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SONO TEK CORP
Form 10-Q
January 16, 2001

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended: November 30, 2000

OR

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

Commission File No.: 0-16035

SONO-TEK CORPORATION
(Exact name of registrant as specified in its charter)

New York 14-1568099 (State or other jurisdiction of (IRS Employer
incorporation or organization) Identification No.)

2012 Rt. 9W, Milton, NY 12547
(Address of Principal Executive Offices) (Zip Code)

Registrant's telephone no., including area code: (845) 795-2020

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 X NO _____

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Class	Outstanding as of January 16, 2001
Common Stock, par value \$.01 per share	9,092,355

SONO-TEK CORPORATION

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SONO-TEK CORPORATION CONSOLIDATED BALANCE SHEETS

ASSETS

	November 30 2000 Unaudited -----
Current Assets	
Cash and cash equivalents	\$ 43,720
Accounts receivable (less allowance of \$36,997 and \$39,997 at November 30 and February 29, respectively)	1,155,788
Inventories (Note 5)	1,240,232
Prepaid expenses and other current assets	131,300
Total current assets	2,571,040
Equipment, furnishings and leasehold improvements (less accumulated depreciation of \$532,913 and \$469,011 at November 30 and February 29, respectively)	320,095
Intangible assets, net:	
Goodwill	1,275,084
Patents, patents pending and copyrights (Note 1)	27,142
Deferred financing fees	27,235
Total intangible assets, net	1,329,461
Long-term equity investments (Note 6)	16,686
Other assets	11,342
TOTAL ASSETS	\$4,248,624

LIABILITIES AND STOCKHOLDERS' EQUITY

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Current Liabilities:		
Accounts payable		\$ 975,647
Deferred revenue		0
Accrued expenses		736,738
Revolving line of credit		350,000
Short term loans-related parties (Note 7)		302,084
Current maturities of long term debt		253,611
Short term convertible loan		0

Total current liabilities		2,618,080

Subordinated mezzanine debt		398,368
Long term debt, less current maturities		121,737
Subordinated convertible loans-related parties		150,000

Total liabilities		3,288,185
Commitments and Contingencies		
Put Warrants		77,000

Stockholders' Equity		
Common stock, \$.01 par value; 25,000,000 shares authorized, 9,092,355 and 8,866,612 outstanding at November 30 and February 29, respectively		90,924
Additional paid-in capital		5,980,167
Accumulated deficit		(5,187,652)

Total stockholders' equity		883,439

TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY		\$4,248,624
		=====

See notes to consolidated financial statements.

SONO-TEK CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS

	Nine Months Ended November 30, Unaudited		Three Mo
	2000	1999	20
	-----	-----	-----
Net Sales	\$6,274,904	\$3,660,200	\$1,980
Cost of Goods Sold	3,608,736	1,726,067	1,024
	-----	-----	-----
Gross Profit	2,666,168	1,934,133	956
	-----	-----	-----
Operating Expenses			
Research and product development costs	687,693	430,068	218
Marketing and selling expenses	1,108,465	787,757	363
General and administrative costs	691,249	591,840	243
	-----	-----	-----
Total Operating Expenses	2,487,407	1,809,665	824
	-----	-----	-----

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Operating Income	178,761	124,468	132
Other (Loss) Income:			
Interest expense	(230,765)	(167,587)	(53)
Equity loss in PNR (Note 6)	(70,585)	0	(18)
Interest income and other (loss) income	7,773	11,980	3
	-----	-----	-----
Total Other (Loss) Income	(293,577)	(155,607)	(68)
(Loss) Income Before Income Taxes	(114,816)	(31,139)	64
Income Tax Expense	0	0	
	-----	-----	-----
Net (Loss) Income	\$ (114,816)	\$ (31,139)	\$64
	=====	=====	=====
Basic (Loss) Earnings Per Share	\$ (0.01)	\$ (0.00)	\$
	=====	=====	=====
Diluted (Loss) Earnings Per Share	\$ (0.01)	\$ (0.00)	\$
	=====	=====	=====
Weighted Average Shares - Basic	8,984,787	7,155,467	9,047
	=====	=====	=====
Weighted Average Shares - Diluted	8,984,787	7,155,467	10,987
	=====	=====	=====

See notes to consolidated financial statements.

SONO-TEK CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months
CASH FLOWS FROM OPERATING ACTIVITIES:	2000

Net Loss	\$ (114,816)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:	
Non-cash charge for issuance of warrants	75,831
Accrued interest-short term loans-related parties	27,337
Imputed interest expense on subordinated mezzanine debt	16,308
Loss on equity investment	2,624
Depreciation and amortization	141,529
(Benefit) provision for doubtful accounts	(3,000)
(Increase) decrease in:	
Accounts receivable	466,851
Inventories	(15,852)
Prepaid expenses and other current assets	(53,792)
Increase (decrease) in:	
Accounts payable and accrued expenses	219,176
Customer deposits	181,396
Deferred revenue	(725,491)
Non-current rent payable	0

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Net Cash Provided by (Used in) Operating Activities	218,101
<hr/>	
CASH FLOWS FROM INVESTING ACTIVITIES:	
Acquisition costs net of cash received	(102,813)
Purchase of equipment and furnishings	(127,003)
<hr/>	
Net Cash Used in Investing Activities	(229,816)
<hr/>	
CASH FLOW FROM FINANCING ACTIVITIES:	
Proceeds from revolving line of credit	15,693
Proceeds from bank loan for production equipment	78,859
Proceeds from short term loans-related parties	204,000
Proceeds from subordinated mezzanine debt	0
Proceeds from issuance of stock	130,000
Proceeds from exercise of warrants	55,692
Proceeds from exercise of stock options	1,602
Deferred financing fees	0
Repayments of short term loans-related party	(141,000)
Repayments of short term borrowings	(100,000)
Repayments of note payable and equipment loans	(197,587)
<hr/>	
Net Cash Provided by Financing Activities	47,259
<hr/>	
NET INCREASE IN CASH AND CASH EQUIVALENTS	35,544
CASH AND CASH EQUIVALENTS	
Beginning of period	8,176
<hr/>	
End of period	\$43,720
<hr/>	
SUPPLEMENTAL DISCLOSURE:	
Interest paid	\$34,859
<hr/>	
Common stock issued in connection with purchase of SEREC assets	\$7,500
<hr/>	
Non-cash equity contribution in PNR	\$9,800
<hr/>	
Non-cash exchange of accrued bonuses for common stock	\$0
<hr/>	

See notes to consolidated financial statements.

SONO-TEK CORPORATION
Notes to Consolidated Financial Statements
November 30, 2000 and 1999

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Consolidation - The accompanying consolidated financial statements of Sono-Tek Corporation, a New York Corporation (the "Company"), include the accounts of the Company and its wholly owned subsidiary, Sono-Tek Cleaning Systems, Inc. ("SCS"), a New Jersey Corporation formerly known as S&K Products International, Inc., ("S&K"), which the Company acquired on August 3, 1999 (the "Acquisition"). All significant intercompany accounts and transactions are eliminated in consolidation. The inclusion of SCS's results since August 3, 1999 has an effect on the comparison of the Company's Fiscal Year 2001 results to prior periods.

Interim Reporting - The attached summary consolidated financial information does

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not include all disclosures required to be included in a complete set of financial statements prepared in conformity with accounting principles generally accepted in the United States of America. Such disclosures were included with the financial statements of the Company at February 29, 2000, and included in its report on Form 10-K. Such statements should be read in conjunction with the data herein.

The financial information reflects all adjustments which, in the opinion of management, are necessary for a fair presentation of the results for the interim periods presented. The results for such interim periods are not necessarily indicative of the results to be expected for the year.

Patent and Patent Pending Costs - Costs of patent applications are deferred and charged to operations over seventeen years for domestic patents and twelve years for foreign patents. However, if it appears that such costs are related to products which are not expected to be developed for commercial application within the reasonably foreseeable future, or are applicable to geographic areas where the Company no longer requires patent protection, they are written-off to operations. The accumulated amortization is \$84,554 and \$80,053 at November 30 and February 29, 2000, respectively.

Reclassifications - Certain February 29, 2000 balances have been reclassified to conform with the current period presentations.

Adoption of Financial Accounting Standards - In June 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). This statement establishes standards for the accounting and reporting for derivative instruments and for hedging activities and requires the recognition of all derivatives as assets or liabilities measured at their fair value. Gains or losses resulting from changes in the fair value of derivatives would be recognized in earnings in the period of change unless certain hedging criteria are met. The Company does not expect SFAS 133 to have a material impact on the consolidated financial statements. The FASB issued SFAS Nos. 137 and 138, which deferred the effective date of implementation of SFAS 133 to all fiscal quarters of all fiscal years beginning after June 15, 2000 and amended SFAS 133, respectively.

Revenue Recognition in Financial Statements - In December 1999, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. 101 ("SAB 101"), "Revenue Recognition in Financial Statements." SAB 101 summarizes certain of the SEC's views in applying accounting principles generally accepted in the United States of America to revenue recognition in financial statements. On June 26, 2000, the SEC issued SAB 101B to defer the effective date of implementation of SAB 101 until no later than the fourth quarter of fiscal years beginning after December 31, 1999. The Company is required to adopt SAB 101 by February 28, 2001. The Company does not expect the adoption of SAB 101 to have a material impact on the consolidated financial statements.

NOTE 2: SEGMENT INFORMATION

The Company has two reportable segments: spraying products and cleaning and drying systems. The spraying products segment is primarily engaged in the business of developing, manufacturing, selling, installing and servicing ultrasonic spray equipment. The cleaning and drying systems segment is engaged in the business of developing, manufacturing, selling, installing and servicing cleaning and drying systems for the semiconductor, disk drive and precision cleaning industries.

Summary financial information concerning the Company's reportable segments is shown in the following table:

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	Nine Months Ended November 30, 20	
	Spraying Products	Cleaning Systems
Net Sales	\$3,361,438	\$2,913,466
Net Income (Loss)	370,566	(485,382)
Capital Expenditures	121,561	5,442
Depreciation and Amortization Expense	57,225	84,305

	Three Months Ended November 30,	
	Spraying Products	Cleaning Systems
Net Sales	\$1,190,617	\$790,303
Net Income (Loss)	233,426	(169,404)
Capital Expenditures	23,253	0
Depreciation and Amortization Expense	23,329	30,871

The Company operated in a single reportable segment for the period from March 1, 1999 through August 3, 1999.

NOTE 3: ACQUISITION OF SCS

On August 3, 1999 the Company purchased all the outstanding stock of S&K, a supplier of cleaning and drying systems for the semiconductor, disk drive, and precision cleaning industries. In June 2000, the Company changed S&K's name to SCS.

The following unaudited proforma information presents a summary of the consolidated results of operations of the Company and SCS as if the acquisition had occurred on March 1, 1999.

Proforma Consolidated Statement of Operati
 Nine months ended November 30, 1999

Net Sales	\$4,219,427
Cost of Goods Sold	1,962,130

Gross Profit	2,257,297
Operating Expenses	2,329,840

Operating Loss	(72,543)
Interest Expense	(198,672)
Interest & Misc. Income	28,382

Net Loss	\$ (242,833)
	=====

These unaudited pro forma results have been prepared for comparative purposes only and include certain adjustments, such as additional amortization expense as a result of goodwill and the elimination of extraordinary items associated with

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the acquisition. They do not purport to be indicative of the results of operations that actually would have resulted had the combination occurred on March 1, 1999, or of future results of operations of the consolidated entities.

NOTE 4: ACQUISITION OF SEREC ASSETS

On September 21, 2000, the Company acquired certain intellectual property and intangible assets of Serec Corporation, a Rhode Island corporation which manufactured and sold solvent based cleaning systems. In exchange for \$100,000 cash, the Company received the rights to seven patents, one registered trademark, unfulfilled purchase orders, engineering designs and certain other intangible assets. Professional fees and other costs of \$10,313, \$7,500 of which, was attributed to the issuance of common stock, were capitalized as additional purchase price. The aggregate purchase price of \$110,313 is recorded as goodwill due to the inability to specifically identify the values associated with the various intangible assets acquired. The goodwill will be amortized on the straight-line basis over 5 years. Accumulated amortization of goodwill at November 30, 2000 was \$3,678.

NOTE 5: INVENTORY

Inventories at November 30, 2000 are comprised of:

Finished goods	\$440,492
Work in process	135,188
Raw materials and subassemblies	860,152

Total	1,435,832
Less: Allowance	(195,600)

Net total inventories	\$1,240,232

NOTE 6: LONG-TERM EQUITY INVESTMENT - NET

In January 2000, in connection with the formation of PNR America, LLC, a Delaware limited liability company ("PNR America"), the Company invested \$19,600 in PNR America for a 49% ownership interest. Flowtech Srl ("Flowtech"), an Italian pressure nozzle manufacturer, owns the remaining 51%. In August 2000, the Company and Flowtech pledged an additional investment of \$9,800 and \$10,200, respectively, in PNR America, thereby maintaining each's proportional share. On November 30, 2000 the Company made its \$9,800 contribution by decreasing the amount owed to the Company by PNR America.

PNR America was formed to market and sell nozzles imported from Flowtech in the U.S. The PNR America product line compliments the Company's existing business as there are certain basic nozzle properties common to both product lines and capitalizes on the Company's existing relationships with its customers. Prior to the formation of PNR America, the Company had been a U.S. distributor of Flowtech products.

Certain of the Company's officers and directors are also officers and directors of PNR America, however, PNR America's board of directors is controlled by Flowtech. The Company does not control PNR America and it is therefore not consolidated for reporting purposes.

The Company shares its facilities and personnel with PNR America. The Company allocated costs of \$21,438 and \$78,668 to PNR America for the three and nine month periods ended November 30, 2000, respectively, and \$13,967 for the period of inception through February 29, 2000. Balances due from PNR America of \$58,161 and \$13,967 at November 30, 2000 and February 29, 2000, respectively, are expected to be repaid out of PNR America's fiscal year 2001 operating cash flows.

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PNR America's year end is December 31, however, for financial reporting purposes the Company will reflect its proportionate share of the operating results of PNR America on a monthly basis, as the records are compiled by the Company. The Company's cumulative recorded equity loss in PNR America at November 30, 2000 was \$55,442. The Company recognized, during the nine and three month period ended November 30, 2000 and the period from inception to February 29, 2000, \$70,585, \$18,558 and \$14,257, respectively, as its estimate of the proportionate share of the net loss of PNR America. The Company, for financial reporting purposes, has netted the cumulative equity loss in PNR America with the intercompany balances due from PNR America.

The condensed financial information of PNR America as of November 30, 2000 and for the three month period ended November 30, 2000 is as follows:

Net loss-three months ended November 30, 2000	\$ (35,654)
	=====
Net loss-nine months ended November 30, 2000	\$ (144,048)
	=====
Total assets - current	\$91,622
	=====
Due to Sono-Tek	\$72,128
Due to Flowtech	137,087
Accrued Expenses	5,756

Liabilities	214,971
Stockholders' deficiency	(123,49)

Total liabilities and stockholders' deficiency	\$91,622
	=====

Note 7: SHORT TERM LOANS RELATED PARTIES

From time to time the Company has required short-term loans to meet its payment obligations. All of these loans, which are payable on demand, have been provided by certain officers and directors of the Company at an interest rate of prime plus 2% computed at the time of the loan (9.75% to 11.5% at November 30, 2000). As of November 30, 2000 the amount of these loans outstanding was \$302,084. Interest expense for the nine month period and three month period ended November 30, 2000 was \$16,657 and \$7,381, respectively. Accrued interest was \$27,337 and \$13,165 at November 30, 2000 and February 29, 2000, respectively.

NOTE 8: COMMITMENTS AND CONTINGENCIES

On October 1, 2000, the Company entered into a lease agreement for additional production space in Milton, NY. The lease, which terminates November 30, 2002, has an annual rent of \$18,000. The Company has the option to renew the lease for a period of three years after expiration.

NOTE 9. EARNINGS (LOSS) PER SHARE

Basic earnings per share ("EPS") and loss per share ("LPS") are computed by dividing net income (loss) by the weighted-average number of common shares outstanding for the period. Diluted EPS would reflect, if applicable, the potential dilution that could occur if securities or other obligations to issue common stock were exercised or converted into common stock. Stock options granted but not yet exercised under the Company's stock option plans would be included for Diluted EPS calculations, if applicable, under the treasury stock method.

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The computation of basic and diluted (loss) per share are set forth on the following table:

	Nine Months Ended November 30,		Three M No 2000 ----
	2000	1999	2000
Numerator-			
Numerator for basic and diluted earnings (loss) per share	\$(114,816)	\$(31,139)	\$64,022
Denominator:			
Denominator for basic earnings (loss) per share - weighted average shares	8,984,787	7,155,467	9,047,025
Effects of dilutive securities:			
Stock warrants	0*	0*	1,526,483
Stock options for employees, directors and outside consultants	0*	0*	414,140
Denominator for diluted earnings (loss) per share	8,984,787*	7,155,467*	10,987,648

*Stock options and warrants for employees, directors and outside consultants are antidilutive as a result of the net loss and therefore are not considered in the Diluted LPS calculation.

Under the assumption that stock options, warrants and convertible long term loans were not antidilutive as described above, the denominator for Diluted LPS would be 11,234,771 and 9,408,667 weighted average shares for the nine month period at November 30, 2000 and 1999, respectively and 11,340,411 weighted average shares for the three month period at November 30, 1999.

On October 9, 2000, the Board of Directors of the Company granted options to acquire 72,500 shares of common stock to qualified employees of the Company which are exercisable at the fair market value on the date of grant, under the Company's 1993 Stock Incentive Plan, as amended.

NOTE 10: SUBSEQUENT EVENTS

Letter of intent - On May 16, 2000, the Company signed a letter of intent to purchase all the outstanding stock of a corporation to further expand the Company's product base. This letter of intent has expired by its terms and the Company is no longer pursuing the purchase.

Short term loans - related parties - During December 2000, a director of the Company loaned the Company \$20,000 at the fixed rate of 9%, convertible at \$1.00 per share into the Company's common stock.

Subordinated mezzanine debt - During December 2000, the note was increased by \$100,000. If the \$100,000 plus interest is not repaid by March 22, 2001, the scheduled principal payments will increase to \$15,278 per month and a replacement Warrant will be issued for 1,344,444 shares of the Company's common stock.

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

Forward-Looking Statements

Certain statements made in this report may constitute "forward-looking statements" within the meaning of the Federal Securities Laws. Such forward-looking statements include statements regarding the intent, belief or current expectations of the Company and its management and involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors include, among other things, the following: general economic and business conditions; political, regulatory, competitive and technological developments affecting the Company's operations or the demand for its products; timely development and market acceptance of new products; adequacy of financing; capacity additions; and ability to enforce patents.

The Company undertakes no obligation to update publicly any forward-looking statements.

Liquidity and Capital Resources

The Company's working capital decreased \$69,652 from \$22,612 at February 29, 2000 to a working capital deficiency of \$(47,040) at November 30, 2000. The decrease in working capital was primarily a result of a decrease in accounts receivable of \$466,851 that was offset by a decrease in deferred revenue of \$725,491 and increases in accrued expenses of \$219,176 and customer deposits of \$181,396.

The Company's stockholders' equity increased \$155,809 from \$727,630 on February 29, 2000 to \$883,439 on November 30, 1999. Of this increase, \$137,500 was due to the sale of 137,500 shares of common stock through a Private Placement, \$132,242 was due to the exercise of warrants and options that were offset by the \$114,816 loss for the nine months ended November 30, 2000.

During Fiscal Year 2000, the Company entered into an agreement with a Small Business Investment Corporation, Norwood Venture Corporation ("Norwood"), pursuant to which the Company obtained a five-year loan in the principal amount of \$450,000. The terms of the loan require interest payments only for the first two years followed by monthly payments of \$12,500 plus interest through September 30, 2004. The Company also granted Norwood a warrant to purchase 1,100,000 shares of the Company's common stock which can be put to the Company. Such warrants were valued at \$77,000 which is accounted for as a discount and will be imputed as additional interest expense over the term of the loan.

The Company currently has a \$350,000 line of credit with a bank. The loan is collateralized by accounts receivable, inventory and all other personal property of the Company and is guaranteed by the Chairman and CEO of the Company. As of November 30, 2000 the outstanding balance was \$350,000.

Due to losses incurred during Fiscal Years 2000 and 1999, the Company has borrowed on a short-term basis from officers and directors. As of November 30, 2000 the balance owed these officers and directors was \$302,084.

Although there can be no assurances, management believes that its current backlog of orders and continued sales and expanding markets for its products will lead to increases in profits. These factors, and the anticipated success of PNR America, should allow the Company to meet its current obligations as they become due.

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Results of Operations

The Company's sales increased \$2,614,704 from \$3,660,200 for the nine months ended November 30, 1999 to \$6,274,904 for the nine months ended November 30, 2000. The increase was due to an increase in SCS sales of \$2,310,100, increased sales of the SonoFlux System of \$609,948, that were offset by a decrease in nozzle and liquid delivery sales of \$107,657.

The Company's sales increased \$429,149 from \$1,551,772 for the three months ended November 30, 1999 to \$1,980,921 for the three months ended November 30, 2000. The increase was due to \$274,710 in sales attributable to SCS, increased sales of the SonoFlux System of \$109,084, MCSoInfinity and AccuMistoSystems of \$163,673, that were offset by a decrease in nozzle and liquid delivery sales of \$68,918.

Gross profit increased \$732,035 from \$1,934,133 for the nine-month period ended November 30, 1999 to \$2,666,168 for the nine-month period ended November 30, 2000. The increase in gross profit is due to the increase in sales that was offset by increases in personnel costs of \$607,175, service travel of \$135,651 and warranty expense of \$75,314.

The Company's gross profit increased \$144,261 from \$812,249 for the three months ended November 30, 1999 to \$956,510 for the three months ended November 30, 2000. The increase in gross profit is due to the increase in sales that was offset by increases in personnel costs of \$89,627, service travel of \$45,899 and warranty expense of \$19,922.

The gross profit was 42% and 53% of sales for the nine month period ending November 30, 2000 and 1999, respectively. The gross profit was 48% and 52% of sales for the three month period ending November 30, 2000 and 1999, respectively. For both the three and nine month periods the decrease in the Company's gross profit was primarily a result of increased sales of the Company's products with lower profit margins.

Research and product development costs increased \$257,625 from \$430,068 for the nine months ended November 30, 1999 to \$687,693 for the nine months ended November 30, 2000. Research and product development costs increased \$47,346 from \$170,712 for the three months ended November 30, 1999 to \$218,058 for the three months ended November 30, 2000. For both the three and nine month periods, the increase in the Company's research and product development costs was a result of increased compensation and rent expense resulting from a larger engineering staff and travel costs associated with new products for SCS.

Marketing and selling costs increased \$320,708 from \$787,757 for the nine months ended November 30, 1999 to \$1,108,465 for the nine months ended November 30, 2000. The increase was a result of increased sales commissions and additional sales personnel that totaled \$236,312 and increased marketing expenses of \$25,030.

Marketing and selling costs increased \$60,130 from \$303,061 for the three months ended November 30, 1999 to \$363,191 for the three months ended November 30, 2000. The increase was a result of additional commissions of \$118,707 that were offset by decreases in personnel costs of \$15,623, travel costs of \$11,471 and marketing costs of \$23,899.

General and administrative costs increased \$99,409 from \$591,840 for the nine month period ended November 30, 1999 to \$691,249 for the nine month period ended November 30, 2000. The increase was due to increases in professional and consulting fees of \$128,817 plus goodwill and deferred financing amortization of \$44,232 that were offset by a decrease in personnel costs of \$58,929.

General and administrative costs decreased \$57,881 from \$300,986 for the three

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month period ended November 30, 1999 to \$243,105 for the three month period ended November 30, 2000. The decrease was due to increases in professional and consulting fees of \$45,758 that were offset by decreased personnel costs of \$81,313.

Interest expense increased \$63,178 from \$167,587 for the nine month period ended November 30, 1999 to \$230,765 for the nine months ended November 30, 2000. Interest expense increased \$14,852 from \$38,550 for the three month period ended November 30, 1999 to \$53,402 for the three months ended November 30, 2000. The increase is primarily due to an increase in interest costs associated with the addition of SCS and Norwood loan interest and new equipment loans from the bank.

For the nine months ended November 30, 2000 the Company had a net loss of \$114,816 or \$(0.01) per share as compared to a net loss of \$31,139 or \$(0.00) per share for the nine months ended November 30, 1999.

For the three months ended November 30, 2000 the Company had a net income of \$64,022 or \$0.01 per share as compared to a net loss of \$1,648 or \$(0.00) per share for the three months ended November 30, 1999.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to market risk related to changes in interest rates. The interest rate on the Company's debt is based on fluctuations in the prime rates. If the prime rate increased by 1 percentage point from the levels at February 29, 2000, the negative effect on the Company's results of operations would approximate \$1,300 for the quarter ended November 30, 2000 and \$3,500 for the nine months ended November 30, 2000.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings
None

Item 2. Changes in Securities and Use of Proceeds
None

Item 3. Defaults on Senior Securities
None

Item 4. Submission of Matters to a Vote of Security Holders
None

Item 5. Other Information
None

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

Exhibit No.	Description
3(d)	Restated Certificate of Incorporation
10(g)	Lease for the Company's facilities in Milton, NY dated September 29, 2000

(b) Reports on Form 8-K
None

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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.

Dated: January 16, 2001

SONO-TEK CORPORATION
(Registrant)

By: /s/ James L. Kehoe
James L. Kehoe
Chief Executive Officer

By: /s/ Kathleen N. Martin
Kathleen N. Martin
Chief Financial Officer

Exhibit 3(d)

CERTIFICATE OF INCORPORATION OF
SONO-TEK CORPORATION

Under Section 402 of the business Corporation Law

IT IS HEREBY CERTIFIED THAT:

(1) The name of the proposed corporation is:

SONO-TEK CORPORATION

(2) The purpose or purposes for which this corporation is formed, are as follows, to wit:

To engage in the business of manufacturing, designing, creating, compounding, developing, formulating, investing, patenting, owning, acquiring, producing, processing, constructing, storing, applying, assembling, adapting, conducting, operating, using, preparing for market, exhibiting, distributing, installing, buying, selling, disposing, leasing, renting, mortgaging, exploiting, licensing, exchanging, reconstructing, repairing, importing, exporting and generally dealing in and with household and industrial fuel combustion systems including but not limited to all kinds of burners, furnaces, fuel atomizers, stoves, boilers, engines, fuel delivery systems, heating devices, lighting devices, refrigerating devices, devices for producing and furnishing gases, heat, light, cold, power, or electricity, and all other kinds of mechanical and electrical machines, devices, and appliances, and all kinds of materials, supplies, accessories, equipment, devices or other things used for

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any of the foregoing, or in any other way thereto relating, and any and all other kinds of machinery, appliances, device, supplies and articles.

To acquire such property, real and personal, as may be necessary to the conduct of such business.

The powers, rights and privileges provided in this Certificate of Incorporation are not to be deemed to be in limitation of similar, other, or additional powers, rights and privileges granted or permitted to a corporation by the Business Corporation Law, it being intended that this Corporation shall have the right to engage in such similar activities as like corporations may lawfully engage in under the Business Corporation Law of the State of New York, as now in effect, or as hereafter promulgated.

To do everything necessary, suitable or proper for the accomplishment, attainment or furtherance of, to do every other act or thing incidental to, appurtenant to, growing out of or connected with, the purposes, objects or powers set forth in this Certificate of Incorporation, whether alone or in association with others, to possess all the rights, powers and privileges now or hereafter conferred by the laws of the State of New York upon a corporation organized under the laws of the State of New York and, in general, to carry on any of the activities and to do any of the things herein set forth to the same extent and as fully as a natural person or partnership might or could do; provided, that nothing herein set forth shall be construed as authorizing the Corporation to possess any purpose, object or power, or to do any act or thing forbidden by law to a Corporation organized under the laws of the State of New York.

- (3) The office of the Corporation is to be located in the Town of Milton, County of Ulster, State of New York.
- (4) The aggregate number of shares of all classes which the Corporation shall have authority to issue is twenty-five million (25,000,000) common shares, par value \$0.01 per share. No holder of any share of the Corporation shall, because of his ownership of shares, have a pre-emptive or other right to purchase, subscribe for, or take any part of any shares or any part of any notes, debentures, bonds, or other securities convertible into or carrying options or warrants to purchase shares of the Corporation issued, optioned or sold by the Corporation.
- (5) The Secretary of State is designated as agent of the corporation upon whom process against it may be served. The post office address to which the Secretary of State shall mail a copy of any process against the Corporation served upon him is c/o Sono-Tek Corporation 2012 Route 9W, Building 3 Milton, New York 12547
- (6) The Corporation may, to the fullest extent permitted by Sections 721 through 726 of the Business Corporation Law of New York, indemnify any and all directors and officers whom it shall have power to indemnify under the said Sections from and against any and all of the expenses, liabilities or other matters referred to in or covered by such sections, and the indemnification provided for herein shall not be deemed exclusive of any other rights to which the persons so indemnified may be entitled under any By-law, agreement, vote of shareholders or disinterested directors or otherwise, both as to action in his official capacity and as to action in another capacity by holding such office, and shall continue as a person who has ceased to be a director or officer and shall inure to the benefit of the heirs, executors and administrators of such a person.
- (7) No director of the Corporation shall be personally liable to the Corporation or shareholders for damages for any breach of duty as a director; provided that this Article (7) shall neither eliminate nor limit liability: (a) if a

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judgment or other final adjudication adverse to such director establishes that his or her acts or omissions were in bad faith or involved intentional misconduct or a knowing violation of law or that he or she personally gained in fact a financial profit or other advantage to which he or she was not legally entitled or that his or her acts violated Section 719 of the Business Corporation law; or (b) for any act or omission prior to the effectiveness of this Article (7). Any repeal or any modification to the provisions of this Article (7) shall not adversely affect any right or protection of a director of the Corporation existing pursuant to this Article (7) immediately prior to such repeal or modification.

- (8) The business of the Corporation shall be managed under the direction of a Board of Directors in accordance with the following:
- (a) The Board shall consist of six directors, unless and until otherwise determined by vote of a majority of the entire board of directors (whether or not there exist any vacancies in previously authorized directorships at the time such resolution is presented to the Board for adoption).
 - (b) The directors shall be divided into two classes, designated Class I and Class II. All classes shall be as nearly equal in number as possible, and no class shall include less than three directors. The terms of office of the directors initially classified shall be as follows: at the 1989 annual meeting of shareholders, Class I directors shall be elected for a one year term expiring at the next annual meeting of shareholders and Class II directors for a two year term expiring at the second succeeding annual meeting of shareholders. At each annual meeting of shareholders after such initial classification, directors to replace those whose terms expire at such annual meeting shall be elected to hold office until the second succeeding annual meeting. Each director shall hold office until the expiration of his term and until his successor is elected and qualified or until his earlier death, resignation or removal.
 - (c) A director elected to fill a vacancy shall be elected to hold office for a term expiring at the next meeting of shareholders at which the election of directors is in the regular order of business and until his successor has been elected and qualified.
 - (d) If the number of directors is changed, (1) any newly created directorships or any decrease in directorships shall be so apportioned among the classes as to make all classes as nearly equal in number as possible; and (2) when the number of directors is increased by the Board and any newly created directorships are filled by the Board, there shall be no classification of the additional directors until the next annual meeting of shareholders.
 - (e) Newly created directorships resulting from an increase in the number of directors and vacancies occurring in the Board for any reason may be filled only by vote of the Board. If the number of directors then in office is less than a quorum, such newly created directorships and vacancies may be filled by a majority of the directors then in office.
 - (f) Any director may be removed for cause by action of the Board. Any director may also be removed for cause (but not without cause) by the affirmative vote of the holders of at least two-thirds of the outstanding shares entitled to vote thereon.

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- (g) The provisions of this Article (8) may be altered, amended or repealed, and any provision inconsistent herewith may be adopted, only by the affirmative vote of the holders of at least two-thirds of the outstanding shares entitled to vote thereon.

The undersigned incorporator is of the age of eighteen years or over.

IN WITNESS WHEREOF, this certificate has been subscribed this 21st day of March, 1975 by the undersigned who affirms that the statements made herein are true under penalties of perjury.

Exhibit 10(a)

LEASE

LEASE MADE THIS 29th DAY OF September, 2000

BETWEEN Jean K. Woodward, owner, as may be represented by William Woodward (William Woodward Enterprises) residing at 50 Riverview Drive, Marlboro, New York 12542-5310 herein referred to as Lessor,

AND Sono-Tek Corporation, having it's principal place of business at 2012 Route 9-W, Milton Industrial Park, Milton, New York 12547, herein referred to as Lessee.

RECITALS:

- 1: Lessor is the sole owner of the premises described below and desires to lease the premises to a suitable Lessee for business purposes.
- 2: Lessee desires to lease the premises for the purpose of conducting a business of light manufacturing, electronics and related machinery and equipment.
- 3: The parties desire to enter a lease agreement defining their rights, duties and liabilities relating to the premises.

In consideration of the mutual covenants contained herein, the parties agree as follows:

I. SUBJECT AND PURPOSES:

Lessor leases a portion of the building known as Phase I, Building 1, in the Milton Industrial Park, in the County of Ulster, State of New York and more particularly described as follows:

Approximately 4,200 square feet of space located adjacent to the SonoTek existing facilities containing a separate electric meter, gas meter, bathroom, small office and one drive-in overhead door.

II. TERM AND RENT:

Lessor demises the above premises for a term of two (2) Years and two (2) months, commencing October 1, 2000 and terminating on November 30, 2002 at five o'clock P.M., or sooner as provided herein, at the annual rental of Eighteen Thousand Dollars (\$18,000.00) or proportioned thereof..

Such sums are payable in advance on October first for the first year and on the anniversary date for each succeeding year. However and provided the lessee is not otherwise in default, the lessee for convenience and with the consent of the lessor may pay such annual rent in equal monthly installments of OneThousand Five Hundred Dollars (\$1,500.00) in advance on the first day of each month for that month's rental, during the term of this lease. All rental payments shall be made to Lessor at the address specified above. Lessee shall

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pay the rent as specified herein and in Section Three hereof.

III. ADDITIONAL RENT:

All taxes, charges, costs, and expenses that Lessee assumes or agrees to pay hereunder, together with all interest and penalties that may accrue thereon in the event of the failure of Lessee to pay those items, and all other damages, costs, expenses, and sums that Lessor may suffer or incur, or that may become due by reason of any default of Lessee or failure by Lessee to comply with the terms and conditions of this lease shall be deemed to be additional rent, and, in the event of nonpayment, lessor shall have all the rights and remedies as herein provided for failure to pay rent.

IV. UTILITIES NOT FURNISHED BY LESSOR - ENTIRE RESPONSIBILITY OF LESSEE:

Lessee shall initiate, contract for, and obtain, in its name, electric, natural gas, and telephone utility services as required on the demised premises.

Lessee shall indemnify and hold harmless lessor from any claims whatsoever arising out of lessee's failure to pay for utility services and/or the charges therefor. Lessee shall pay Lessor's attorney's fees arising out of any claims against Lessor arising out of charges for Lessee's utility services.

Except in the case of acts of negligence committed by Lessor, Lessor shall not be liable for any personal injury or property damage resulting from the negligent operation or faulty installation of utility services provided for use on the demised premises, nor shall Lessor be liable for any injury or damage suffered by lessee as a result of the failure to make necessary repairs to the utility facilities.

Lessee shall be liable for any injury or damages to the equipment of service lines of the utility suppliers that are located on the demised premises, resulting from the negligent or deliberate acts of lessee, or the agents or employees of lessee.

V. BROKERS COMMISSION:

There is no Broaker's Commission payable or due from either the Lessor or the Lessee.

VI. IMPROVEMENTS TO BE MADE TO PREMISES:

Lessee shall make the following improvements to the premises: Install access from the existing rental space into the new rental spacethrough a common wall area as located and type of materials approved by the lessor.

The above improvements shall be at the direction of Sono-Tek Corporation and completed no later than January 1, 2001. The above improvements shall be subject to the provisions of paragraph VII.

VII: ALTERATIONS, ADDITIONS AND IMPROVEMENTS:

1. Subject to the limitation that no portion of the building on the demised premises shall be demolished or removed by Lessee without the prior written consent of Lessor, and , if necessary, of any mortgagee. Lessee may at any time during the lease term subject to the conditions set forth below and at his own expense, make alterations, additions, or improvements in and to the demised premisses and the building. Alterations shall be performed in a workmanlike manner and shall not weaken or impair the structural strength, or lessen the value, of the building on the premises, or change the purposes for which the building, or any pert thereof, may be used.
2. Conditions with respect to alterations, additions or improvements are as follows:

1. Before commencement of any work all plans and specifications shall be filed with and approved by all governmental departments or authorities having jurisdiction and any public utility company having an interest therein, and all work shall be done in accordance with requirements of local regulations. The plans and

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specifications of any alterations shall be submitted to the Lessor for written approval prior to commencing work. Said approval not to be unreasonably withheld. . The lessee shall have the right to install one identification sign at the main entrance to the demised premises. Such sign shall not violate local building codes. At the end of the term of this lease the lessee shall at the option of lessor remove such alterations as are designated by lessor.

2. Prior to commencement of any work Lessee shall pay the amount of any increase in premiums on insurance policies provided for herein because of endorsements to be made covering the risk during the course of work. 1.
3. Alterations, additions and improvements on or in the demised premises may commence upon the signing of this agreement. All additions and improvements that may be erected or installed prior to or during the term, shall become part of the demised premises and the sole property of Lessor, except that all movable trade fixtures, and a modular Class 100 clean room if installed by lessee shall be and remain the property of Lessee.

VIII. TAXES AND OTHER CHARGES:

Lessor shall pay and discharge when due all state, municipal and local real estate taxes, inheritance, succession and , assessments, levies and other charges, general and special, ordinary and extraordinary, of whatever name, nature and kind that are or may be during the term hereof or any renewal, beginning with the fiscal year 2000, levied, assessed, imposed or charged on the land or the premises hereby demised or on the (building or buildings) and improvements now thereon or hereafter to be built or made thereon, and all of which may be levied, assessed, imposed or charged on or against the leasehold estate hereby created and on the reversionary estate in the demised premises during the term hereof or any renewal.

If at any time during the term of this lease, the present method of taxation or assessment should be changed so that the whole or any part of the taxes, assessments, levies or charges now levied, assessed or imposed on the real estate hereby demised and improvements thereon, shall be transferred to the rentals received from such real estate, lessee shall pay such proportionate share of taxes and assessments levied and assessed on such rentals as shall proportionately relieve the taxes and assessments on such real estate, it being the intent of the parties hereto that lessor shall receive the rents reserved herein with deduction of taxes (except gift, estate, inheritance, succession and income taxes on the interest of lessor), assessments levies or charges in respect to the real estate and improvements thereon, but that lessee shall not be obligated to pay full taxes and assessments on such real estate and improvements and also on such rentals.

IX. REPAIRS:

Lessee shall, at all times during the lease and at his own cost and expense, repair, replace and maintain in good, safe and substantial condition, all buildings and any improvements, additions, and alterations on the demised premises, and shall use all reasonable precaution to prevent waste, damage or injury to the demised premises. It is intended that this clause refers to non-structural repairs, unless structural repairs are necessitated by the conduct of lessee, its agents or assigns. In such case, lessee shall be responsible for structural repairs.

Lessor shall maintain the building exterior, lawn and landscaping. Lessor shall be responsible for snow removal, and grounds cleaning. Lessor shall replace all shrubs to the property which have died.

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Lessee shall remove snow and debris from walkways and in front of doors.. Lessee shall be responsible for office cleaning, window cleaning, refuse removal, maintenance of light fixtures, bi-annual service of heating and air condition equipment, and to maintain all plumbing fixtures against leaks and water wasting.

X. SECURITY DEPOSIT:

Lessee shall deposit No Money with lessor upon the signing here of for the purposes of a security deposit.

XI. INSURANCE:

1. In the term of the lease and for any further time that Lessee shall hold the demised premises, Lessee shall obtain and maintain at his expense the following types and mounts of insurance: Personal Injury and Property Damage Insurance. Insurance against liability for bodily injury and property damage in the sum of Two Million Dollars (\$2,000,000.00) per claimant and in the sum of Five Million Dollars (\$5,000,000.00) per occurrence.
2. All insurance provided by Lessee as required by this section shall be carried in favor of Lessor and Lessee as their respective interests may appear, and in the case of insurance against damage to the demised premises by fire and other casualty, shall provide that loss, if any, shall be adjusted with and be payable to Lessor. If required by Lessor, any insurance against fire or other casualty shall provide that loss shall be payable to the holder under a standard mortgage clause. Rent insurance and the proceeds are hereby assigned to lessor to be held by Lessor as security for the payment of the rent and any additional rent hereunder until restoration of the premises. All insurance shall be written with responsible companies that Lessor shall approve, and the policies shall be held by lessor, or when appropriate, by the holder of any mortgage in which case copies of the policies or certificates of insurance shall be delivered by Lessee to Lessor. All policies shall require 30 days notice by registered mail to Lessor of any cancellation or change affecting any interest of Lessor.

XII. UNLAWFUL OR DANGEROUS ACTIVITY:

Lessee shall neither use nor occupy the demised premises or any part thereof for any unlawful, disreputable or ultra hazardous business purpose nor operate or conduct his business in a manner constituting a nuisance of any kind. Lessee shall immediately, on discovery of any unlawful, disreputable or ultra hazardous use, take action to halt such activity and keep such premises environmentally clean and safe.

XIII. DEFAULT OR BREACH:

Each of the following events shall constitute a default or breach of this lease by Lessee:

1. If Lessee, or any successor or assignee of Lessee while in possession, shall file a petition in bankruptcy or insolvency or for reorganization under any bankruptcy act, or shall voluntarily take advantage of any such act by answer or otherwise, or shall make an assignment fo the benefit of creditors.
2. If involuntary proceedings under any bankruptcy law or insolvency act shall be institute against Lessee, or if a receiver or trustee shall be appointed of all or substantially all of the property of Lessee, and such proceedings shall not be dismissed or the receivership or trusteeship vacated within

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- 20 days after the institution or appointment.
3. If Lessee shall fail to pay Lessor any rent owed or additional rent when the rent shall become due within five days after written notice of such failure to lessee at the address above given. Lessee shall pay as additional rent the sum of \$300.00. If such rent is not received on or before the 1st day of the month and lessor sends such written notice of default. Lessor shall extend to lessee, a five (5) day grace period relative to such rent payment.
 4. If lessee shall fail to perform or comply with any of the conditions of this lease and if the nonperformance shall continue for a period of 10 days after notice thereof by Lessor to Lessee or, if the performance cannot be reasonably had within the 10 day period, Lessee shall not in good faith have commenced performance within the 10 day period and shall not diligently proceed to completion of performance.
 5. If this lease or the estate of Lessee hereunder shall be transferred to or shall pass to or devolve on any other person or party, except in the manner herein permitted.
 6. If Lessee fails to take possession of the demised premises on the term commencement date, or within 10 days after notice that the demised premises are available for occupancy, if the term commencement date is not fixed herein or shall be deferred as herein provided.

XIV. EFFECT OF DEFAULT:

In the event of any default hereunder, as set forth in Section I, the rights of Lessor shall be as follows:

1. Lessor shall have the right to cancel and terminate this lease, as well as all of the right, title and interest of lessee hereunder, by giving to lessee not less than 10 days notice of the cancellation and termination. On expiration of the time fixed in the notice; this lease and the right, title and interest of lessee hereunder, shall terminate in the same manner and with the same force and effect, except as to lessee's liability, as if the date fixed in the notice of cancellation and termination were the end of the term cancellation and termination were the end of the term herein originally determined.
2. Lessor may elect, but shall not be obligated to make any payment required by lessee herein or comply with any agreement, term or condition required hereby to be performed by Lessee, and the lessor shall have the right to enter the demised premises for the purpose of correcting or remedying any such default and to remain until the default has been corrected or remedied, but any expenditure for the correction by lessor shall not be deemed to waive or release the default of lessee or the right of lessor to take any action as may be other wise permissible hereunder in the case of any default.
3. Lessor may re-enter the premises immediately and remove the property and personnel of lessee, and store the property in a public warehouse or at a place selected by lessor, at the expense of lessee. After re-entry lessor may terminate the lease on giving 10 days written notice of termination to lessee. Without the notice, re-entry will not terminate the lease. On termination, the lessor may recover from lessee all damages proximately resulting from the breach, including the costs recovering the premises, and the present worth of the balance of this lease over the present worth of the reasonable rental value of the premises for the remainder of the lease

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4. term, which sum shall be immediately due lessor from lessee. After re-entry, lessor may relet the premises or any part thereof for any term without terminating the lease, at the rent and on the terms as lessor may choose. Lessor may make alterations and repairs to the premises. The duties and liabilities of the parties if the premises are relet as provided herein shall be as follows:
- a. In addition to lessee's liability to lessor for breach of the lease, lessee shall be liable for all expenses of the reletting, for the alterations and repairs made, and for the difference between the rent received by lessor under the new lease agreement and the rent installments that are due for the same period under this lease.
- b. Lessor shall have the right, but shall not be required, to apply the rent received from the reletting for the premises (1) to reduce the indebtedness of lessee to lessor under the lease, not including indebtedness for rent, (2) to expenses of the reletting and alterations and repairs made, (3) to rent due under this lease, or (4) to payment of future rent under this lease as it becomes due.
- If the new lessee does not pay a rent installment promptly to lessor, and the rent installment has been credited in advance of payment to the indebtedness of lessee other than rent, or if rentals from the new lessee have been otherwise applied by Lessor as provided for herein and during any rent installment period are less than the rent payable for the corresponding installment period under this lease, lessee shall pay lessor the deficiency, separately for each rent installment deficiency period, and before the end of that period. Lessor may at any time after a reletting terminate the lease for the breach on which lessor had based the re-entry and subsequently relet the premises.
5. After re-entry, lessor may procure the appointment of a receiver to take possession and collect rents and profits of the business of lessee, and, if necessary to collect the rents and profits. The receiver may take possession of the personal property used in the business of lessee, including inventory, trade fixtures, and furnishings, and use them in the business without compensating lessee. Proceedings for appointment of a receiver by lessor, or the appointment of a receiver, shall not terminate and forfeit this lease unless lessor has given written notice of termination to lessee as provided herein.

XV. CONDEMNATION:

Rights and duties in the event of condemnation are as follows:

1. If the whole of the demised premises shall be taken or condemned by any public, or quasi-public use or purpose, this lease shall cease and terminate as of the date on which title shall vest thereby in that authority, and the rent reserved hereunder shall be apportioned and paid up to that date.
2. .If only a portion of the demised premises shall be taken or condemned, this lease and the terms hereof shall not cease or terminate, but the rent payable after the date on which lessee shall be required to surrender possession of such portion shall be reduced in proportion to the decreased use suffered by lessee as the parties may agree or as shall be determined by arbitration.
3. In the event of any taking or condemnation in whole or in part, the entire resulting award of consequential damages shall belong to lessor without any deduction therefrom for the value of the unexpired term of this lease or for any other

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estate or interest in the demised premises now or later vested in lessee. Lessee assigns to lessor all his right, title and interest in any and all such awards. If a separate award is made for moving expenses, business interruption and fixtures then such award of moving expenses, business interruption and fixtures shall belong to the lessee.

4. In the event of a partial taking, lessor shall promptly proceed to restore the remainder of the building on the demised premises to a self-contained architectural unit.
5. In case of any governmental action not resulting in the taking or condemnation of any portion of the demised premises but creating a right to compensation therefor, or if less than a fee title to all or any portion of the demised premises shall be taken or condemned by any governmental authority for temporary use of occupancy, this lease shall continue in full force and effect without reduction or abatement of rent, and the rights of the parties shall be unaffected by the other provisions of this section, but shall be governed by applicable law.

XVI. DESTRUCTION OF PREMISES:

In the event of a partial destruction of the premises (not caused by lessee and/or its' agents and/or independent contractors) by fire or other cause for which lessee has provided insurance payable to lessor under paragraph XIII or condemnation during the term, lessor shall forth with repair the same, provided the repairs can be made within 30 days of receipt of such insurance or governmental authorities. Any partial destruction shall neither annul nor void this lease. If the repairs cannot be made in the specified time, lessor may, at lessor's option, make repairs within a reasonable time, this lease continuing in full force and effect and the rent to be proportionately rebated. In the event that lessor does not elect to make repairs that cannot be made in the specified time, or those repairs cannot be made under the laws and regulations of the applicable governmental authorities, this lease may be terminated at the option of either party. Should the building in which the demised premises are situated be destroyed as set forth herein or condemned to the extent of not less than 75 percent (75%) of the replacement cost thereof, this lease shall be terminated.

XVII. SUBORDINATION:

This lease and all rights of lessee hereunder shall be subject and subordinate to the lien of any and all mortgages that may now or hereafter affect the demised premises, or any part thereof, and to any and all renewals, modifications or extensions of any such mortgages. Lessee shall on demand execute, acknowledge and deliver to lessor, without expense to lessor, any and all instruments that may be necessary or proper to subordinate this lease and all rights therein to the lien of any such mortgage or mortgages and each renewal, modification or extension, and if lessee shall fail at any time to execute, acknowledge and deliver any such subordination instrument, lessor in addition to any other remedies available in consequence thereof, may execute, acknowledge and deliver the same as lessee's attorney in fact and in lessee's name. Lessee hereby irrevocably makes, constitutes and appoints lessor, its successors and assigns, his attorney in fact for that purpose.

Lessor hereby covenants and warrants that, subject to Section XVIII, he is owner of the demised premises and that lessee, on payment

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of the rents herein provided for and the performance of the provisions hereof on its part to be performed, shall and may peacefully possess and enjoy the demised premises during the term hereof without any interruption or disturbance.

XVIII. ACCESS TO PREMISES; SIGNS POSTED BY LESSOR:

Lessee shall permit lessor or its agents to enter the demised premises at all reasonable hours to inspect the premises or make repairs that lessee may neglect or refuse to make in accordance with the provisions of this lease, and also to show the premises to prospective buyers. At any time within one year prior to expiration of the term, lessor may show the premises to persons prior to expiration of the term, permit the usual notices of "For Rent" and "For Sale" to be placed on the demised premises and to remain thereon without hindrance and molestation.

XIX. EASEMENTS, AGREEMENTS OR ENCUMBRANCES:

The parties shall be bound by all existing easements, agreements and encumbrances of record relating to the demised premises, and lessor shall not be liable to lessee for any damages resulting from any action taken by a holder of an interest pursuant to the rights of that holder thereunder.

XX. LIABILITY OF LESSOR:

Lessee shall be in exclusive control and possession of the demised premises, and lessor (except for acts of negligence of lessor) shall not be liable for any injury or damages to any property or to any person on or about the demised premises nor for any injury to any property of lessee. The provisions herein permitting lessor to enter and inspect the demised premises are made to insure that lessee is in compliance with the terms and conditions hereof and makes repairs that lessee has failed to make. Lessor shall not be liable to lessee for any entry on the premises for inspection purposes (except for acts of negligence of Lessor).

XXI. RENT ABATEMENT:

No abatement, diminution or reduction of rent shall be claimed or allowed to lessee or any person claiming under him under any circumstances, whether for inconvenience, discomfort, interruption of business or otherwise, arising from and during the restoration of the demised premises after the destruction or damage thereof by fire or other cause or the taking or condemnation of a portion only of the demised premises.

XXII. STORAGE OF TOXIC MATERIALS, EXPLOSIVES AND FLAMMABLES PROHIBITED:

Lessee shall not, at anytime whatsoever, keep for use on the demised premises any toxic materials, explosives or inflammable substances.

XXIII. REPRESENTATIONS BY LESSOR:

At the commencement of the term lessee shall accept the buildings and improvements and any equipment in their existing condition and state of repair and lessee agrees that no representations, statements or warranties, express or implied, have been made by or on behalf of lessor in respect thereto except as contained in the provisions of this lease.

XXIV. WAIVERS:

The failure of lessor to insist on a strict performance of any of the terms and conditions hereof shall be deemed a waiver of the rights or remedies that lessor may have regarding that specific instance only, and shall not be deemed a waiver of any subsequent

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breach or default in any terms and conditions.

XXV. NOTICE:

All notices to be given with respect to this lease shall be in writing. Each notice shall be sent by registered or certified mail, postage prepaid and return receipt requested, to the party to be notified at the address set forth herein or at such other address as either party may from time to time designate in writing.

Every notice shall be deemed to have been given at the time it shall be deposited in the United States mails in the manner prescribed herein. Nothing contained herein shall be construed to preclude personal service of a summons or other legal process.

XXVI. ASSIGNMENT, MORTGAGE OR SUBLEASE:

Neither lessee nor his successors or assigns shall assign, mortgage, pledge or encumber this lease or sublet the demised premises in whole or in part, or permit the premises to be used or occupied by others, nor shall this lease be assigned or transferred by operation of law, without the prior consent in writing of lessor in each instance. Exception to this would be legal subsidiaries of lessee. After two years such consent is not to be unreasonably withheld. If this lease is assigned or transferred, or if all or any part of the demised premises is sublet or occupied by anybody other than lessee, lessor may, after default by lessee, collect rent from the assignee, transferee, subtenant, or occupant, and apply the net amount collected to the rent reserved herein, but no such assignment, subletting, occupancy or collection shall be deemed a waiver of any agreement or condition hereof, or the acceptance of the assignee, transferee, subtenant or occupant as lessee. Lessee shall continue to be liable hereunder in accordance with the terms and conditions of this lease and shall not be released from the performance of the terms and conditions hereof. The consent by lessor to an assignment, mortgage, pledge or transfer shall not be construed to relieve lessee from obtaining the express written consent of lessor to any future transfer of interest.

XXVII. OPTION TO RENEW:

Lessor grants to lessee an option to renew this lease for a period of Three (3) years after expiration of the term of this lease. The rental rate shall be increased an amount equal to the Consumer Price Index (CPI) as noted for New York and area, each year of the renewal. All other terms and condition of this renewal lease to be the same as those herein. To exercise this option, lessee must give lessor written notice of the intention to do so at least six (6) months before this lease expires.

XXVIII. SURRENDER OF POSSESSION:

Lessee shall, on the last day of the term, or on earlier termination and forfeiture of the lease, peaceably and quietly surrender and deliver the demised premises to lessor free of subtenancies, including all buildings, additions and improvements constructed or placed thereon by lessee, except moveable trade fixtures, all in good condition and repair subject to reasonable wear and tear (except to the extent provided for under paragraph XI, and XVI herein. Any trade fixtures or personal property not used in connection with the operation of the demised premises and belonging to Lessee, if not removed at the termination of default, and if lessor shall so elect, shall be deemed abandoned and become the property of lessor without any payment or offset therefor. Lessor may remove such fixtures or property from the demised premises and store them at the risk and expense of lessee if lessor shall not so elect. Lessee shall repair and restore all damage to the demised premises caused by the removal of equipment, trade fixtures and personal property.

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XXIX. REMEDIES OF LESSOR:

- A. In the event of a breach or a threatened breach by lessee of any of the terms or conditions hereof, lessor shall have the right of injunction to restrain lessee and the right to invoke any remedy allowed by law or in equity, as if the specific remedies of indemnity or reimbursements were not provided herein.
- B. The rights and remedies given to lessor in this lease are distinct, separate and cumulative and no one of them, whether or not exercised by lessor, shall be deemed to be in exclusion of any of the others herein, by law, or by equity provided.
- C. In all cases hereunder, and in any suit, action or proceeding of any kind between the parties, it shall be presumptive evidence of the fact of the existence of a charge being due if lessor shall produce a bill, notice or certificate of any public official entitled to give that notice to the effect that such charge appears of record on the books in his office and has not been paid.
- D. No receipt of money by lessor from lessee after default or cancellation of this lease in any lawful manner shall (1) reinstate, continue or extend the term or affect any notice given to lessee, (2) operated as a waiver of the right of lessor to enforce the payment of rent and additional rent then due or falling due, or (3) operated as a waiver of the right of lessor to recover possession of the demised premises by proper suit, action, proceeding or other remedy. After (1) service of notice of termination and forfeiture as herein provided and the expiration of the time specified therein (2) the commencement of any suit, action, proceeding or other remedy, or (3) final order or judgement for possession of the monies due, without in any manner affecting such notice, order or judgement. Any and all such monies so collected shall be deemed to be payment on account of the use and occupation of the demised premises or at the election of lessor, on account of the liability of lessee hereunder.

XXX. TOTAL AGREEMENT; APPLICABLE TO SUCCESSORS:

This lease contains the entire agreement between the parties and cannot be changed to terminated except by a written instrument subsequently executed by the parties hereto. This lease and the terms and conditions hereof apply to and are binding on the heirs, legal representatives, successors and assigns of both parties.

XXXI. INDEMNIFICATION - LIABILITIES AND LOSSES:

Lessee shall, at all times prior to the termination of this lease and to the delivery to a lessor possession of the demised premises and all improvements thereon, indemnify lessor against all liability, loss, cost, damage or expense sustained by lessor, including attorney's fees and other expenses of litigation arising prior to termination of the lease term and delivery to lessor of possession of the premises:

1. On account of or through the use of the demised premises or improvements or any part thereof or by any other reason for any purpose inconsistent with the provisions of this lease.
2. Arising out of, or directly or indirectly due to, any failure of lessee in any respect promptly and faithfully to satisfy his obligations under this lease.
3. Arising out of, or directly or indirectly due to, any accident or other occurrence causing injury to any person or persons or property resulting from the use of the demised premises and improvements or any part thereof.
4. For which the demised premises and improvements or any part thereof or the lessor as owner thereof or interested therein may hereafter without fault by lessor become liable, and especially, but not exclusively, any such liability, loss, cost, damage or expense that may arise under any statute, ordinance or regulation except such requirements as to which compliance is

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related to the improvements on the demised premises (other than improvements made by Lessee) and are not caused by use and occupancy of lessee. It is not intended by this clause that Lessee shall be responsible for liabilities imposed by the acts of others committed prior to the date of this lease.

Lessee also shall, at all times prior to termination of the lease term and delivery to lessor of possession of the premises, indemnify lessor against all liens and charges of any and every nature that may at any time be established against the premises or any improvements thereon or any part thereof as a consequence, direct or indirect, of any act or omission of lessee or as a consequence, direct or indirect, of the existence of lessee's interest under this lease.

XXXII. NOTICE BY LESSEE OF LITIGATION - PAYMENT OF ATTORNEY'S FEES AND COSTS:

Within five days after lessee has knowledge of any material litigation or other proceeding that shall be instituted against lessee, against the demised premises to secure or recover possession thereof, or that may affect the title to or the interest of lessor in the demised premises, lessee shall give written notice thereof to lessor.

Lessee shall pay all reasonable attorney's fees and costs on behalf of lessor if (a) lessor institutes litigation against lessee for a breach of the terms and conditions of this lease, (b) lessor institutes litigation against lessee for an unlawful detainer of the demised premises, or (c) lessor is made a part to litigation against lessee instituted by a third party, relating to the demised premises, wherein lessor is not at fault. The reasonable attorney's fees and costs incurred by lessor herein shall be paid by lessee whether litigation is prosecuted to judgement or not.

The payment of all attorney's fees and court costs required hereby shall be made to lessor as additional rental and shall be due in full on the next regular date for a rental payment. This additional rental shall be subject to an interest charge of eighteen (18%) per cent per annum, and lessor may enforce the payment by using any remedy available at law or under this lease of the collection of past due rent.

XXXIII. APPLICABLE LAW:

This agreement shall be governed by and construed in accordance with the laws of the State of New York.

IN WITNESS WHEREOF, the parties have executed this lease in the State of New York the day and year first above written.

/s/ Jean K. Woodward
Jean K. Woodward, Lessor

By: /s/ James L. Kehoe
Sono-Tek Corp, Lessee

/s/ Kathleen N. Martin, Witness