance of the Award or lapse of restrictions, as appropriate in context.

If the Administrator does not specify otherwise, Options will become exercisable and restrictions on Stock Grants (other than the Director Formula Grants) will lapse as to one-third of the covered shares on each of the first, second, and third anniversaries of the Date of Grant.

No portion of an Award that is unexercisable at a participant's termination of employment will thereafter become exercisable, unless the Award Agreement provides otherwise, either initially or by amendment.

#### CHANGE OF CONTROL

Upon a Change of Control (as defined below), all Options held by current Employees and directors will become fully exercisable and all restrictions on Stock Grants will lapse. A Change of Control for this purpose means the occurrence, after the Company's IPO, of any one or more of the following events:

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a person, entity, or group (other than the Company, any Company subsidiary, any Company benefit plan, or any underwriter temporarily holding securities for an offering of such securities) acquires ownership of more than 80% of the undiluted total voting power of the Company's then-outstanding securities eligible to vote to elect members of the Board ("Company Voting Securities");

consummation of a merger or consolidation of the Company into any other entity -- unless the holders of the Company Voting Securities outstanding immediately before such consummation, together with any trustee or other fiduciary holding securities under a Company benefit plan, hold securities that represent immediately after such merger or consolidation at least 20% of the combined voting power of the then outstanding voting securities of either the Company or the other surviving entity or its parent; or

the stockholders of the Company approve (i) a plan of complete liquidation or dissolution of the Company or (ii) an agreement for the Company's sale or disposition of all or substantially all the Company's assets, and such liquidation, dissolution, sale, or disposition is consummated.

Even if other tests are met, a Change of Control has not occurred under any circumstance in which the Company files for bankruptcy protection or is reorganized following a bankruptcy filing.

The ADJUSTMENT UPON CHANGES IN CAPITAL STOCK provisions will also apply if the Change of Control is a SUBSTANTIAL CORPORATE CHANGE (as defined in those provisions).

LIMITATION ON  
ISOS

An Option granted to an employee will be an ISO only to the extent that the aggregate Fair Market Value (determined at the Date of Grant) of the stock with respect to which ISOs are exercisable for the first time by the optionee during any calendar year (under the Plan and all other plans of the Company and its subsidiary corporations, within the meaning of Code Section 422(d)), does not exceed \$100,000. This limitation will be applied by taking Options into account in the order in which such Options were granted. If, by design or operation, the Option exceeds this limit, the excess will be treated as an NQSO.

METHOD OF  
EXERCISE

To exercise any exercisable portion of an Award, the participant must:

Deliver a written notice of exercise to the Secretary of the Company (or to whomever the Administrator designates), in a form complying with any rules the Administrator may issue, signed by the participant, and

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specifying the number of shares of Common Stock underlying the portion of the Award the participant is exercising;

Pay the full Exercise Price, if any, by cashier's or certified check for the shares of Common Stock with respect to which the Award is being exercised, unless the Administrator consents to another form of payment (which could include the use of Common Stock); and

Deliver to the Administrator such representations and documents as the Administrator, in its sole discretion, may consider necessary or advisable.

Payment in full of the Exercise Price need not accompany the written notice of exercise provided the notice directs that the stock certificates for the shares issued upon the exercise be delivered to a licensed broker acceptable to the Company as the agent for the individual exercising the option and at the time of closing of the sale of the Common Stock issued upon exercise of the Option, the broker will tender to the Company cash or cash equivalents acceptable to the Company and equal to the Exercise Price.

If the Administrator agrees to payment through the tender to the Company of shares of Common Stock, the individual must have held the stock being tendered for at least six months at the time of surrender. Shares of stock offered as payment will be valued, for purposes of determining the extent to which the participant has paid the Exercise Price, at their Fair Market Value on the date of exercise. The Administrator may also, in its discretion, accept attestation of ownership of Common Stock and issue a net number of shares upon Option exercise.

AWARD  
EXPIRATION

No one may exercise an Award more than ten years after its Date of Grant (or five years, for an ISO granted to a more-than-10% shareholder). Unless the Award Agreement provides otherwise, either initially or by amendment, no one may exercise an Award after the first to occur of:

EMPLOYMENT  
TERMINATION

The 90th day after the date of termination of employment (other than for death or Disability), where termination of employment means the time when the employer-employee or other service-providing relationship between the employee and the Company ends for any reason, including retirement. Unless the Award Agreement provides otherwise, termination of employment does not include instances in which the Company immediately rehires a common law employee as an independent contractor. The Administrator, in its sole discretion, will determine all questions of whether particular terminations or leaves of absence are terminations of employment;

**DISABILITY** For disability, the earlier of (i) the first anniversary of the participant's termination of employment for disability and (ii) thirty (30) days after the participant no longer has a disability, where "disability" means the inability to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment that can be expected to result in death or that has lasted or can be expected to last for a continuous period of not less than twelve months; or

**DEATH** The date twelve months after the participant's death.

If exercise is permitted after termination of employment, the Award will nevertheless expire as of the date that the former service provider violates any covenant not to compete in effect between the Company and the former employee. In addition, an optionee who exercises an Option more than 90 days after termination of employment with the Company and/or the Eligible Subsidiaries will only receive ISO treatment to the extent permitted by law, and becoming or remaining an employee of another related company (that is not an Eligible Subsidiary) or an independent contractor to the Company will not prevent loss of ISO status as a result of the formal termination of employment.

Nothing in this Plan extends the term of an Award beyond the tenth anniversary of its Date of Grant, nor does anything in this AWARD EXPIRATION section make an Award exercisable that has not otherwise become exercisable.

**AWARD AGREEMENT** Option Agreements will set forth the terms of each Option and will include such terms and conditions, consistent with the Plan, as the Administrator may determine are necessary or advisable. To the extent the agreement is inconsistent with the Plan, the Plan will govern. The Option Agreements may contain special rules. The Administrator may, but is not required to, issue agreements for Stock Grants.

**STOCK SUBJECT TO PLAN** Except as adjusted below under CORPORATE CHANGES, the aggregate number of shares of Common Stock that may be issued under the Awards (whether ISOs, NQSOs, or Stock Grants) may not exceed 3,000,000 shares and the maximum number of shares that may be granted under Awards for a single individual in a calendar year may not exceed 400,000 shares. (The individual maximum applies only to Awards first made under this Plan and not to Awards made in substitution of a prior employer's options or other incentives, except as Code Section 162(m) otherwise requires.) The Common Stock will come from either authorized but unissued shares or from previously issued shares that the Company reacquires, including shares it purchases on the open market. If any Award expires, is canceled, or terminates for any other reason, the shares of Common Stock available under that Award will

again be available for the granting of new Awards (but will be counted against that calendar year's limit for a given individual).

No adjustment will be made for a dividend or other right for which the record date precedes the date of exercise.

The participant will have no rights of a stockholder with respect to the shares of stock subject to an Award except to the extent that the Company has issued certificates for, or otherwise confirmed ownership of, such shares upon the exercise of the Award.

The Company will not issue fractional shares pursuant to the exercise of an Award, but the Administrator may, in its discretion, direct the Company to make a cash payment in lieu of fractional shares.

PERSON WHO  
MAY EXERCISE

During the participant's lifetime, only the participant or his duly appointed guardian or personal representative may exercise the Awards. After his death, his personal representative or any other person authorized under a will or under the laws of descent and distribution may exercise any then exercisable portion of an Award. If someone other than the original recipient seeks to exercise any portion of an Award, the Administrator may request such proof as it may consider necessary or appropriate of the person's right to exercise the Award.

ADJUSTMENTS  
UPON CHANGES  
IN CAPITAL STOCK

Subject to any required action by the Company (which it shall promptly take) or its stockholders, and subject to the provisions of applicable corporate law, if, after the Date of Grant of an Award,

the outstanding shares of Common Stock increase or decrease or change into or are exchanged for a different number or kind of security by reason of any recapitalization, reclassification, stock split, reverse stock split, combination of shares, exchange of shares, stock dividend, or other distribution payable in capital stock, or

some other increase or decrease in such Common Stock occurs without the Company's receiving consideration,

the Administrator may make a proportionate and appropriate adjustment in the number of shares of Common Stock underlying each Award, so that the proportionate interest of the participant immediately following such event will, to the extent practicable, be the same as immediately before such event. (This adjustment does not apply to Common Stock that the optionee has already purchased nor to Stock Grants that are already nonforfeitable, except to the extent of similar treatment for all stockholders.) Unless the Administrator determines another method would be appropriate, any such

adjustment to an Award will not change the total price with respect to shares of Common Stock underlying the unexercised portion of the Award but will include a corresponding proportionate adjustment in the Award's Exercise Price.

The Administrator will make a commensurate change to the maximum number and kind of shares provided in the STOCK SUBJECT TO PLAN section.

Any issue by the Company of any class of preferred stock, or securities convertible into shares of common or preferred stock of any class, will not affect, and no adjustment by reason thereof will be made with respect to, the number of shares of Common Stock subject to any Award or the Exercise Price except as this ADJUSTMENTS section specifically provides. The grant of an Award under the Plan will not affect in any way the right or power of the Company to make adjustments, reclassifications, reorganizations or changes of its capital or business structure, or to merge or to consolidate, or to dissolve, liquidate, sell, or transfer all or any part of its business or assets.

**SUBSTANTIAL  
CORPORATE  
CHANGE**

Upon a Substantial Corporate Change, the Plan and any unexercised Awards will terminate unless provision is made in writing in connection with such transaction for

the assumption or continuation of outstanding Awards, or

the substitution for such options or grants of any options or grants covering the stock or securities of a successor employer corporation, or a parent or subsidiary of such successor, with appropriate adjustments as to the number and kind of shares of stock and prices, in which event the Awards will continue in the manner and under the terms so provided.

Unless the Board determines otherwise, if an Award would otherwise terminate pursuant to the preceding sentence, participants who are then Employees or directors of the Company will have the right, at such time before the consummation of the transaction causing such termination as the Board reasonably designates, to exercise any unexercised portions of the Award, whether or not they had previously become exercisable. However, unless the Board determines otherwise, the acceleration will not occur if it would render unavailable "pooling of interest" accounting for any reorganization, merger, or consolidation of the Company.

A Substantial Corporate Change means the

dissolution or liquidation of the Company,

merger, consolidation, or reorganization of the Company with one or more corporations in which the Company is not the surviving corporation,

the sale of substantially all of the assets of the Company to another corporation, or

any transaction (including a merger or reorganization in which the Company survives) approved by the Board that results in any person or entity (other than any affiliate of the Company as defined in Rule 144(a)(1) under the Securities Act) owning 100% of the combined voting power of all classes of stock of the Company.

SUBSIDIARY  
EMPLOYEES

Employees of Company Subsidiaries will be entitled to participate in the Plan, except as otherwise designated by the Board of Directors or the Committee.

Eligible Subsidiary means each of the Company's Subsidiaries, except as the Board otherwise specifies. For ISO grants, Subsidiary means any corporation (other than the Company) in an unbroken chain of corporations beginning with the Company if, at the time an ISO is granted to a Participant under the Plan, each of the corporations (other than the last corporation in the unbroken chain) owns stock possessing 50% or more of the total combined voting power of all classes of stock in one of the other corporations in such chain. For NQSOs, the Board or the Committee can use a different definition of Subsidiary in its discretion.

LEGAL  
COMPLIANCE

The Company will not issue any shares of Common Stock under an Award until all applicable requirements imposed by Federal and state securities and other laws, rules, and regulations, and by any applicable regulatory agencies or stock exchanges, have been fully met. To that end, the Company may require the participant to take any reasonable action to comply with such requirements before issuing such shares. No provision in the Plan or action taken under it authorizes any action that is otherwise prohibited by Federal or state laws.

The Plan is intended to conform to the extent necessary with all provisions of the Securities Act of 1933 ("Securities Act") and the Exchange Act and all regulations and rules the Securities and Exchange Commission issues under those laws. Notwithstanding anything in the Plan to the contrary, the Administrator must administer the Plan, and Awards may be granted and exercised, only in a way that conforms to such laws, rules, and regulations. To the extent permitted by applicable law, the Plan and any Awards will be deemed amended to the extent necessary to conform to such laws, rules, and regulations.

PURCHASE FOR  
INVESTMENT  
AND OTHER  
RESTRICTIONS

Unless a registration statement under the Securities Act covers the shares of Common Stock a participant receives upon exercise of his Award, the Administrator may require, at the time of such exercise or receipt of a grant, that the participant agree in writing to acquire such shares for investment and not for public resale or distribution, unless and until the shares subject to the Award are registered under the Securities Act. Unless the shares are registered under the Securities Act, the participant must acknowledge:

that the shares purchased on exercise of the Award are not so registered,

that the participant may not sell or otherwise transfer the shares unless

the shares have been registered under the Securities Act in connection with the sale or transfer thereof, or

counsel satisfactory to the Company has issued an opinion satisfactory to the Company that the sale or other transfer of such shares is exempt from registration under the Securities Act, and

such sale or transfer complies with all other applicable laws, rules, and regulations, including all applicable Federal and state securities laws, rules, and regulations.

Additionally, the Common Stock, when issued upon the exercise of an Award, will be subject to any other transfer restrictions, rights of first refusal, and rights of repurchase set forth in or incorporated by reference into other applicable documents, including the Company's articles or certificate of incorporation, by-laws, or generally applicable stockholders' agreements.

The Administrator may, in its sole discretion, take whatever additional actions it deems appropriate to comply with such restrictions and applicable laws, including placing legends on certificates and issuing stop-transfer orders to transfer agents and registrars.

## TAX WITHHOLDING

The participant must satisfy all applicable Federal, state, and local income and employment tax withholding requirements before the Company will deliver stock certificates upon the exercise of an Award. The Company may decide to satisfy the withholding obligations through additional withholding on salary or wages. If the Company does not or cannot withhold from other compensation, the participant must pay the Company, with a cashier's check or certified check, the full amounts required by withholding. Payment of withholding obligations is due before the Company issues shares with respect to the

Award. If the Committee so determines, the participant may instead satisfy the withholding obligations by directing the Company to retain shares from the Award exercise, by tendering previously owned shares, or by attesting to his ownership of shares (with the distribution of net shares).

TRANSFERS,  
ASSIGNMENTS,  
AND PLEDGES

Unless the Administrator otherwise approves in advance in writing, an Award may not be assigned, pledged, or otherwise transferred in any way, whether by operation of law or otherwise or through any legal or equitable proceedings (including bankruptcy), by the participant to any person, except by will or by operation of applicable laws of descent and distribution. If Rule 16b-3 then applies to an Award, the participant may not transfer or pledge shares of Common Stock acquired under a Stock Grant or upon exercise of an Option until at least six (6) months have elapsed from (but excluding) the Date of Grant, unless the Administrator approves otherwise in advance in writing.

AMENDMENT OR  
TERMINATION  
OF PLAN AND  
OPTIONS

The Board may amend, suspend, or terminate the Plan at any time, without the consent of the participants or their beneficiaries; provided, however, that no amendment will deprive any participant or beneficiary of any previously declared Award. Except as required by law or by the CORPORATE CHANGES section, the Administrator may not, without the participant's or beneficiary's consent, modify the terms and conditions of an Award so as to adversely affect the participant. No amendment, suspension, or termination of the Plan will, without the participant's or beneficiary's consent, terminate or adversely affect any right or obligations under any outstanding Awards.

PRIVILEGES OF  
STOCK OWNERSHIP

No participant and no beneficiary or other person claiming under or through such participant will have any right, title, or interest in or to any shares of Common Stock allocated or reserved under the Plan or subject to any Award except as to such shares of Common Stock, if any, that have been issued to such participant.

EFFECT ON  
OTHER PLANS

Whether exercising or receiving an Award causes the participant to accrue or receive additional benefits under any pension or other plan is governed solely by the terms of such other plan.

LIMITATIONS ON  
LIABILITY

Notwithstanding any other provisions of the Plan, no individual acting as a director, employee, or agent of the Company shall be liable to any participant, former participant, spouse, beneficiary, or any other person for any claim, loss, liability, or expense incurred in connection with the Plan, nor shall such individual be personally liable because of any contract or other instrument he executes in such other capacity. The Company will indemnify and hold harmless each director, employee, or agent of the Company to whom any duty or power relating to the administration or interpretation of the Plan

has been or will be delegated, against any cost or expense (including attorneys' fees) or liability (including any sum paid in settlement of a claim with the Board's approval) arising out of any act or omission to act concerning this Plan unless arising out of such person's own fraud or bad faith.

NO EMPLOYMENT  
CONTRACT

Nothing contained in this Plan constitutes an employment contract between the Company and the participants. The Plan does not give any participant any right to be retained in the Company's employ, nor does it enlarge or diminish the Company's right to terminate the participant's employment.

APPLICABLE LAW

The laws of the State of Delaware (other than its choice of law provisions) govern this Plan and its interpretation.

DURATION OF PLAN

Unless the Board extends the Plan's term, the Administrator may not grant Awards after May 8, 2008. The Plan will then terminate but will continue to govern unexercised and unexpired Awards.

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## EMPLOYMENT AGREEMENT

This AGREEMENT (the "Agreement") dated this 1st day of May, 2000 (the "Effective Date") is by and between CoStar Realty Information, Inc., a Delaware corporation (the "Company"), and John Place (the "Executive").

The Company desires to employ the Executive to devote his full time and best efforts to the business of the Company, and the Executive desires to be so employed on the terms and conditions outlined below.

The parties agree as follows:

1. Employment. The Company agrees to employ Executive at the Company's offices in the Greater Washington D.C. metropolitan area, and Executive agrees to be so employed in the capacity of Executive Vice President. Executive shall perform such functions and undertake such responsibilities as are assigned from time to time by the President of the Company. Executive agrees that he shall spend no less than four (4) Business Days (as defined below) per week in the Company's principal executive offices in the Greater Washington D.C. metropolitan area, other than when Executive is traveling on Company business or on vacation. "Business Day" means any day other than a Saturday, Sunday or a day that is designated as a holiday pursuant to the Company's written policies.

2. Term. The term of Executive's employment under this Agreement shall commence on the date of this Agreement and shall continue for the initial term of two (2) years (the "Initial Term"), and for automatic and successive renewal terms of one (1) year each (each, a "Renewal Term" and collectively, the "Renewal Terms"), unless either the Company or Executive elects not to extend the term beyond the Initial Term or any Renewal Term (herein, the Initial Term or a Renewal Term is sometimes referred to as the "Current Term") and gives to the other party hereto written notice of termination at least three (3) months prior to the end of the Initial Term or the Renewal Term.

3. Full time and efforts. Executive shall diligently and conscientiously devote substantially his full time and exclusive attention and best efforts to his duties under this Agreement.

4. Compensation.

(a) Commencing as of the Effective Date of this Agreement, the Company shall pay Executive base compensation for his services in the amount of \$280,000 per year (the "Base Compensation"). The President of the Company in consultation with the Compensation Committee of the Board of Directors of the Company will review Executive's performance and determine any appropriate increases annually thereafter. Base Compensation shall be payable in biweekly or such other installments as shall be consistent with the Company's payroll procedures for its senior executives.

(b) In addition, Executive shall be eligible to be granted an annual performance bonus (the "Annual Bonus") of between 25% and 85% of Base Compensation. The first annual bonus paid will be calculated pro rata based on Base Compensation for the period from the Effective Date of the Agreement through December 31, 2000. Thereafter, the annual bonus will be based on Base Compensation during each calendar year. The minimum annual bonus will be 25% of Base Compensation, and additional amounts up to an aggregate amount of 85% of Base Compensation will be determined based on performance related to criteria established by the President of the Company and the Board of Directors.

(c) In addition, Executive will be awarded 60,000 stock options in CoStar Group, Inc. ("CoStar") (the "Initial Options"), the Company's parent, vesting 25% on the grant date (the Effective Date of employment), 25% after the first year, 25% after the second year, and 25% after three years. The exercise price for the Initial Options shall be the Fair Market Value (as defined in CoStar's 1998 Incentive Stock Plan) of the CoStar common stock on the Effective Date.

(d) In addition, Executive shall be awarded an initial bonus of \$75,000 (the "Initial Bonus"), with \$25,000 to be paid within 30 days of the Effective Date, \$25,000 to be paid within 60 days of the Effective Date, and \$25,000 to be paid within 90 days of the Effective Date; provided, however, that if Executive is terminated with cause (as defined in Section 8) or if Executive terminates his employment with the Company (or has given notice to the Company to terminate his employment with the Company) within twelve (12) months of the Effective Date, then Executive shall pay to the Company within ten (10) days of his termination date with the Company the full amount of the Initial Bonus.

5. Benefits. Executive shall be entitled to participate in, and receive benefits from any insurance, medical, disability, vacation or pension plan of the Company for which Executive satisfies the generally applicable criteria for eligibility, and to other perquisites which may be in effect at any time during the term hereof that are generally available to executive officers of the Company.

6. Expense reimbursement. The Company shall reimburse Executive for all categories of expenses incurred in carrying out his duties under this Agreement that the Company's policies regard as reasonable and necessary. Executive shall present to the Company from time to time an itemized account of, and supporting documentation for, such expenses in any form generally required by the Company. The Company hereby agrees to reimburse Executive for Executive's reasonable relocation expenses to the Greater Washington D.C. area in accordance with the Company's relocation policy in effect from time to time. For the period between the Effective Date and December 31, 2000, the Company agrees to provide an apartment in the greater Bethesda, Maryland area for the Executive's use.

7. Termination without cause.

(a) By the Company. The Company may terminate this Agreement without cause (and regardless of the time periods and provisions in Section 2 hereof) upon sixty (60)

days written notice. In such an event (other than a termination as provided for in Section 2 of this Agreement): (i) any remaining Initial Options due to vest within twelve (12) months of the date of such written notice shall vest immediately; and (ii) Executive will, as severance and liquidated damages and in consideration of his execution of a complete and absolute release of the Company and its affiliates and their respective directors and officers from any and all further claims, receive on a monthly basis, as if he had not been terminated, all payments (other than bonus) he would have received for the lessor of (x) the term remaining under the Agreement had he not been terminated from the date of such written notice, or (y) twelve months from the date of such written notice.

(b) Termination after merger or acquisition. In the event of the merger of the Company or CoStar, or the acquisition, directly or indirectly, of all or substantially all of the Company's or CoStar's assets or a controlling interest in the voting shares of the Company or CoStar by an unaffiliated party (a "Change of Control"), Executive may elect to treat that event as a termination by the Company without cause unless the new party: (a) extends to him a reasonable offer to (i) be retained by the Company in an executive position of responsibility, authority and compensation comparable in material respects (including location) to the position of Executive immediately prior to the Change of Control, (ii) retain all rights accorded under this Agreement and (iii) be afforded all privileges accorded to other executives of the Company; and (b) in fact retains Executive in such capacity for at least twelve (12) months after the Change of Control.

(c) By Executive. Executive may without cause terminate this Agreement, by giving one hundred eighty (180) days written notice during the Initial Term, or ninety (90) days written notice during any Renewal Term, to the Company. In such event, at the sole discretion of the Company, Executive shall continue to render all services through the date of termination. Executive shall be paid the base compensation, accrued Annual Bonus, if any, and vested options as provided by Section 4 up to the date of termination, but shall not receive any salary or bonus payment thereafter nor shall any stock option that is not otherwise vested or nonforfeitable on the date of termination become vested or nonforfeitable on such date or thereafter.

8. Termination for cause. The Company may terminate this Agreement (a) for cause at any time by notifying Executive in writing of such termination and the cause thereof or (b) in the event of Executive's death or prolonged disability; provided, however, that the only grounds constituting "cause" shall be: (i) Executive's negligence in the performance of his duties hereunder, intentional nonperformance or mis-performance of such duties, or refusal to abide by or comply with the reasonable, directives of the Board of Directors of the Company or the President of the Company, or the Company's material policies and procedures (including without limitation the provisions of Section 9 hereof), which actions continue uncured for a period of at least ten (10) days after receipt by Executive of written notice of the need to cure or cease; (ii) Executive's willful dishonesty, fraud, or misconduct with respect to the business or affairs of the Company; (iii) Executive's indictment for, conviction of, or guilty or nolo contendere plea to, a felony; and (iv) Executive's abuse of alcohol or drugs (legal or illegal), other than legal drugs taken under the directions of a physician, that, in the Company's reasonable judgment, materially impairs Executive's ability to perform his duties hereunder. In any such event, Executive will forfeit all unvested options and all claims to bonuses not yet awarded, and will be paid salary,

excluding bonus, through the date of the termination; provided, however, that in the event of termination for death or prolonged disability, all unvested options shall immediately vest.

#### 9. Confidentiality, Invention and Non-Compete Agreement.

(a) During the term of this Agreement, and thereafter for the duration of the period, if any, that Executive continues to be employed by the Company and/or any other entity owned by or affiliated with the Company or on an "at will" basis, and thereafter for the Non-Competition Period (defined below), Executive shall not, directly or indirectly, for himself or on behalf of or in conjunction with any other person, company, partnership, corporation, business, group, or other entity (each, a "Person"):

(i) engage, as an officer, director, shareholder, owner, partner, member, joint venturer, or in a managerial capacity, whether as an employee, independent contractor, consultant, advisor, or sales representative, in any business selling any products or services in direct competition with the Company in the United States, Canada, the United Kingdom, or other nations in which the Company is conducting or in which he was aware the Company had plans to conduct business within the eighteen (18) months following his termination (the "Territory"); provided, however, that the foregoing covenant shall not be deemed to prohibit Executive from acquiring as an investment not more than one percent (1%) of the capital stock of a competing business whose stock is traded on a national securities exchange or over-the-counter;

(ii) call upon any Person who is, at that time, within the Territory, an employee of the Company for the purpose or with the intent of enticing such employee away from or out of the employ of the Company;

(iii) call upon any Person who or that is, at that time, or has been, within one year prior to that time, a customer of the Company within the Territory for the purpose of soliciting or selling products or services in direct competition with the Company within the Territory; or

(iv) on Executive's own behalf or on behalf of any competitor, call upon any Person as a prospective acquisition candidate for an entity other than the Company or its affiliates who or that, during Executive's employment by the Company was, to Executive's knowledge, either called upon by the Company as a prospective acquisition candidate or was the subject of an acquisition analysis conducted by the Company. Executive, to the extent lacking the knowledge described in the preceding sentence, shall immediately cease all contact with any prospective acquisition candidate upon being informed that the Company had called upon such candidate or made an acquisition analysis thereof.

(b) Executive acknowledges that during the course of his employment, he may develop and obtain access to trade secrets, proprietary software and other "confidential business information" of the Company, such as its software systems, sources of data, databases and other competitively sensitive information kept in confidence by the Company such as selling and pricing information and procedures, research methodologies, customer lists, business and

marketing plans, and internal financial statements. Executive agrees to not use or disclose any trade secrets, proprietary software or confidential business information to which he is exposed or has access in the course of his employment with the Company, even if elements of any of them may belong to third parties, during his employment and for so long afterwards as the Company seeks to maintain as confidential the proprietary software, trade secrets or confidential business information, whether or not the software, trade secrets and confidential business information are in written or tangible form, except as required and authorized during the performance of Executive's duties for and with the Company. Executive agrees that, given the nature of the Company's business and business plans there will never come a time when disclosure of the Company's proprietary software, trade secrets or confidential information would not be seriously injurious to the Company.

(c) Executive acknowledges that he has been employed by the Company during its critical developmental and roll-out stages and that leaving the employ of the Company to join any business competitor would seriously hamper the business of the Company. Accordingly, Executive agrees that the Company shall be entitled to injunctive relief to prevent him from violating this Section 9, in addition to all remedies permitted by law, to enforce the provisions of this Agreement. Executive further acknowledges that his training, experience and technical skills are of such breadth that they can be employed to Executive's advantage in other areas which are not in direct competition with the business of the Company on the date of termination of Executive's employment and consequently the foregoing obligations will not unreasonably impair Executive's ability to engage in business activity after the termination of Executive's employment.

(d) For purposes of Section 8 and Section 9 of this Agreement, the term "Company" shall mean the Company, its parent, and each of its parent's direct or indirect subsidiaries, and each of these entities' predecessors in interest and successors; and the term "Non-Competition Period" shall mean the period commencing on the Effective Date to and including the second anniversary of the date on which Executive ceases to be employed by the Company (provided, however, that the Non-Competition Period, during which the agreements and covenants of Executive made in this Section 9 shall be effective, shall be computed by excluding from such computation any time during which Executive is in violation of any provision of this Section 9).

(e) The covenants in this Section 9 are severable and separate, and the unenforceability of any specific covenant shall not affect the provisions of any other covenant. If any provision of this Section 9 relating to the time period or geographic area of the restrictive covenants shall be declared by a court of competent jurisdiction to exceed the maximum time period or geographic area, as applicable, that such court deems reasonable and enforceable, said time period or geographic area shall be deemed to be, and thereafter shall become, the maximum time period or largest geographic area that such court deems reasonable and enforceable and this Agreement shall automatically be considered to have been amended and revised to reflect such determination. Upon termination of this Agreement for any reason, the covenants specified in this Section 9 shall survive for the term specified herein.

(f) All of the covenants in this Section 9 shall be construed as an agreement independent of any other provision in this Agreement, and the existence of any claim or cause of action of Executive against the Company, whether predicated on this Agreement or otherwise, shall not constitute a defense to the enforcement by the Company of such covenants.

10. Notices. All notices required or permitted to be given under this Agreement shall be given by certified mail, return receipt requested, to the parties at the following addresses or to such other addresses as either may designate in writing to the other party.

(a) If to the Company:

Andrew C. Florance  
President  
CoStar Realty Information, Inc.  
7475 Wisconsin Avenue  
Sixth Floor  
Bethesda, Maryland 20814  
Telefax: 301-718-2444

(b) If to Executive, to the address indicated below Executive's name on the signature page.

11. Arbitration. The parties agree that any dispute between the parties relating to this Agreement shall not be resolved in litigation, but instead shall be resolved in final, binding arbitration by a single arbitrator under the auspices of the American Arbitration Association ("AAA") in Washington, D.C. Any such arbitration shall be conducted in accordance to the AAA's Employment Dispute Resolution Procedures.

12. Waiver of Breach. The waiver by either party of a breach of any provisions of this Agreement by the other shall not operate or be construed as a waiver of any subsequent breach. A delay or failure by either party to exercise a right under this Agreement, or a partial or single exercise of that right, shall not constitute a waiver of that or any other right.

13. Governing Law. The Agreement shall be governed by and construed and enforced in accordance with the laws of the State of Delaware.

14. Binding Effect. This Agreement shall be binding upon and share inure to the benefit of the Company and its respective successors and assigns but the rights and obligations of Executive are personal and may not be assigned or delegated without the Company's prior written consent.

15. Counterparts. This Agreement, for the convenience of the parties, may be executed in any number of counterparts, all of which when taken together shall constitute one and the same Agreement.

16. Entire Agreement Concerning Employment; Supremacy of Employment Agreement. This Agreement and any related stock option agreement constitute the entire agreement between the parties as to Executive's employment and compensation therefor and supersede and replace any and all agreements, written or oral, as to such matters. This Agreement may not be modified or amended orally, but only by an agreement in writing, signed by the party against whom enforcement of any waiver, change, modification, extension or discharge is sought. If there is any conflict with respect to Executive between the provisions of this Agreement and the provisions of the Stock Option Plan, the provisions of this Agreement shall govern.

17. Amendments. This Agreement may be amended only in writing, signed by both parties.

In witness whereof, the parties have executed this Agreement effective as of the date set forth above.

COSTAR REALTY INFORMATION, INC.

EXECUTIVE

By: /s/

By: /s/

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Name: Andrew C. Florance  
Title: President

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Name: John Place

The schedule contains summary financial information extracted from the consolidated balance sheet and statement of operations of COSTAR GROUP, INC. as of and for the six months ended June 30, 2000 and is qualified in its entirety by reference to such financial statements.

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	DEC-31-2000	
	JUN-30-2000	
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	(1,410)	
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		0
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	(1.91)	
	(1.91)	