SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)
[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED JUNE 30, 1998.

[ ] 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: 0-16159

LECTEC CORPORATION
(Exact name of registrant as specified in its charter)

MINNESOTA	41-1301878
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

10701 RED CIRCLE DRIVE, MINNETONKA, MINNESOTA	55343
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (612) 933-2291

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: Common Stock, par value $0.01 per share.

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 [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein; and will not be contained, to the best of the Registrant's knowledge, in the definitive proxy statement incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]

The aggregate market value of the Common Stock held by non-affiliates of the Registrant as of September 22, 1998 was $10,074,405 based upon the last reported sale price of the Common Stock at that date by the Nasdaq Stock Market.

The number of shares outstanding of the Registrant's Common Stock as of September 22, 1998 was 3,945,129 shares.

DOCUMENTS INCORPORATED BY REFERENCE

Part III of this Annual Report on Form 10-K incorporates by reference information from the Registrant's Proxy Statement for its Annual Meeting of Shareholders to be held November 19, 1998 (1998 Proxy Statement).

PART I

ITEM 1. BUSINESS

GENERAL

LecTec Corporation (the "Company") designs, manufactures and markets resting diagnostic (ECG or "electrocardiograph") electrodes, conductive and non-conductive adhesive hydrogels, medical tapes and patches for the topical application of over-the-counter (OTC) drugs and therapeutic and skin care compounds. The Company markets its products to medical product distributors, physician clinics, hospital purchasing groups, hospitals, consumers through retail distribution channels, original equipment manufacturers (OEMs) and direct selling groups. All of the products manufactured by the Company are designed to be highly compatible with skin, the largest organ of the human body.

The Company developed one of the first solid gel disposable ECG electrodes, which did not require the use of aqueous conductive gels in order to maintain contact with the skin. The Company has since continued to develop, manufacture and market electrodes as well as hydrogels, medical tapes, topical drug delivery systems, patches and therapeutic products. A hydrogel is a gel-like material having an affinity for water and similar compounds. These gels are ideal for electrical conductivity and skin compatibility. The Company holds multiple domestic and foreign patents.

The Company, through its research and development efforts, is investigating new products for topical drug delivery, new conductive adhesive hydrogel polymers, medical tapes and wound care treatments, as well as a smoking cessation pill. In addition, existing technologies are being refined to focus on new products targeting new customers and new markets.

The Company was organized in 1977 as a Minnesota corporation. Its principal executive office is located at 10701 Red Circle Drive, Minnetonka, Minnesota 55343, and its telephone number is (612) 933-2291.

PRODUCTS

The Company's core competency is skin interface technology. This competency results in products which are chemically compatible with human skin, thereby reducing or eliminating skin irritation and reducing damage to the skin as well as the risk of infection. The electrical properties, adhesive characteristics, product dimensions, drug stability, shelf life and manufacturability are highly consistent and reproducible from product to product.

CONDUCTIVE PRODUCTS

The Company's conductive products include diagnostic electrodes and electrically conductive adhesive hydrogels.

The Company applies its patented conductive, skin compatible, adhesive hydrogel technology to cardiac diagnostic electrodes. The Company's patented natural and synthetic-based hydrogel polymers are self-adherent and are capable of being made electrically conductive. Using natural-based polymers, the Company developed the first solid gel disposable resting diagnostic ECG electrodes. All of the Company's electrodes meet or exceed all national and international performance standards.

The solid gel design of the Company's electrodes provides more consistent electrical performance and eliminates clean-up time. Currently the Company has three different types of diagnostic electrodes: T-1000 Plus, a disposable electrode made of natural polymer solid gel with gentle adhesion; MP-3000 and 3009, synthetic solid gel electrodes with higher levels of adhesion which meet all AAMI (American Association for Medical Instrumentation) standards including defibrillation recovery; and AG4000, a synthetic solid gel, silver substrate electrode which also meets all AAMI standards including defibrillation recovery.

The Company pioneered hydrogel technology and manufactures synthetic and natural-based hydrogels. These hydrogels are resistant to dehydration, evaporation and changes in electrical and physical properties. Hydrogels are also used to deliver specific medications to the skin for topical use. Hydrogels are manufactured with various levels of conductivity as well as with varying degrees of self-adhesive properties, for diagnostic electrodes, electrosurgical grounding pads, external defibrillation, pacing and monitoring electrodes, TENS (Transcutaneous Electronic Nerve Stimulation) products and iontophoretic return electrodes.

Sales of conductive products accounted for approximately 61%, 63% and 61% of the Company's total sales for fiscal years 1998, 1997 and 1996.

MEDICAL TAPE PRODUCTS

The Company manufactures and markets hypoallergenic medical tape products in various individual slit roll widths and in large jumbo rolls for the world market. The Company's medical tape business includes the U.S. healthcare market (hospitals and alternate care segments), the U.S. consumer market and the international healthcare market. The Company's medical tape product line is comprised of the standard paper, plastic and cloth products widely used in the healthcare industry.

The Company manufactures and markets the individual slit roll widths under the private label brand names of customers and under the LecTec brand name. The large jumbo rolls are converted by the customer into individual slit roll widths for ultimate sale to consumers.

Sales of medical tapes accounted for approximately 32%, 25% and 24% of the Company's total sales for fiscal years 1998, 1997 and 1996.

THERAPEUTIC PRODUCTS

The Company manufactures and markets patches for the topical application of OTC drugs and other therapeutic and skin care compounds. Therapeutic products use a hydrogel based, breathable backed skin interface system that delivers drugs and other therapeutic compounds onto the skin. Products currently manufactured using the adhesive-based patch technology are analgesic patches for localized pain relief, a recently launched cough suppressant patch, wart removers, as well as a corn and callus remover. These products are marketed as OTC products. The family of patches is marketed under the LecTec brand name TheraPatch(R).

Sales of therapeutic products accounted for approximately 7%, 12% and 15% of the Company's total sales for fiscal years 1998, 1997 and 1996.

CUSTOMERS

Burdick Corporation accounted for 18%, 19% and 17% of the Company's total sales for the fiscal years 1998, 1997 and 1996. The Company sold its products to approximately 190, 140 and 150 active customers during 1998, 1997 and 1996. The Company's backlog orders (purchase orders received from customers for future shipment) as of August 12, 1998 totaled $911,000 (all of which the Company expects to fill in fiscal 1999), compared with approximately $1,663,000

on August 12, 1997.

GOVERNMENTAL AND ENVIRONMENTAL REGULATION

Design development planning, clinical testing, manufacturing, packaging, labeling and distribution of the Company's products are subject to federal (FDA - Food and Drug Administration), state, local and foreign regulation. The Company's electrodes under current FDA policy are marketed pursuant to Section 510(k) notification, which is a means of obtaining FDA clearance to market a medical device. Additionally, all LecTec branded electrodes are CE Marked, indicating they are in conformance to the European Union Medical Device Directive 93/42/EEC. The Company's topical drug products are marketed under the applicable existing FDA OTC monographs. Any new drug and transdermal new drug development is marketed after approval of a New Drug Application (NDA) containing full reports of detailed laboratory and clinical investigations on laboratory animals and human patients.

The Company does not use solvents in the manufacturing of its products that have an adverse effect on the environment. The Company does not anticipate any major expenditure for environmental controls during the next fiscal year.

COMPETITION

The markets for electrodes, hydrogels, medical tapes and topical drug delivery patches are highly competitive. Firms in the medical, OEM and consumer industries compete on the basis of product performance, pricing, distribution and service. Many of the Company's major competitors have significantly greater financial, marketing and technological resources than the Company. However, the Company believes that it competes on the basis of proprietary technology, flexibility, customer focus, an experienced executive team and its ability to manufacture and market its products to targeted market segments.

Over the past several years there has been a number of mergers within the electrode and hydrogel industries, resulting in fewer but larger competitors. The Company has also noted a consolidation of customers and reduction in the number of manufacturers of medical tapes.

The Company's dominant competitor for hydrogel sales is the Ludlow division of Tyco, Inc., and the dominant competitors for medical tape sales are 3M Company and Johnson & Johnson. The Company's OTC TheraPatch family of analgesic and cough suppressant patches competes with ointments, lotions and creams manufactured by various competitors including Hisamitsu Pharmaceutical Co, Inc.

PATENTS AND TRADEMARKS

The Company has U.S. and foreign patents on adhesive hydrogels, electrodes, transdermal and topical delivery systems and tape structures. Twenty-seven active U.S. patents and twenty-five active international patents are currently assigned or licensed to the Company. Seven U.S. patents and two international patents were issued to the Company during fiscal 1998. Twelve U.S. and foreign applications are pending. The patents most pertinent to the Company's major products have a remaining duration ranging from two to sixteen years. Only one of these patents has a remaining duration of less than five years and the expiration of this patent is not expected to have a material effect on the Company's proprietary position.

One trademark registration was received in fiscal 1998. Four trademark registrations are pending.

The Company expects that its products will be subject to continuous modifications due to improvements in materials and technological advances in the market for medical products. Therefore, the Company's continued success does not depend solely upon ownership of patents, but upon technical expertise, creative skills and the ability to forge these talents into the timely release of new products into the marketplace.

The Company uses both patents and trade secrets to protect its proprietary property and information. In addition, the Company monitors competitive products and patent publications to be aware of potential infringement of its rights.

RESEARCH AND DEVELOPMENT

The Company's research and development staff consists of professionals drawn from the business and academic communities with experience in the biological, chemical, pharmaceutical and engineering sciences. The research and development staff is responsible for the investigation, development and implementation of new and improved products and new technologies.

The Company may develop products internally, jointly with corporations and/or with inventors from outside the Company. The Company may then market resulting products, by sponsoring partners or through a marketing arrangement with an appropriate distributor. Research and development contract opportunities are evaluated on an individual basis.

Research and development resources are being used to fund development of new topical patch products, conductive products, medical tapes and a cotinine based smoking cessation product.

The Company believes that cotinine is a promising non-nicotine drug for use in treating tobacco withdrawal symptoms. Because of the additional cost associated with the remaining clinical work on cotinine, the Company is actively seeking outside partners to help fund this development and move this non-nicotine program to completion.

During fiscal years 1998, 1997 and 1996, the Company spent approximately $1,037,000, $1,515,000 and $1,975,000 on research and development.

MARKETING AND MARKETING STRATEGY

The Company markets and sells its products to medical products distributors, physician clinics, hospital purchasing organizations, hospitals, long-term care facilities, consumers through retail outlets (food, chain drug and discount stores) and original equipment manufacturers (OEMs).

The Company implemented a proactive marketing and sales strategy to expand its sales to existing customers and to develop a base of new customers. The Company also continues to execute a balanced distribution strategy, consisting of traditional private label distribution and the new LecTec TheraPatch brand strategy. This balanced approach is designed to increase penetration into current markets, while allowing the Company to move into several highly promising new markets for its electrode, medical tape and patch products.

A major entry into the consumer markets was supported by the hiring of a new sales executive and a retail sales team. In the consumer market, retail broker and manufacturer's representative relationships have been established. The TheraPatch(R) brand will be the umbrella brand for all LecTec topical patches introduced to all markets.

The Company has not experienced any significant seasonality in sales of its products.

The Company sells its products in the U.S., Europe, Middle East, Latin America, Canada and Asia. Export sales accounted for approximately 26% of total sales for 1998 and 19% of total sales for both 1997 and 1996.

The Company's international sales are made by the Company's corporate sales force. The Company does not maintain a separate international marketing staff or operations. The following table sets forth export sales by geographic area:

	Years ended June 30		
	1998	1997	1996
Europe	$1,705,996	$1,456,141	$1,652,941
Middle East	912,240	14,854	295,159
Latin America	371,854	484,319	225,440
Canada	199,082	117,966	80,746
Asia	62,027	132,590	32,366
Other	71,949	82,062	139,252
Total Export Sales	$3,323,148	$2,287,932	$2,425,904

MANUFACTURING

The Company manufactures its conductive and therapeutic membranes at the Company's Minnetonka, Minnesota facility. The Minnetonka facility also manufactures and packages the Company's therapeutic products and conducts raw material processing operations. The Company's second manufacturing facility in Edina, Minnesota is the primary site for the manufacturing and packaging of medical tape and diagnostic electrodes. The Edina location also provides the majority of the Company's warehouse capacity.

The Company believes that the raw materials used in manufacturing its products are generally available from multiple suppliers.

EMPLOYEES

As of June 30, 1998, the Company employed 85 full-time employees. None of the Company's employees are represented by labor unions or other collective bargaining units. The Company believes relations with its employees are good.

PHARMADYNE CORPORATION AND RESTRUCTURING CHARGE

On June 30, 1992, the Company entered into a Research, Development and Marketing Agreement with Pharmadyne Corporation (formerly Natus Corporation) related to the analgesic patch product. During 1993 through 1996, the Company made various investments in and advances to Pharmadyne Corporation resulting in a cumulative ownership of 61%.

During 1997, the Company adopted a plan for eliminating the Pharmadyne subsidiary and recorded a nonrecurring restructuring charge of $2,180,000 which increased the 1997 net loss by $.57 per share. The restructuring charge included approximately $1,369,000 for the planned acquisition of the minority interests in Pharmadyne in exchange for newly issued shares of LecTec Corporation common stock, $480,000 for the write-off of Pharmadyne's 15% interest in Natus, L.L.C.,

an Arizona-based direct marketing company, and $331,000 for completion of restructuring activities, consisting primarily of fees for professional services. In October 1997, the Company issued 221,948 shares of its common stock to acquire the minority interest in Pharmadyne. In November 1997, the newly issued shares were registered with the Securities and Exchange Commission. On December 31, 1997, Pharmadyne Corporation was merged into LecTec Corporation.

EXECUTIVE OFFICERS OF THE REGISTRANT

<TABLE>
<CAPTION>

Name	Age	Title
<S>	<C>	
Rodney A. Young	43	Chairman, Chief Executive Officer and President
Deborah L. Moore	41	Chief Financial Officer and Secretary
Jane M. Nichols	52	Vice President, Marketing and New Business Development
Daniel M. McWhorter	58	Vice President, Research and Development

</TABLE>

Rodney A. Young is Chairman, Chief Executive Officer and President. He joined the Company in August 1996. Mr. Young has 20 years of healthcare industry experience including sales and marketing for Upjohn Company and 3M Company. Prior to joining LecTec he was Vice President and General Manager of the Specialized Distribution Division of Baxter International, Inc.

Deborah L. Moore is Chief Financial Officer and Secretary. She joined the Company in February 1997. Ms. Moore's 21-year professional background includes public accounting with the big six firms of Ernst & Young LLP and Deloitte & Touche LLP. Prior to joining LecTec she was the Vice President of Corporate Development for Varitronic Systems, Inc.

Jane M. Nichols is Vice President, Marketing and New Business Development. She joined the Company in April 1997. Ms. Nichols' 26-year career includes clinical, technical and management roles at Methodist Hospital and Park Nicollet Medical Centers, and senior marketing positions at 3M Company and Ecolab.

Daniel M. McWhorter is Vice President, Research and Development. He joined the Company in January 1997. Mr. McWhorter has more than 26 years of experience in the medical products industry including both technical and general management positions at The Kendall Company and Pharmacia Deltec and senior technical positions at Abbott Laboratories and Mentor Corporation.

ITEM 2. PROPERTIES

The Company owns a building located in Minnetonka, Minnesota, containing 18,000 square feet of office and laboratory space and 12,000 square feet of manufacturing and warehouse space. In addition, the Company leases a building in Edina, Minnesota containing 29,000 square feet of manufacturing and warehouse space.

ITEM 3. LEGAL PROCEEDINGS

None

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

None

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's common stock trades on the Nasdaq National Market tier of The Nasdaq Stock Market ("Nasdaq") under the symbol LECT.

The following table sets forth the high and low daily trade price information for the Company's common stock for each quarter of fiscal 1998 and 1997. Such prices reflect interdealer prices, without retail mark-up, mark-down, or commission, and may not necessarily represent actual transactions.

YEARS ENDED JUNE 30,	1998		1997	
	HIGH	LOW	HIGH	LOW
First Quarter	$9.750	$5.375	$13.500	$8.500

Second Quarter	7.000	4.500	9.500	5.500
Third Quarter	5.750	3.875	8.500	5.000
Fourth Quarter	4.469	3.250	7.000	4.875

As of September 22, 1998 the Company had 3,945,129 shares of common stock outstanding, and 359 common shareholders of record which number does not include beneficial owners whose shares were held of record by nominees or broker dealers.

The Company has not declared or paid cash dividends on its common stock since its inception, and intends to retain all earnings for use in its business for the foreseeable future.

ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

STATEMENT OF OPERATIONS DATA

<TABLE>
<CAPTION>

Years ended June 30,	1998	1997	1996	1995	1994
<S>	<C>	<C>	<C>	<C>	<C>
Net sales	$ 12,922,365	$ 12,256,327	$ 13,100,754	$ 14,138,290	$ 10,715,490
Gross profit	3,715,032	4,324,180	4,969,659	5,697,562	4,041,853
Earnings (loss) from operations	(474,935)	(2,215,951) *	(724,074)	69,761	837,161
Earnings (loss) before equity in losses of unconsolidated subsidiary	(404,061)	(2,140,660) *	(632,193)	153,863	768,974
Equity in losses of unconsolidated subsidiary	--	126,067	--	--	133,639
Net earnings (loss)	(404,061)	(2,266,727) *	(632,193)	153,863	635,335
Net earnings (loss) per common and common equivalent share (BASIC AND DILUTED)	(.10)	(.59) *	(.17)	.04	.17

BALANCE SHEET DATA

At June 30,	1998	1997	1996	1995	1994
Cash, cash equivalents and short-term investments	$ 2,186,532	$ 1,242,777	$ 800,693	$ 839,942	$ 2,182,570
Current assets	6,728,531	6,873,696	5,624,682	5,764,363	6,124,640
Working capital	5,335,861	4,035,084	4,240,024	4,490,796	4,737,567
Property, plant and equipment, net	4,306,568	4,592,304	5,112,975	5,559,807	4,705,602
Long-term investments	8,676	8,013	574,806	568,156	585,855
Total assets	11,317,774	11,837,356	12,494,003	12,646,745	12,363,075
Long-term liabilities	222,000	211,000	174,000	167,000	139,000
Shareholders' equity	9,703,104	8,787,744	10,935,345	11,206,178	10,837,002

</TABLE>

* Includes a nonrecurring restructuring charge of $2,180,353 or $.57 per share.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS

NET SALES

Net sales were $12,922,000 in 1998, an increase of 5.4% from net sales of $12,256,000 in 1997. Net sales were $13,101,000 in 1996. The increase in 1998 net sales was due primarily to increased medical tape sales. The decrease in 1997 net sales was due primarily to the absence of direct marketing sales for the entire 1997 fiscal year. While there were no direct marketing sales in fiscal 1997, such sales totaled $1,410,000 or 10.8% of total net sales in fiscal 1996. The Company's Pharmadyne Corporation subsidiary, which was merged into LecTec Corporation on December 31, 1997, divested its direct marketing related assets near the end of the third quarter of fiscal 1996. In 1997, the absence of direct marketing therapeutic product sales was partially offset by an increase in the volume of therapeutic products sold through indirect distribution channels. Net sales of conductive products and medical tape products decreased by 2.8% and 2.7%, respectively, in 1997 from the prior

year.

Net sales of conductive products (medical electrodes and hydrogels) increased by 2.5% in 1998 to $7,907,000 from $7,714,000 in 1997. Conductive product net sales were $7,940,000 in 1996. These fluctuations in sales were primarily volume-related. The Company expects to maintain or increase fiscal 1998 levels of conductive sales in fiscal 1999.

Net sales of medical tapes increased by 34.4% in 1998 to $4,157,000 from $3,093,000 in 1997. Medical tape net sales were $3,180,000 in 1996. The increase in 1998 was primarily attributable to an order from an international customer whose business fluctuates from year to year. Excluding sales to this international customer, medical tape sales to all other customers increased by 5.2% in 1998. The decrease in 1997 was primarily attributable to the absence of an order from this same international customer. Excluding sales to this international customer, medical tape sales to all other customers increased by 6.8% in 1997. This increase was primarily the result of increased sales volume. Excluding sales to the international customer referred to above, the Company expects to maintain or increase fiscal 1998 levels of medical tape product sales in fiscal 1999.

Net sales of therapeutic products decreased 41.6% in 1998 to $846,000 from $1,449,000 in 1997. Therapeutic product net sales were $1,981,000 in fiscal 1996. The decrease in 1998 was primarily due to decreased analgesic patch sales to CNS, Inc. and decreased wart remover product sales. The agreement under which CNS distributed the TheraPatch(R) product was terminated at the end of fiscal 1998 and the Company assumed responsibility for the retail distribution of the product. The decrease in sales in 1997 was primarily due to the absence of Pharmadyne direct marketing sales for the entire 1997 fiscal year as compared to the inclusion of direct marketing sales for the first three quarters of fiscal 1996, which totaled $1,410,000. The absence of direct marketing sales beginning in the fourth quarter of 1996 resulted from the divestiture of Pharmadyne's direct marketing related assets near the end of the third quarter of 1996. Management believes that sales of the Company's therapeutic patch products will represent an increased percentage of total net sales during fiscal 1999 due to the launch of its new TheraPatch family of products, including two new vapor products.

International sales, consisting primarily of semi-finished conductive and medical tape products sold to overseas converters for final processing, packaging and marketing, were 25.7%, 18.7% and 18.5% of total net sales in 1998, 1997 and 1996. The increase in the percent for 1998 resulted from medical tape sales to an international customer. The Company expects fiscal 1999 international sales to be comparable to fiscal 1997 and 1996 sales levels.

GROSS PROFIT

The Company's gross profit was $3,715,000 in 1998, down from $4,324,000 in 1997. Gross profit was $4,970,000 in 1996. As a percentage of net sales, gross profit was 28.8% in 1998, 35.3% in 1997 and 37.9% in 1996. The decrease in gross profit in 1998 resulted primarily from a shift in the sales mix from higher margin conductive and therapeutic products to lower margin medical tape products, increased material costs, and a shift in labor costs from research and development to manufacturing. In 1997, the decrease in the gross profit percent resulted primarily from the absence of higher margin direct marketing related sales and increased inventory obsolescence costs which were partially offset by decreased material and labor costs for conductive products. While the direct marketing sales present in 1996 carried higher gross margins than sales made through the Company's indirect distribution channels, the selling, general and administrative costs associated with the direct marketing operation were

substantially greater than the costs required to support sales through indirect distribution. The higher operating expenses of the direct marketing organization more than offset the higher gross margins associated with those sales.

SALES AND MARKETING EXPENSES

Sales and marketing expenses totaled $1,043,000 or 8.1% of net sales in 1998, compared to $597,000 or 4.9% of net sales in 1997, and $482,000 or 3.7% of net sales in 1996. The 1998 increase was primarily due to increased sales promotion expense, as well as increased staffing levels and consulting expense. These increases were especially significant in the fourth quarter and to a great extent were related to the launch of the TheraPatch family of patch products. The 1997 increase was primarily due to staffing level increases and separation costs associated with a former executive. The Company anticipates sales and marketing expenses in fiscal 1999 will increase significantly due to increased sales and marketing efforts, particularly marketing programs associated with patch sales. However, the Company also expects the gross margin on patch sales to increase since the Company will also be selling directly to retail outlets and consumers rather than selling exclusively to distributors.

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses totaled $2,110,000 or 16.3% of net sales in 1998, compared to $2,247,000 or 18.3% of net sales in 1997, and $3,237,000 or 17.8% of net sales in 1996. The 1998 decrease was primarily due to the absence of goodwill amortization and lower fees associated with executive recruitment. The 1997 decrease was primarily due to the absence of the direct marketing expenses of the Pharmadyne subsidiary during all of 1997 as compared to 1996, which included direct marketing expenses for the first three quarters. The 1997 decrease was partially offset by increased administrative expenses associated with hiring a new executive staff, and separation costs associated with former executives. The Company anticipates general and administrative expenses in fiscal 1999 will be comparable to fiscal 1998.

RESEARCH AND DEVELOPMENT EXPENSES

Research and development expenses totaled $1,037,000 or 8.0% of

net sales in 1998, compared to $1,515,000 or 12.4% of net sales in 1997, and $1,975,000 or 15.1% of net sales in 1996. The decrease in research and development expense for 1998 reflects reductions in research costs associated with the internal development of the cotinine-based smoking cessation product as well as a shift in labor costs to manufacturing. The higher levels of research and development expenditures in 1997 and 1996 reflect the utilization of internally generated funds to develop additional therapeutic products and a new cotinine-based product. The decrease in 1997 research and development expense was primarily due to decreased labor costs and decreased cotinine related expenses. Research and development resources are also being used to fund development of new patch products, conductive products and specialized medical tapes. Management believes that research and development expenditures in fiscal 1999 will be comparable to fiscal 1998.

RESTRUCTURING CHARGE

During 1997 the Company recorded a nonrecurring restructuring charge of $2,180,000 related to its plan for eliminating the Pharmadyne Corporation subsidiary. The restructuring charge included approximately $1,369,000 for the planned acquisition of the minority interests in Pharmadyne in exchange for newly issued shares of LecTec Corporation common stock, $480,000 for the write-off of Pharmadyne's 15% interest in Natus, L.L.C., an Arizona-based direct marketing company, and $331,000 for the completion of restructuring activities, consisting primarily of fees for professional services. In October 1997, the Company issued 221,948 new shares of its common stock to acquire the minority interests in Pharmadyne. In November 1997, the newly issued shares were registered with the Securities and Exchange Commission. On December 31, 1997, Pharmadyne Corporation was merged into LecTec Corporation.

OTHER INCOME, NET

Other income, net totaled $70,000 in 1998, compared to $75,000 in 1997 and $54,000 in 1996. The decrease in 1998 was due to the absence of a gain on the sale of equipment, which was partially offset by increased investment income due to higher cash and short-term investment balances during 1998. The increase in 1997 resulted primarily from the gain on sale of equipment.

INCOME TAX BENEFIT

The Company recorded an income tax benefit of $1,000 in 1998, no income tax expense or benefit in 1997, and an income tax benefit of $38,000 in 1996. The tax benefit in 1998 was minimal since the loss benefit for the year may not be realizable by the Company. There was no income tax benefit recorded during 1997 due primarily to the effect of the non-deductible restructuring charge. The tax benefit in 1996 resulted from losses incurred in 1996 reduced by the effect of the subsidiary losses which could not be utilized by the Company at that time and the effect of goodwill amortization.

EQUITY IN LOSSES OF UNCONSOLIDATED SUBSIDIARY

On March 12, 1996, the Company contributed the direct marketing related assets of the Pharmadyne Corporation to Natus L.L.C. (an Arizona limited liability company) in exchange for a 15% interest in Natus L.L.C. This investment was accounted for using the equity method. During 1997 the Company recorded $126,000 of equity in the losses of Natus L.L.C. The remaining investment in Natus L.L.C. of $480,000 was fully written off in 1997 as part of the $2,180,000 restructuring charge.

OPERATIONS SUMMARY

The net loss for 1998 resulted primarily from a decrease in the gross profit percent due to a shift in the sales mix from higher margin conductive and therapeutic products to lower margin medical tape products and increased material costs and usage. In 1997, the restructuring charge of $2,180,000 or $.57 per share was the primary component of the total net loss of $2,267,000 or $.59 per share. Excluding the impact of this one-time charge, the loss for 1997 was $87,000 or $.02 per share. The net loss in 1996 was $632,000 or $.17 per share. The largest components of the net loss for fiscal 1996 were the losses associated with the direct marketing related operations of the Pharmadyne Corporation subsidiary and increased research and development expense.

EFFECT OF INFLATION

Inflation has not had a significant impact on the Company's operations or cash flow.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents increased by $1,522,000 to $2,187,000 at June 30, 1998 from $665,000 at June 30, 1997. Short and long-term investments decreased by $577,000 to $9,000 at June 30, 1998 from $586,000 at June 30, 1997 due to the sale of investments. The Company's investment policy reflects its goals of preservation of capital, minimization of risk and maintainance of flexibility through the use of highly liquid temporary investments with maturity dates of three months or less (primarily short-term commercial paper). Refundable income taxes decreased by $342,000 to $60,000 due to the receipt of income tax refunds. Inventories decreased by $859,000 to $1,718,000 due to the implementation of programs designed to more effectively manage raw material inventories. Capital spending for plant improvement and various equipment totaled $407,000 in 1998. There were no material commitments for capital expenditures at June 30, 1998.

Working capital totaled $5,336,000 at June 30, 1998, compared to $4,035,000 at the end of fiscal 1997. The Company's current ratio was 4.8 at June 30, 1998 compared to 2.4 at June 30, 1997. Excluding the accrued restructuring charge, the Company's current ratio at June 30, 1997 was 5.2.

Net property, plant and equipment decreased by $285,000 to

$4,307,000 at June 30, 1998 from $4,592,000 at June 30, 1997, reflecting the excess of depreciation expense over additions.

The Company has no short or long-term debt. During August 1997 the Company obtained an unsecured $1,000,000 working capital line of credit which expired on September 1, 1998. There were no borrowings outstanding under the line of credit as of June 30, 1998, nor during fiscal year 1998. Shareholders' equity increased by $915,000 to $9,703,000 as of June 30, 1998 from $8,788,000 as of June 30, 1997, primarily due to the impact of the shares issued to acquire the minority interests in Pharmadyne Corporation. In April 1998, the Company announced a stock repurchase program authorizing the repurchase of up to 500,000 shares to be funded with internally generated funds. As of September 22, 1998 the Company has repurchased 120,350 share of common stock under the program for an aggregate purchase price of approximately $425,000.

Management believes that internally generated cash flow and the expected renewal of the short-term line of credit will be sufficient to support anticipated operating and capital spending requirements during fiscal 1999.

IMPACT OF THE YEAR 2000 ISSUE

The Year 2000 ("Y2K") issue is the result of computer programs using a two-digit format, as opposed to four digits, to indicate the year. Such computer systems will be unable to interpret dates beyond the year 1999, which could cause a system failure or other computer errors, leading to disruptions in operations. A number of other date issues (i.e. incorrect handling of leap years) may also cause problems. All of these issues are collectively referred to as Y2K.

In fiscal 1998, the Company developed a comprehensive program for Y2K compliance consisting of two parts; internal systems compliance and third party compliance. Internal systems compliance includes informational, manufacturing, financial and communication systems. A committee consisting of representatives from all key areas of the Company developed the program. The internal systems compliance program consists of four-phases. Phase I is the identification of all internal computer systems in the Company, including embedded microprocessor or similar circuitry. Phase II is the determination of Y2K compliance for these systems. Phase III is development and implementation of action plans to achieve compliance where needed, and is followed by the testing in Phase IV of these systems after action plans have been completed. The third party compliance program consists of three phases with Phase I being the identification of major and/or critical third party vendors and customers. Phase II consists of contacting these third parties and determining their Y2K compliance. Phase III involves establishing risk and developing contingency plans where necessary (third party compliance can not be established or the risks associated with noncompliance are significant).

The Company has completed Phases I and II of the internal systems compliance program and has found the majority of its systems and all of its core systems to be Y2K compliant. Plans have been developed and are underway to achieve Y2K compliance for the non-core systems by the end of calendar 1998. The Y2K compliant status of the core systems benefited from upgrades undertaken during the past several years to make these systems adequate for the business needs of the Company. Phase IV of the program, testing of systems after implementation of changes, is being undertaken concurrently with Phase III and will continue through the end of calendar 1998. The Company is approximately 50% complete with Phase III and 40% complete with Phase IV. The Company expects to have substantially completed all aspects of the internal systems compliance program before the end of calendar 1998 and considers the risk that compliance will not be achieved to be minimal. Costs to-date for this program have been immaterial.

The Company has completed Phase I of the third party compliance program and is approximately 50% complete with Phase II. Initial questionnaires have been sent to major and/or critical third party vendors and customers, and approximately 75% of those contacted have responded. Responses are being sought from the remaining major and/or critical vendors and customers. The Company is in the initial stages of Phase III, the evaluation of responses, establishment of risk and the development of contingency plans. Because of the diversity of sources available for the Company's raw material, packaging material and supplies, the Company believes that third party Y2K compliance issues will not have a material adverse effect on the Company's financial position, operations or cash flow. There can, however, be no assurance that this will be the case. The Company expects to have substantially completed all phases of the third party compliance program by the end of calendar 1998. Costs to-date for the third party compliance program have also been immaterial.

All costs for Y2K compliance which have been incurred have been expensed in the period incurred and have been paid from operating funds. The Company does not expect the cumulative costs for Y2K compliance to be material.

FORWARD-LOOKING STATEMENTS

From time to time, in reports filed with the Securities and Exchange Commission (including this Form 10-K), in press releases, and in other communications to shareholders or the investment community, the Company may provide forward-looking statements concerning possible or anticipated future results of operations or business developments which are typically preceded by the words "believes", "expects", "anticipates", "intends", "will", "may", "should" or similar expressions. Such forward-looking statements are subject to risks and uncertainties which could cause results or developments to differ materially from those indicated in the forward-looking statements. Such risks and uncertainties include, but are not limited to, the buying patterns of major customers; competitive forces including new products or pricing pressures; costs associated with and acceptance of the Company's new brand strategy; impact of interruptions to production; dependence on key personnel; need for regulatory approvals; changes in governmental regulatory requirements or accounting pronouncements; and ability to satisfy funding requirements for operating needs, expansion or capital expenditures.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The disclosures required by this item are not required by the Company for its fiscal year ended June 30, 1998.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

LecTec Corporation and Subsidiaries Financial Statements Furnished Pursuant to the Requirements of Form 10-K.

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Shareholders and
Board of Directors
LecTec Corporation

We have audited the accompanying consolidated balance sheets of LecTec Corporation and subsidiaries as of June 30, 1998 and 1997, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended June 30, 1998. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of LecTec Corporation and subsidiaries as of June 30, 1998 and 1997, and the consolidated results of their operations and their consolidated cash flows for each of the three years in the period ended June 30, 1998, in conformity with generally accepted accounting principles.

/s/ Grant Thornton LLP

Minneapolis, Minnesota
August 12, 1998

LECTEC CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

<TABLE>
<CAPTION>

ASSETS	June 30 1998	June 30 1997
<S>	<C>	<C>
CURRENT ASSETS		
Cash and cash equivalents	$ 2,186,532	$ 665,190
Short-term investments	--	577,587
Receivables		
Trade, net of allowance of $90,818 in 1998 and $48,529 in 1997	2,251,757	2,178,984
Refundable income taxes	59,544	401,263
Other	30,624	22,780
	2,341,925	2,603,027
Inventories	1,718,011	2,577,021
Prepaid expenses and other	103,063	84,871
Deferred income taxes	379,000	366,000

Total current assets	6,728,531	6,873,696
PROPERTY, PLANT AND EQUIPMENT --		
AT COST		
Building and improvements	1,816,277	1,635,157
Equipment	6,791,765	6,578,960
Furniture and fixtures	384,260	371,670
	8,992,302	8,585,787
Less accumulated depreciation	4,933,465	4,241,214
	4,058,837	4,344,573
Land	247,731	247,731
	4,306,568	4,592,304
OTHER ASSETS		
Patents and trademarks, less accumulated amortization of $1,001,157 in 1998 and $848,814 in 1997	273,999	363,343
Other	8,676	8,013
	282,675	371,356
	$11,317,774	$11,837,356

</TABLE>

The accompanying notes are an integral part of these statements.

LECTEC CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS - CONTINUED

<TABLE>
<CAPTION>

	June 30	
LIABILITIES AND SHAREHOLDERS' EQUITY	1998	1997
<S>	<C>	<C>
CURRENT LIABILITIES		
Accounts payable	$ 809,147	$ 779,699
Accrued expenses		
Payroll related	384,135	324,381
Restructuring charge	--	1,521,107
Other	199,388	213,425
Total current liabilities	1,392,670	2,838,612
DEFERRED INCOME TAXES	222,000	211,000
COMMITMENTS AND CONTINGENCIES	--	--
SHAREHOLDERS' EQUITY		
Common stock, $.01 par value; 15,000,000 shares authorized; issued and outstanding: 4,036,000 shares in 1998 and 3,842,800 shares in 1997	40,360	38,428
Additional paid-in capital	11,769,053	10,476,428
Unrealized losses on securities available-for-sale	(8,508)	(33,372)
Deficit in retained earnings	(2,097,801)	(1,693,740)
	9,703,104	8,787,744
	$ 11,317,774	$ 11,837,356

</TABLE>

The accompanying notes are an integral part of these statements.

LECTEC CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

<TABLE>
<CAPTION>

	Years ended June 30		
	1998	1997	1996
<S>	<C>	<C>	<C>
Net sales	$ 12,922,365	$ 12,256,327	$ 13,100,754
Cost of goods sold	9,207,333	7,932,147	8,131,095
Gross profit	3,715,032	4,324,180	4,969,659
Operating expenses			
Sales and marketing	1,042,788	597,169	481,748
General and administrative	2,110,084	2,247,449	3,236,748
Research and development	1,037,095	1,515,160	1,975,237
Restructuring charge	--	2,180,353	--
	4,189,967	6,540,131	5,693,733
Loss from operations	(474,935)	(2,215,951)	(724,074)
Other income, net	69,874	75,291	53,881
Loss before income taxes and equity in losses of unconsolidated subsidiary	(405,061)	(2,140,660)	(670,193)
Income tax benefit	(1,000)	--	(38,000)
Loss before equity in losses of unconsolidated subsidiary	(404,061)	(2,140,660)	(632,193)
Equity in losses of unconsolidated subsidiary	--	126,067	--
Net loss	$ (404,061)	$ (2,266,727)	$ (632,193)
Net loss per share - basic and diluted	$ (.10)	$ (.59)	$ (.17)
Weighted average shares outstanding - basic and diluted	4,005,455	3,836,618	3,801,155

</TABLE>

The accompanying notes are an integral part of these statements.

LECTEC CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

YEARS ENDED JUNE 30, 1998, 1997 AND 1996

<TABLE>
<CAPTION>

	Common stock		Additional paid-in capital	Unrealized losses on securities available-for-sale	Retained earnings (deficit)	Total shareholders' equity
	Shares	Amount				
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Balance, June 30, 1995	3,786,500	$37,865	$10,013,949	$(50,816)	$ 1,205,180	$11,206,178
Net loss	-	-	-	-	(632,193)	(632,193)
Cost of shares retired	(16,281)	(163)	(184,319)	-	-	(184,482)
Common shares issued upon exercise of options	65,581	656	450,536	-	-	451,192
Unrealized gain on securities available-for-sale	-	-	-	6,650	-	6,650
Tax benefit from exercise of stock options	-	-	88,000	-	-	88,000
Balance, June 30, 1996	3,835,800	38,358	10,368,166	(44,166)	572,987	10,935,345
Net loss	-	-	-	-	(2,266,727)	(2,266,727)
Cost of shares retired	(8,278)	(83)	(54,023)	-	-	(54,106)

Common shares issued upon exercise of options	15,278	153	51,690	–	–	51,843
Unrealized gain on securities available-for-sale	–	–	–	10,794	–	10,794
Investment by minority shareholders in consolidated subsidiary	–	–	83,595	–	–	83,595
Tax benefit from exercise of stock options	–	–	27,000	–	–	27,000
Balance, June 30, 1997	3,842,800	38,428	10,476,428	(33,372)	(1,693,740)	8,787,744
Net loss	–	–	–	–	(404,061)	(404,061)
Cost of shares retired	(10,863)	(109)	(40,627)	–	–	(40,736)
Common shares issued upon exercise of options	11,615	116	38,629	–	–	38,745
Unrealized gain on securities available-for-sale	–	–	–	24,864	–	24,864
Common shares issued to acquire minority shares of consolidated subsidiary	221,948	2,220	1,367,191	–	–	1,369,411
Shares repurchased	(29,500)	(295)	(124,268)	–	–	(124,563)
Warrants issued for services	–	–	50,000	–	–	50,000
Tax benefit from exercise of stock options	–	–	1,700	–	–	1,700
Balance, June 30, 1998	4,036,000	$40,360	$11,769,053	$ (8,508)	$(2,097,801)	$ 9,703,104

</TABLE>

The accompanying notes are an integral part of these statements.

LECTEC CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

<TABLE>
<CAPTION>

	Years ended June 30		
	1998	1997	1996
<S>	<C>	<C>	<C>
Cash flows from operating activities:			
Net loss	$ (404,061)	$(2,266,727)	$ (632,193)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Restructuring charge	--	2,180,353	--
Depreciation and amortization	844,594	1,014,251	1,128,103
Warrants issued for services	50,000	--	--
Loss on sales of investments	10,915	--	--
Deferred income taxes	(2,000)	(45,000)	65,000
Equity in losses of unconsolidated subsidiary	--	126,067	--
Changes in operating assets and liabilities:			
Trade and other receivables	(80,617)	(171,781)	161,057
Refundable income taxes	341,719	(25,683)	(256,040)
Inventories	859,010	(565,694)	(298,803)
Prepaid expenses and other	(18,192)	38,228	(29,011)
Accounts payable	29,448	(31,552)	123,375
Accrued expenses	(104,279)	(104,152)	(12,284)
Net cash provided by operating activities	1,526,537	148,310	249,204
Cash flows from investing activities:			
Purchase of property, plant and equipment	(406,515)	(187,040)	(430,956)
Investment in patents and trademarks	(62,999)	(104,705)	(164,796)
Sale of investments	590,873	--	--
Other	--	10,195	40,589
Net cash provided by (used in) investing activities	121,359	(281,550)	(555,163)
Cash flows from financing activities:			
Issuance of common stock	38,745	51,843	451,192
Retirement of common stock	(165,299)	(54,106)	(184,482)

Net cash provided by (used in) financing activities	(126,554)	(2,263)	266,710
Net increase (decrease) in cash and cash equivalents	1,521,342	(135,503)	(39,249)
Cash and cash equivalents at beginning of year	665,190	800,693	839,942
Cash and cash equivalents at end of year	$ 2,186,532	$ 665,190	$ 800,693

</TABLE>

The accompanying notes are an integral part of these statements.

LECTEC CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS - Continued

	Years ended June 30		
	1998	1997	1996
Supplemental disclosures:			
Cash paid during the year for interest	$ 1,106	$ 6,189	$ --
Cash paid during the year for income taxes	$16,732	$ 6,000	$33,199

Supplemental schedule of non-cash activities:

During fiscal 1998, the Company issued 221,948 shares of common stock in exchange for the minority interest in Pharmadyne, valued at $1,369,411.

The accompanying notes are an integral part of these statements.

LECTEC CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED JUNE 30, 1998, 1997 AND 1996

NOTE A - SUMMARY OF ACCOUNTING POLICIES

LecTec Corporation (the Company) is primarily engaged in the research, design, manufacture and sale of diagnostic electrodes, conductive hydrogels, medical tapes and therapeutic products. The Company sells and extends credit without collateral to customers located throughout the United States as well as Europe, the Middle East, Latin America, Canada and Asia. A summary of the Company's significant accounting policies consistently applied in the preparation of the accompanying financial statements follows:

Basis of Financial Statement Presentation

The consolidated financial statements include the accounts of LecTec Corporation ("LecTec"), LecTec International Corporation, a wholly-owned subsidiary, and Pharmadyne Corporation, a wholly-owned owned subsidiary which was merged into LecTec Corporation on December 31, 1997 (note G). All material intercompany accounts and transactions have been eliminated.

Cash and Cash Equivalents

The Company considers all highly liquid temporary investments with an original maturity of three months or less to be cash equivalents. Cash equivalents consist primarily of short-term commercial paper.

Investments

The Company's investments are classified as available-for-sale and are reported at fair value. In 1997, the investments consisted of a preferred stock fund classified as short-term. The Company utilizes the specific identification method in computing realized gains and losses.

Inventories

Inventories are stated at the lower of cost (determined on a first-in, first-out basis) or market and consist of the following:

	June 30	
	1998	1997
Raw materials	$1,184,778	$1,655,924
Work in process	15,055	184,208
Finished goods	518,178	736,889
	$1,718,011	$2,577,021

NOTE A - SUMMARY OF ACCOUNTING POLICIES - Continued

Depreciation and Amortization

Depreciation is provided in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives. The straight-line method of depreciation is followed for financial reporting purposes, and accelerated methods are used for tax purposes. Estimated useful lives used in the calculation of depreciation for financial statement purposes are:

Buildings and improvements	5 - 40 years
Equipment	4 - 15 years
Furniture and fixtures	5 - 7 years

The investment in patents and trademarks consists primarily of the cost of applying for patents and trademarks. Patents and trademarks are amortized on a straight-line basis over the estimated useful life of the asset, generally five years.

Revenue Recognition

Sales are recognized at the time of shipment of product against a confirmed sales order.

Stock Options

The Company accounts for the issuance of stock options using the intrinsic value method.

Net Earnings (Loss) Per Share

On December 31, 1997, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 128 "Earnings per Share." All current and prior year net earnings (loss) per share data have been restated to conform to the provisions of SFAS 128.

The Company's basic net earnings (loss) per share amounts are computed by dividing net earnings (loss) by the weighted average number of outstanding common shares. The Company's diluted net earnings per share amounts are computed by dividing net earnings by the weighted average number of outstanding common shares and common share equivalents, when dilutive. Options and warrants to purchase 795,997, 628,062 and 478,500 shares of common stock with a weighted average exercise price of $8.09, $8.82 and $8.25 were outstanding during the years ended June 30, 1998, 1997 and 1996, but were excluded because they were antidilutive.

Use of Estimates

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

NOTE A - SUMMARY OF ACCOUNTING POLICIES - Continued

Reclassifications

Certain 1997 and 1996 amounts have been reclassified to conform to the 1998 financial statement presentation.

New Accounting Pronouncements

SFAS No. 130, "Reporting Comprehensive Income," and SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," are effective for fiscal years beginning after December 15, 1997.

SFAS 130 requires a company to display an amount representing comprehensive income, as defined by the statement, as part of the company's basic financial statements. Comprehensive income will include items such as unrealized gains or losses on certain investment securities and foreign currency items. SFAS 131 requires a company to disclose financial and other information, as defined by the statement, about its business segments, their products and services, geographic areas, major customers, sales, profits, assets and other information.

The adoption of these statements is not expected to have a material effect on the consolidated financial statements of the Company.

NOTE B - LINE OF CREDIT

The Company has an unsecured $1,000,000 working capital line of credit through September 1, 1998 with interest at the bank's reference rate (effective rate of 8.5% at June 30, 1998 and 1997). There were no borrowings outstanding on the line of credit as of June 30, 1998 or 1997, nor during the fiscal years then ended. The credit agreement contains certain restrictive covenants which require the Company to maintain, among other things, specified levels of working capital and net worth and certain financial ratios. At June 30, 1998, the Company was in compliance with all such covenants. Management believes the Company will be able to renew its line of credit.

NOTE C - COMMITMENTS AND CONTINGENCIES

The Company conducts portions of its operations in a leased facility. The lease provides for payment of a portion of taxes and other operating expenses by the Company.

The minimum rental commitments under all operating leases, which expire at various times through June 30, 2002, are as follows for the years ending June 30:

1999	$ 241,511
2000	250,535
2001	255,328
2002	255,899
	$1,003,273

NOTE C - COMMITMENTS AND CONTINGENCIES - Continued

Total rent expense for operating leases was $248,931, $224,849 and $219,095 for the years ended June 30, 1998, 1997 and 1996.

The Company is subject to various legal proceedings in the normal course of business. Management believes these proceedings will not have a material adverse effect on the Company's financial position or results of operations.

NOTE D - INCOME TAXES

The provision for income taxes consists of the following:

	Years ended June 30		
	1998	1997	1996
Current			
Federal	$(1,000)	$ 43,000	$(17,000)
State	2,000	2,000	2,000
	1,000	45,000	(15,000)
Deferred			
Federal	(2,000)	(45,000)	(23,000)

State	–	–	–
	(2,000)	(45,000)	(23,000)
	$(1,000)	$ –	$(38,000)

Deferred tax assets and liabilities represent the tax effects, based upon current tax law, of cumulative future deductible or taxable items that have been recognized in the financial statements as follows:

	June 30	
	1998	1997
Deferred current assets and liabilities:		
Net operating loss carryforwards	$ 1,147,800	$ 1,006,800
Tax credit carryforwards	244,900	260,000
Inventory capitalization and reserve	146,800	124,800
Vacation pay accrual	63,700	37,800
Other	46,100	4,400
	1,649,300	1,433,800
Valuation allowance	(1,270,300)	(1,067,800)
Net current asset	$ 379,000	$ 366,000

NOTE D – INCOME TAXES – Continued

Deferred long-term assets and liabilities:		
Tax depreciation in excess of book depreciation	$(289,700)	$ (293,100)
Charitable contribution carryforwards	18,400	64,400
Other	49,300	46,400
	(222,000)	(182,300)
Valuation allowance	–	(28,700)
Net long-term liability	$(222,000)	$ (211,000)

At June 30, 1998, the Company has available net operating loss carryforwards of approximately $3,400,000 which can be used to reduce future taxable income. The utilization of a portion of these net operating loss carryforwards is restricted under Section 382 of the Internal Revenue Code due to past ownership changes. These net operating loss carryforwards begin to expire in 2007. A valuation allowance has been recorded for these net operating loss carryforwards as they may not be realizable.

At June 30, 1998, the Company has available tax credit carryforwards of approximately $245,000 which can be used to reduce future tax liabilities. These carryforwards begin to expire in 2008. A valuation allowance has been recorded for a portion of the tax credit carryforwards as they may not be fully realizable.

Differences between income tax benefit and the statutory federal income tax rate of 34% are as follows:

	1998	1997	1996
Federal statutory income tax rate	(34.0)%	(34.0)%	(34.0)%
State income taxes, net of federal effect	0.3	0.1	0.2
Nondeductible restructuring charge	–	34.6	–
Foreign sales corporation	(11.1)	(2.1)	(5.5)
Losses producing no current benefit	58.0	.6	25.7
Tax exempt investment income	(1.7)	(0.8)	(0.8)
Goodwill amortization	–	2.3	10.0
Prior years' overaccruals	(3.7)	–	–
Other	(8.0)	(.7)	(1.3)
	(0.2)%	– %	(5.7)%

NOTE E – EMPLOYEE BENEFIT PLAN

The Company maintains a contributory 401(k) profit sharing benefit plan covering substantially all employees who have completed one hour of service. The Company matches 50% of voluntary employee contributions to the plan not to exceed 50% of a maximum 5% of a participant's compensation. The Company's contributions under this plan were $54,901, $37,936 and $44,549 for the years

ended June 30, 1998, 1997 and 1996. The Company may also make a discretionary contribution. No discretionary contributions were made for the years ended June 30, 1998, 1997 and 1996.

NOTE F - STOCK OPTIONS AND WARRANTS

The Company has stock option plans for the benefit of selected officers, employees and directors of the Company. A total of 973,049 shares of common stock are reserved for issuance under the plans. Options under the Company's plans are granted at fair market value and expire ten years from the grant date. Options given to directors are exercisable at the date of grant. Options given to selected officers and employees are exercisable at such times as set forth in the individual option agreements, generally vesting 100% after four years.

A summary of the Company's stock option transactions for the years ended June 30, 1998, 1997 and 1996 is as follows: Weighted average Number of shares exercise price

	Number of shares	Weighted average exercise price
Outstanding at June 30, 1995	477,796	$ 7.99
Granted	133,500	10.18
Exercised	(65,581)	6.87
Canceled	(21,020)	8.92
Outstanding at June 30, 1996	524,695	8.65
Granted	343,350	8.26
Exercised	(15,278)	3.39
Canceled	(129,934)	9.30
Outstanding at June 30, 1997	722,833	8.46
Granted	219,000	5.31
Exercised	(11,615)	3.35
Canceled	(82,598)	6.37
Outstanding at June 30, 1998	847,620	$ 7.86

A total of 459,994, 371,946 and 264,945 options were exercisable at June 30, 1998, 1997 and 1996, with a weighted average price of $8.35, $8.30 and $7.50.

The following information applies to grants that are outstanding at June 30, 1998:

<TABLE>
<CAPTION>

	Options outstanding			Options exercisable	
Range of exercise prices	Number outstanding	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable	Weighted average exercise price
<S> <C>	<C>	<C>	<C>	<C>	<C>
$3.34 - $ 5.00	174,974	8.1 years	$4.70	52,474	$4.08
6.00 - 8.62	300,260	6.9 years	7.08	141,759	7.59
9.00 - 13.50	372,386	5.1 years	9.97	265,761	9.60

</TABLE>

NOTE F - STOCK OPTIONS AND WARRANTS - Continued

The weighted average fair value of the options granted during 1998, 1997 and 1996 were $2.77, $4.45 and $5.23. The fair value of each option grant is estimated on the date of grant using the Black-Scholes options-pricing model with the following weighted-average assumptions used for all grants in 1998, 1997 and 1996: zero dividend yield, expected volatility of 52%, 54% and 59%, risk-free interest rate of 5.57%, 6.22% and 6.04% and expected lives of 5.16, 5.09 and 4.52 years.

The Company's net loss and net loss per share for 1998, 1997 and 1996 would have been increased to the pro forma amounts indicated below had the fair value method been used for options granted to employees and directors. These effects may not be representative of the future effects of applying this method.

<TABLE>
<CAPTION>

	1998		1997		1996	
	As reported	Pro forma	As reported	Pro forma	As reported	Pro forma
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Net loss	$(404,061)	$(897,365)	$(2,266,727)	$(2,620,449)	$(632,193)	$(781,467)
Net loss per share - basic/diluted	$(.10)	$(.22)	$(.59)	$(.68)	$(.17)	$(.21)

</TABLE>

During 1998, the Company issued a warrant to an outside consultant for the purchase of 12,953 shares of the Company's common stock at $6.25 per share, expiring November 20, 2004, in exchange for recruiting and placement services. The fair value of the warrant granted was calculated on the date of grant using the Black-Scholes option-pricing model.

NOTE G - PHARMADYNE CORPORATION AND RESTRUCTURING

During 1993 through 1996, the Company made various investments in and advances to Pharmadyne Corporation resulting in a cumulative ownership of 61%.

During 1997, the Company adopted a plan for eliminating the Pharmadyne subsidiary and recorded a nonrecurring restructuring charge of $2,180,353 which increased the 1997 net loss by $.57 per share. The restructuring charge included approximately $1,369,000 for the planned acquisition of the minority interests in Pharmadyne in exchange for newly issued shares of LecTec Corporation common stock, $480,000 for the write-off of Pharmadyne's 15% interest in Natus, L.L.C., an Arizona-based direct marketing company, and $331,000 for completion of restructuring activities, consisting primarily of fees for professional services. In October 1997, the Company issued 221,948 new shares of its common stock to acquire the minority interests in Pharmadyne. In November 1997, the newly issued shares were registered with the Securities and Exchange Commission. On December 31, 1997, Pharmadyne Corporation was merged into LecTec Corporation.

NOTE H - DISPOSITION OF DIRECT MARKETING RELATED ASSETS

On March 12, 1996, the Company contributed the direct marketing related assets of Pharmadyne to Natus L.L.C. (an Arizona limited liability company) in exchange for a 15% interest in Natus L.L.C. This investment was accounted for using the equity method.

During 1997 the Company recorded $126,067 of equity in the losses of Natus L.L.C. The investment in Natus L.L.C. of $480,100 was fully written off in 1997 as part of the restructuring charge (note G).

NOTE I - MAJOR CUSTOMERS AND EXPORT SALES

One customer accounted for 18%, 19% and 17% of total sales for the years ended June 30, 1998, 1997 and 1996. The accounts receivable from this customer represented 18% and 27% of trade receivables at June 30, 1998 and 1997 and the accounts receivable from another customer represented 10% and 12% of trade receivables at June 30, 1998 and 1997. Export sales accounted for approximately 26% of total sales during the year ended June 30, 1998 and 19% of total sales during each of the years ended June 30, 1997 and 1996. Export sales by geographic area were as follows:

	Years ended June 30		
	1998	1997	1996
Europe	$1,705,996	$1,456,141	$1,652,941
Middle East	912,240	14,854	295,159
Latin America	371,854	484,319	225,440
Canada	199,082	117,966	80,746
Asia	62,027	132,590	32,366
Other	71,949	82,062	139,252

$3,323,148	$2,287,932	$2,425,904
==========	==========	==========

NOTE J - STOCK REPURCHASE PROGRAM

In April 1998, the Company's Board of Directors authorized a stock repurchase program pursuant to which up to 500,000 shares, or approximately 12.4% of the Company's outstanding common stock, may be repurchased. The shares may be purchased from time to time through open market transactions, block purchases, tender offers, or in privately negotiated transactions. The total consideration for all shares repurchased under this program cannot exceed $2,000,000. During the year ended June 30, 1998, 29,500 shares were repurchased for $124,563. During the period from July 1, 1998 through August 11, 1998 the Company repurchased an additional 54,150 shares for $186,400.

ITEM 9.

CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information required under this item with respect to directors will be included under the heading "Election of Directors" in the Company's definitive Proxy Statement for the Annual Meeting of Shareholders to be held November 19, 1998, and is incorporated herein by reference. The information required under this item with respect to executive officers is included under the heading "Executive Officers of the Registrant" of Item 1 of this Form 10-K.

ITEM 11. EXECUTIVE COMPENSATION

The information required under this item will be included under the heading "Executive Compensation" in the Company's definitive Proxy Statement for the Annual Meeting of Shareholders to be held November 19, 1998, and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information required under this item will be included under the heading "Security Ownership of Certain Beneficial Owners and Management" in the Company's definitive Proxy Statement for the Annual Meeting of Shareholders to be held November 19, 1998, and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Information required under this item with respect to certain relationships and related transactions will be included under the heading "Certain Relationships and Related Transactions" in the Company's definitive Proxy Statement for the Annual Meeting of Shareholders to be held on November 19, 1998, and is incorporated herein by reference.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

(a) Financial Statements, Schedules and Exhibits

1. Financial Statements

The following consolidated financial statements of the Company and its subsidiaries are filed as a part of this Form 10-K in Part II, Item 8:

(i) Report of Independent Certified Public Accountants
(ii) Consolidated Balance Sheets at June 30, 1998 and 1997
(iii) Consolidated Statements of Operations for the years ended June 30, 1998, 1997 and 1996

(iv) Consolidated Statements of Shareholders' Equity for the years ended June 30, 1998, 1997 and 1996
(v) Consolidated Statements of Cash Flows for the years ended June 30, 1998, 1997 and 1996
(vi) Notes to the Consolidated Financial Statements

2. Financial Statement Schedules :

All schedules have been omitted since the required information is not present or not present in amounts sufficient to require submission of the schedule, or because the information required is included in the financial statements or the notes thereto.

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3. Exhibits

		Method of Filing
<S>	<C>	<C>
3.01	Articles of Incorporation of Registrant, as amended	(1)
3.02	By-laws of Registrant	(1)
10.01	Service Agreement dated July 1, 1986, between LecTec International, Inc., a U.S. Virgin Islands corporation, and LecTec Corporation, relating to the sale, lease or rental of certain property outside the United States.	(1)
10.02	Distribution and Commission Agreement dated July 1, 1986, between LecTec International, Inc., a U.S. Virgin Islands corporation, and LecTec Corporation, relating to the sale, lease or rental of certain property outside the United States.	(1)
10.03	Certificate of Secretary pertaining to Resolution of Board of Directors of LecTec Corporation, dated October 30, 1986, implementing a Profit Sharing Bonus Plan.	(1)
10.04	Research Agreement dated December 31, 1991, between LecTec Corporation and the University of Minnesota, whereby LecTec Corporation received exclusive rights to market and sell	

	a non-nicotine compound to be mutually developed for smoking cessation.	(2)
10.05	Assignment and Mutual Release Agreement dated March 9, 1993 between Pharmaco Behavioral Associates, Inc., Robert M. Keenan, Ph.D., M.D. and the University of Minnesota, whereby the University assigned title, royalty and patent rights associated with the technology to alleviate symptoms of tobacco withdrawal to Pharmaco Behavioral Associates, Inc. and Dr. Keenan. Also included is a mutual release of all parties on all past title, royalty and patent rights.	(2)
10.06	License Agreement dated March 9, 1993 between Pharmaco Behavioral Associates, Inc. and LecTec Corporation, whereby the Company received an exclusive, worldwide license to market, make and sublicense product associated with the technology to alleviate symptoms of tobacco withdrawal.	(2)
10.07	Consultant Contract and Invention Assignment dated March 9, 1993 between Robert Keenan, Ph.D., M.D. and LecTec Corporation, whereby the Company received assignment of patent and invention rights associated with the technology to alleviate symptoms of tobacco withdrawal including provisions that the Company enter into a consulting agreement with Dr. Keenan.	(2)
10.08	Marketing and Distribution Agreement dated January 11, 1996 between LecTec Corporation, Pharmadyne Corporation (formerly Natus Corporation) and CNS, Inc. regarding an analgesic pain patch	(3)
10.09	LecTec Corporation 1989 Stock Option Plan	(4)
10.10	LecTec Corporation 1991 Directors' Stock Option Plan	(4)
10.11	Building lease dated May 24, 1991 between LecTec Corporation and Sierra Development Co. for the lease of the manufacturing and warehouse facility located in Edina, Minnesota	(4)

10.12	First amendment dated May 5, 1997 between LecTec Corporation and Rushmore Plaza Partners Limited Partnership for the extension of the previous lease of the manufacturing and warehouse facility located in Edina, Minnesota	(4)
10.13	Credit Agreement dated August 22, 1997 between LecTec Corporation and The First National Bank of Saint Paul, a national banking association, whereby LecTec Corporation has an unsecured $1 million working capital line of credit	(4)
10.14	Revolving Credit Note dated August 22, 1997 between LecTec Corporation and The First National Bank of Saint Paul, a national banking association	(4)

10.15	Articles of Merger of Pharmadyne Corporation into LecTec Corporation dated December 31, 1997 , whereby Pharmadyne, a wholly-owned subsidiary, is merged into LecTec Corporation	(5)
10.16	Change In Control Termination Pay Plan adopted May 27, 1998, for the benefit of certain employees of LecTec Corporation in the event of a Change in Control	(5)
*10.17	Termination Agreement dated July 30, 1998 between LecTec Corporation and CNS, Inc., whereby the Marketing and Distribution Agreement date January 11, 1996 is terminated	(5)
21.01	Subsidiaries of the Company	(5)
23.01	Consent of Grant Thornton LLP	(5)
27.01	Financial Data Schedule	(5)

</TABLE>

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* Confidential treatment requested for portions of this Exhibit pursuant to Rule 24b-2 under the Securities Exchange Act of 1934 as amended, the confidential portions have been deleted and filed separately with the Securities and Exchange Commission together with a confidential treatment request

(1) Incorporated herein by reference to the Company's Form S-18 Registration Statement (file number 33-9774C) filed on October 31, 1986 and amended on December 12, 1986.

(2) Incorporated herein by reference to the Company's Annual Report on Form 10-K for the year ended June 30, 1993.

(3) Incorporated herein by reference to the Company's Annual Report on Form 10-K for the year ended June 30, 1996.

(4) Incorporated herein by reference to the Company's Annual Report on Form 10-K for the year ended June 30, 1997.

(5) Filed herewith.

(b) 1. Reports on Form 8-K.

None.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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, on the 25th day of September, 1998.

LECTEC CORPORATION

/s/Rodney A. Young

Rodney A. Young
Chairman, Chief Executive Officer and President

(Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the date indicated.

/s/Rodney A. Young *Rodney A. Young* *Chairman, Chief Executive Officer and President* *(Principal Executive Officer)*	*September 25, 1998*
/s/Deborah L. Moore *Deborah L. Moore* *Chief Financial Officer and Secretary* *(Principal Financial Officer and Accounting Officer)*	*September 25, 1998*
/s/Lee M. Berlin *Lee M. Berlin* *Director*	*September 25, 1998*
/s/Alan C. Hymes *Alan C. Hymes* *Director*	*September 25, 1998*
/s/Paul O. Johnson *Paul O. Johnson* *Director*	*September 25, 1998*

EXHIBIT INDEX

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*10.17 Termination Agreement dated July 30, 1998 between LecTec Corporation and CNS, Inc., whereby the Marketing and Distribution Agreement date January 11, 1996 is terminated . . . . . .

21.01 Subsidiaries of the Company . . . . . .

23.01 Consent of Grant Thornton LLP. . . . . .

27.01 Financial Data Schedule. . . . . .

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(4) Incorporated herein by reference to the Company's Annual Report on Form 10-K for the year ended June 30, 1997.

EXHIBIT 10.15

ARTICLES OF MERGER
OF
PHARMADYNE CORPORATION
INTO
LECTEC CORPORATION

The undersigned, Rodney A. Young, the Chairman, Chief Executive Officer and President of LecTec Corporation, a Minnesota corporation, hereby certifies as follows:

1. The plan of merger attached hereto as Exhibit A, for the merger into LecTec Corporation of its wholly-owned subsidiary, Pharmadyne Corporation, a Minnesota corporation, was duly adopted by the board of directors of LecTec Corporation on November 20, 1997.

2. The number of outstanding shares of Pharmadyne Corporation is 747,282 shares of common stock. All of the outstanding shares of such common stock are owned by LecTec Corporation.

3. Since Pharmadyne Corporation has no shareholders other than LecTec Corporation, no copy of the plan of merger was mailed to any shareholder of Pharmadyne Corporation.

IN WITNESS WHEREOF, the undersigned, Chairman, Chief Executive Officer and President of LecTec Corporation, being duly authorized on behalf of LecTec Corporation, has executed this document this 31st day of December, 1997.

LECTEC CORPORATION

/S/Rodney A. Young

Rodney A. Young, Chairman,
Chief Executive Officer and President

EXHIBIT A

PLAN OF MERGER
OF
PHARMADYNE CORPORATION
INTO
LECTEC CORPORATION

1. The name of the subsidiary corporation is Pharmadyne Corporation.

2. The name of the parent and surviving corporation is LecTec Corporation.

3. The merger shall be effective when articles of merger are filed with the Minnesota secretary of state (the "Effective Date").

4. Upon the Effective Date of the merger, all outstanding shares of each class and series of stock of Pharmadyne Corporation shall be cancelled, and no shares of LecTec Corporation shall be issued in lieu thereof.

5. Upon the Effective Date, the provisions of section 302A.641, subdivisions 2 and 3 of the Minnesota Business Corporation Act shall apply.

EXHIBIT 10.16

LECTEC CORPORATION

CHANGE IN CONTROL
TERMINATION PAY PLAN

LECTEC CORPORATION

CHANGE IN CONTROL
TERMINATION PAY PLAN

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SECTION 1

INTRODUCTION

Effective May 27, 1998, LecTec Corporation, a Minnesota corporation (hereinafter sometimes referred to as "Employer"), hereby creates a change in control termination pay plan for the benefit of certain employees of the Employer in the event of a Change in Control. Capitalized terms used herein shall have the meaning provide in Section 9.

SECTION 2

PARTICIPATION

All Participants in the Plan shall be identified in Schedule A attached. Participants shall be classified as Class I or Class II Participants. An employee who has become a Participant shall be considered to continue as a Participant in the Plan until the date of the Participant's death or, if earlier, the date when the Participant is no longer employed by the Employer; provided, however, that a Participant who has a Termination of Employment within 12 months following the date of a Change in Control will not cease to be a Participant.

SECTION 3

TERMINATION OF EMPLOYMENT

3.1 NOTICE OF TERMINATION. Any purported termination of a Participant's employment by the Employer or the Participant (including a Termination of Employment) (other than by reason of the Participant's death) within twelve (12) months following the month in which a Change in Control occurs, shall be communicated by Notice of Termination to the other. No purported termination by the Employer of a Participant's employment shall be effective if it is not pursuant to a Notice of Termination. Failure by a Participant to provide Notice of Termination shall not limit any rights of the Participant under the Plan except to the extent the Employer can demonstrate that it suffered actual damages by reason of such failure.

3.2 PARTICIPANT'S TERMINATION RIGHTS. A Participant's right to terminate his or her employment pursuant to the terms of the Plan shall not be affected by the Participant's incapacity due to physical or mental illness. A Participant's continued employment shall not constitute consent to, or a waiver of rights with respect to, any circumstance constituting Good Reason pursuant to the terms of the Plan. Termination by a Participant of the Participant's employment for Good Reason shall constitute termination for Good Reason for all purposes of the Plan, notwithstanding that the Participant may also thereby be deemed to have "retired" under any applicable retirement programs of the Employer.

SECTION 4

TERMINATION PAYMENT

4.1 QUALIFICATION. To qualify for a termination payment under the Plan, a Participant must (a) be a Participant as of the date of the Change in Control, and (b) have a Termination of Employment within 12 months following a Change in Control.

4.2 AMOUNT. Subject to the eligibility requirement set forth in Section 4.1, and the limitations set forth in Section 4.4 and Section 5, termination payments for Class I and Class II Participants shall be determined as follows:

4.2.1 CLASS I PARTICIPANTS. Termination payments shall be made to a Class I Participant in a single sum in an amount equal to the sum of (a) twenty (20) times the Class I Participant's highest monthly base compensation during the six (6) months immediately before the Date of Termination, and (b) all annual incentive payments that the Class I Participant would have received for the year in which the Date of Termination occurs, had required performance targets been met, which shall be deemed to have occurred on the Date of Termination, whether or not they have occurred or could possibly occur.

Additionally, the Class I Participant shall receive the following: (a) until the end of the twentieth (20th) month following the month in which occurs the Class I Participant's Date of Termination, the Employer will arrange to provide the Class I Participant with welfare benefits (including life and health insurance benefits) and other employee benefits of substantially similar design and cost (to the Class I Participant) as the welfare benefits and other employee benefits available to the Class I Participant immediately prior to the Notice of Termination or immediately prior to the date of the Change in Control, whichever is greater; but benefits otherwise receivable by the Class I Participant pursuant to this clause (a) shall be discontinued if the Class I Participant obtains full-time employment providing welfare benefits during such period following such termination; and (b) group outplacement counseling services for twenty (20) months from the Date of Termination up to $10,000 in value. Notwithstanding the foregoing, the Employer shall not be required to continue to provide disability benefits following a Class I Participant's Date of Termination other than with respect to benefits to which the Class I Participant became entitled prior to the Date of Termination and which are required to be paid following such Date of Termination in accordance with the terms of applicable disability plans or policies in effect prior to such Date of Termination. The Class I Participant shall not be required to mitigate the amount of any payment provided for under the Plan by seeking other employment or otherwise, nor shall the amount of any payment provided for under the Plan be reduced by any compensation earned by the Class I Participant as the result of employment by another employer after the Date of Termination, or otherwise, except as set forth in clause (a) of this paragraph.

4.2.2 CLASS II PARTICIPANTS. Termination payments shall be made to a Class II Participant in a single sum in an amount equal to the sum of (a) twelve (12) times the Class II Participant's highest monthly base compensation during the six (6) months immediately before the Date of Termination, and (b) all annual incentive payments that the Class II Participant would have received for the year in which the Date of Termination occurs, had required performance targets been met, which shall be deemed to have occurred on the Date of Termination, whether or not they have occurred or could possibly occur.

Additionally, the Class II Participant shall receive the following: (a) until the end of the twelfth (12th) month following the month in which occurs the Class II Participant's Date of Termination, the Employer will arrange to provide the Class II Participant with welfare benefits (including life and health insurance benefits) and other employee benefits of substantially similar design and cost (to the Class II Participant) as the welfare benefits and other employee benefits available to the Class II Participant immediately prior to the Notice of Termination or immediately prior to the date of the Change in Control, whichever is greater; but benefits otherwise receivable by the Class II Participant pursuant to this clause (a) shall be discontinued if the Class II Participant obtains full-time employment providing welfare benefits during such period following such termination; and (b) group outplacement counseling services for twelve (12) months from the Date of Termination up to $5,000 in value. Notwithstanding the foregoing, the Employer shall not be required to continue to provide disability benefits following a Class II Participant's Date of Termination other than with respect to benefits to which the Class II

Participant became entitled prior to the Date of Termination and which are required to be paid following such Date of Termination in accordance with the terms of applicable disability plans or policies in effect prior to such Date of

Termination. The Class II Participant shall not be required to mitigate the amount of any payment provided for under the Plan by seeking other employment or otherwise, nor shall the amount of any payment provided for under the Plan be reduced by any compensation earned by the Class II Participant as the result of employment by another employer after the Date of Termination, or otherwise, except as set forth in clause (a) of this paragraph.

4.3 TIME AND FORM OF CASH PAYMENT. If a Participant is eligible to receive a cash termination payment under the Plan, payment will be made to the Participant in a single lump sum cash payment within sixty (60) days after the Date of Termination. If a Participant should die before the Participant actually receives payment, payment will be made to the Participant's estate.

4.4 ERISA LIMITATION. No termination payment under the Plan shall in the aggregate provide for payment in excess of twice a Participant's annual compensation during the Plan Year immediately preceding the termination of the Participant's employment. Annual compensation for determining the limitation in the preceding sentence means the total of all compensation, including wages, salary, incentive payments, and any other benefit of monetary value, whether paid in the form of cash or otherwise, which was paid as consideration for a Participant's service during the year, or which should have been so paid at the Participant's usual rate and compensation if the Participant had worked a full year. To the extent that a termination payment would exceed the foregoing limitation, payment under the Plan shall be reduced.

4.5 LEGAL FEES AND EXPENSES. The Employer will pay any legal fees and expenses incurred by a Participant (a) as a result of successful litigation against the Employer or Employer for nonpayment of any benefit under the Plan or (b) in connection with any dispute with any Federal, state or local governmental agency with respect to benefits claimed under the Plan. If the Participant utilizes arbitration to resolve any such dispute, the Employer will pay any legal fees and expenses incurred by the Participant in connection therewith.

SECTION 5

280G LIMITATION

The amount of any cash payment to be received by a Participant pursuant to the Plan shall be reduced (but not below zero) by the amount, if any, necessary to prevent any part of any payment or benefit received or to be received by the Participant in connection with a Change in Control of the Employer or the termination of the Participant's employment (whether payable pursuant to the terms of the Plan or any other plan, contract, agreement or arrangement with the Employer, with any person whose actions result in a Change in Control of the Employer or with any person constituting a member of an "affiliated group" (as defined in section 280G(d)(5) of the Code)) (such foregoing payments or benefits referred to collectively as the "Total Payments"), from being treated as an "excess parachute payment" within the meaning of section 280G(b)(1) of the Code, but only if and to the extent such reduction will also result in, after taking into account all applicable state or federal taxes (computed at the highest marginal rate) including any taxes payable pursuant to section 4999 of the Code, a greater after-tax benefit to the Participant than the after-tax benefit to the Participant of the Total Payments computed without regard to any such reduction. For purposes of the foregoing, (a) no portion of the Total Payments shall be taken into account which in the opinion of tax counsel selected by the Employer and acceptable to the Participant does not constitute a "parachute payment" within the meaning of section 280G(b)(2) of the Code; (b) any reduction in payments pursuant to the Plan shall be computed by taking into account that portion of Total Payments which constitute reasonable compensation within the meaning of section 280G(b)(4) of the Code in the opinion of such tax counsel; (c) the value of any non-cash benefit or of any deferred cash payment included in the Total Payments shall be determined by the Employer in accordance with the principles of section 280G(d)(4) of the Code; and (d) in the event of any uncertainty as to whether a reduction in Total Payments to the Participant is required pursuant to the Plan, the

Employer shall initially make the payment to the Participant and the Participant shall be required to refund to the Employer any amounts ultimately determined not to have been payable under the terms of the Plan.

SECTION 6

AMENDMENT OR TERMINATION OF THE PLAN

The Plan may not be amended if any amendment would adversely affect the rights, expectancies or benefits of any Participant under the Plan (as in effect immediately prior to the amendment) unless such amendment is consented to in writing by 75% of all Participants under the Plan (including the estate of any deceased Participant if the estate would have a claim for benefits under the Plan) on the effective date of such amendment. Similarly the Plan may not be terminated unless such termination is consented to in writing by 75% of all such Participants on the date of such termination. If any of these actions are taken, affected Participants will be notified. Except to the extent benefits have become payable but have not actually been paid, the Plan terminates automatically on the second anniversary of the date of a Change in Control.

SECTION 7

MISCELLANEOUS PROVISIONS

7.1 NONEXCLUSIVITY OF RIGHTS. Nothing in the Plan shall prevent or limit any Participant's continuing or future participation in any benefit, bonus, incentive, retirement or other plan or program provided by the Employer and for which the Participant may qualify, nor shall anything in the Plan limit or reduce such rights as any Participant may have under any other agreement with, or plan, program, policy or practice of, the Employer. Amounts which are vested benefits or which a Participant is otherwise entitled to receive under any agreement with, or plan, program, policy or practice of, the Employer shall be payable in accordance with such agreement, plan, program, policy or practice, except as explicitly modified by the Plan.

7.2 SUCCESSORS. The Employer will require any successor (whether direct or indirect, by purchase, merger, consolidation, or otherwise) to all or substantially all of the business and/or assets of the Employer or of any division or subsidiary thereof employing any Participant to expressly assume and agree to perform under the terms of the Plan in the same manner and to the same extent that the Employer would be required to perform if no such succession had taken place. Failure of the Employer to obtain such assumption and agreement prior to the effectiveness of any such succession shall entitle each affected Participant to compensation from the Employer in the same amount and on the same terms as the Participant would be entitled under the Plan if the Participant terminated employment for Good Reason following a Change in Control, except that for purposes of implementing the foregoing, the date on which any such succession becomes effective shall be deemed the Date of Termination and Notice of Termination shall be deemed to have been given on such date.

7.3 NOTICE. Notices and all other communications provided for under the Plan shall be in writing and shall be deemed to have been duly given when delivered or mailed by United States registered mail, postage prepaid, addressed to the other party as follows:

If to the Employer, to:

LecTec Corporation
Attention: Corporate Secretary
10701 Red Circle Drive
Minnetonka, Minnesota 55343

If to the Participant, to the address shown on the records of the Employer, which the Employer shall keep up to date.

Either party may change its address for purposes of this Section 7.3 by giving appropriate notice to the other party.

7.4 GOVERNING LAW. The validity, interpretation and construction of the Plan shall be governed by the laws of the State of Minnesota, except to the extent that federal law controls.

7.5 VALIDITY. The invalidity or unenforceability of any provision of the Plan shall not affect the validity or enforceability of any other provision of the Plan, which shall remain in full force and effect.

7.6 EMPLOYMENT. The Plan does not constitute a contract of employment or impose on the Employer any obligation to retain any Participant as an employee, to continue any Participant's current employment status or to change any employment policies of the Employer.

7.7. TERMINATION PRIOR TO A CHANGE IN CONTROL. Any termination of the Participant's employment by the Employer without Cause prior to a Change in Control which occurs at the request or insistence of any person (other than the Employer) in connection with a Change in Control shall be deemed to have occurred after the Change in Control for purposes of the Plan.

SECTION 8

CLAIMS PROCEDURE

8.1 GENERAL. If a Participant believes that he or she may be entitled to benefits, or the Participant is in disagreement with any determination that has been made, the Participant may present a claim to the Employer.

8.2 MAKING A CLAIM. A Participant's claim must be written and must be delivered to the Employer. Within 30 days after delivery of such claim, the Participant shall receive either: (a) a decision; or (b) a notice describing special circumstances requiring a specified amount of additional time (but no more than 60 days from the date of delivery of such claim) to reach a decision.

If such claim is wholly or partially denied, the Participant shall receive a written notice specifying: (a) the reasons for denial; (b) the Plan provisions on which the denial is based; and (c) any additional information needed from the Participant in connection with the claim and the reason such information is needed. The Participant also shall receive a copy of Section 8.3 below concerning the Participant's right to request a review.

8.3 REQUESTING REVIEW OF A DENIED CLAIM. A Participant may request that a denied claim be reviewed. Such request for review must be written and must be delivered to the Employer within 30 days after the Participant receives the written notice that the Participant's claim was denied. Such request for review may (but is not required to) include issues and comments the Participant wants considered in the review. The Participant may examine pertinent Plan documents by asking the Employer. Within 30 days after delivery by the Participant of the Participant's request for review, the Participant shall receive either: (a) a decision; or (b) a notice describing special circumstances requiring a specified amount of additional time (but no more than 60 days from the date of delivery of such request for review) to reach a decision. The decision shall be in writing and shall specify the Plan provisions on which it is based.

8.4 EXHAUSTION OF ADMINISTRATIVE REMEDIES. No Participant (nor the estate of any deceased Participant) may commence any legal action to recover Plan benefits or to enforce or clarify rights under

the Plan under Section 502 or Section 510 of ERISA, or under any other provision of law, whether or not statutory, until the claims and review procedures set forth herein have been exhausted in their entirety.

8.5 DECISIONS. All decisions on claims and on reviews of denied claims will be made by the Employer. The Employer may, in its discretion, hold one or more hearings. If a Participant does not receive a decision within the specified time, the Participant should assume. that the claim was denied or re-denied on the date the specified time expired. The Employer reserves the right to delegate its authority to make decisions.

SECTION 9

DEFINITIONS

When the following terms are used in this document with initial capital letters, they shall have the following meanings.

9.1 CAUSE -- shall mean (i) the willful and continued failure by a Participant to resume substantial performance of the Participant's duties with the Employer on a continuous basis within fourteen (14) days after receiving from the Employer a demand for substantial performance that specifically identifies the manner in which the Employer believes that the Participant has not substantially performed the Participant's duties (other than any such failure resulting from a Participant's disability or from termination by a Participant for Good Reason), (ii) the willful engaging by a Participant in conduct which is demonstrably and materially injurious to the Employer, monetarily or otherwise, or (iii) a Participant's conviction of a felony which impairs the Participant's ability substantially to perform the Participant's duties with the Employer. For purposes of this definition, no act, or failure to act, on a Participant's part shall be deemed "willful" unless done, or omitted to be done, by the Participant with reasonable belief that the Participant's action or omission was not in the best interest of the Employer. Failure by a Participant to perform the Participant's duties with the Employer during any period of disability shall not constitute Cause.

9.2 CHANGE IN CONTROL -- shall mean:

(a) a change in control of a nature that would be required to be reported in response to Item 6(e) of Schedule 14A of Regulation 14A promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), whether or not the Employer is then subject to such reporting requirement; or

(b) the public announcement (which, for purposes of this definition, shall include, without limitation, a report filed pursuant to Section 13(d) of the Exchange Act) by the Employer or any "person" (as such term is used in Sections 13(d) and 14(d) of the Exchange Act) that such person has become the "beneficial owner" (as defined in Rule 13d-3 promulgated under the Exchange Act), directly or indirectly, of securities of the Employer (i) representing 25% or more, but not more than 50%, of the combined voting power of the Employer's then outstanding securities unless the transaction resulting in such ownership has been approved in advance by the Continuing Directors (as hereinafter defined) or (ii) representing more than 50% of the combined voting power of the Employer's then outstanding securities (regardless of any approval by the Continuing Directors); provided, however, that notwithstanding the foregoing, no Change in Control shall be deemed to have occurred for purposes of the Plan by reason of the ownership of 25% or more of the total voting capital stock of the Employer then issued and outstanding by the Employer, any subsidiary of the Employer or any employee benefit plan of the Employer or of any subsidiary of the Employer or any entity holding shares of the common stock organized,

appointed or established for, or pursuant to the terms of, any such plan (any such person or entity described in this clause is referred to herein as a "Employer Entity"); or

(c) the announcement of a tender offer by any person or entity (other than an Employer Entity) for 20% or more of the Employer's voting capital stock then issued and outstanding, which tender offer has not been approved by the Board, a majority of the members of which are Continuing Directors, and recommended to the shareholders of the Employer; or

(d) the Continuing Directors cease to constitute a majority of the Employer's Board of Directors; or

(e) the shareholders of the Employer approve (i) any consolidation or merger of the Employer in which the Employer is not the continuing or surviving corporation or pursuant to which shares of Employer stock would be converted into cash, securities or other property, other than a merger of the Employer in which shareholders immediately prior to the merger have the same proportionate ownership of stock of the surviving corporation immediately after the merger; (ii) any sale, lease, exchange or other transfer (in one transaction or a series of related transactions) of all or substantially all

of the assets of the Employer; or (iii) any plan of liquidation or dissolution of the Employer.

9.3 CODE -- shall mean the Internal Revenue Code of 1986, as amended.

9.4 CONTINUING DIRECTOR -- shall mean any person who is a member of the Board of Directors of the Employer, while such person is a member of the Board of Directors, who is not an Acquiring Person (as hereinafter defined) or an Affiliate or Associate (as hereinafter defined) of an Acquiring Person, or a representative of an Acquiring Person or of any such Affiliate or Associate, and who (i) was a member of the Board of Directors as of the Effective Date or (ii) subsequently becomes a member of the Board of Directors, if such person's initial nomination for election or initial election to the Board of Directors is recommended or approved by a majority of the Continuing Directors. For purposes of this definition. "Acquiring Person" shall mean any "person" (as such term is used in Sections 13(d) and 14(d) of the Exchange Act) who or which, together with all Affiliates and Associates of such person, is the "beneficial owner" (as defined in Rule 13d-3 promulgated under the Exchange Act), directly or indirectly, of securities of the Employer representing 20% or more of the combined voting power of the Employer's then outstanding securities, but shall not include the Investors or any Employer Entity; and "Affiliate" and "Associate shall have their respective meanings ascribed to such terms in Rule 12b-2 promulgated under the Exchange Act.

9.5 DATE OF TERMINATION -- shall mean the date specified in the Notice of Termination (except in the case of a Participant's death, in which case Date of Termination shall be the date of death); provided, however, that if the Participant's employment is terminated by the Employer, the date specified in the Notice of Termination shall be at least 30 days from the date the Notice of Termination is given to the Participant and if the Participant's employment is terminated by the Participant for Good Reason, the date specified in the Notice of Termination shall not be more than 60 days from the date the Notice of Termination is given to the Employer.

9.6 EFFECTIVE DATE -- shall mean May 27, 1998.

9.7 EMPLOYER -- shall mean LecTec Corporation, a Minnesota corporation, or any successor thereto pursuant to Section 7.2 hereof or by operation of law.

9.8 GOOD REASON -- shall mean the occurrence, without a Participant's express written consent, within 12 months following a Change in Control of any one or more of the following:

(a) a significant reduction by the Employer in the Participant's base salary as in effect immediately prior to the Change in Control or as the same shall be increased from time to time;

(b) the Employer's requiring the Participant to be based at a location in excess of thirty (30) miles from the location of the Participant's office immediately prior to the Change in Control:

(c) the failure by the Employer to (i) continue in effect any material compensation or benefit plan, program, policy or practice in which the Participant was participating at the time of the Change in Control or (ii) provide the Participant with compensation and benefits at least equal (in terms of benefit levels and/or reward opportunities) to those provided for under each employee benefit plan, program, policy and practice as in effect immediately prior to the Change in Control (or as in effect following the Change in Control, if greater);

(d) the failure of the Employer to obtain a satisfactory agreement from any successor to the Employer to assume and agree to perform under the Plan, as contemplated in Section 7.2 hereof;

(e) any purported termination by the Employer of the Participant's employment that is not effected pursuant to a Notice of Termination (as hereinafter defined); and

(f) the assignment by the Employer to the Participant of any duties inconsistent in any respect with Participant's position (including status, offices, titles, and reporting requirements), authorities, duties, or other responsibilities as in effect immediately prior to the Change in Control or any other action of the Employer which results in a diminishment in such position, authority, duties, or responsibilities, other than an insubstantial and inadvertent action which is remedied by the Employer promptly after receipt of notice thereof given by the Participant.

9.9 NOTICE OF TERMINATION -- shall mean a written notice which shall set forth the Date of Termination and shall set forth in reasonable detail the facts and circumstances claimed to provide a basis for termination of the Participant's employment.

9.10 PARTICIPANT -- shall mean the employees of the Employer identified on Schedule A attached to this Plan document, as the same may be added to by the Employer from time to time. Each Participant shall be assigned to Class I or Class II as stated on Schedule A.

9.11 PLAN -- shall mean the termination pay plan of the Employer established for the benefit of the Participants in the event of a Change in Control. The Plan shall be referred to as the "LecTec Corporation Change in Control Termination Pay Plan."

9.12 PLAN YEAR -- the twelve consecutive month period ending on any December 31.

9.13 TERMINATION OF EMPLOYEMENT -- shall mean termination of a Participant's employment (a) by the Employer for any reason other than Cause or (b) by a Participant for Good Reason; but shall not include termination by reason of a Participant's death.

SCHEDULE A
TO LECTEC CORPORATION

CHANGE IN CONTROL
TERMINATION PAY PLAN

Participants	*Class*
Rodney A. Young	*I*
Deborah Moore	*II*
Jane Nichols	*II*
Daniel McWhorter	*II*
Vice President of Operations (future hire)	*II*
Vice President of Sales (future hire)	*II*

Verified as of the 27th day of May, 1998.

/s/Rodney A. Young
Chairperson of the Board of Directors of LecTec Corporation

EXHIBIT 10.17

TERMINATION AGREEMENT

THIS TERMINATION AGREEMENT is made as of the 30TH day of July, 1998, by and between CNS, Inc., a Delaware corporation ("CNS") and LecTec Corporation, a Minnesota corporation ("Manufacturer").

BACKGROUND

CNS, Manufacturer and Pharmadyne Corporation, (Pharmadyne) a Minnesota Corporation, are parties to that certain Marketing and Distribution Agreement dated January 11, 1996 (the "Distribution Agreement") whereby Manufacturer manufactures and CNS markets and distributes a product (the "Product"), as defined in the Distribution Agreement. In October 1997, Pharmadyne became a wholly-owned subsidiary of Manufacturer and in December 1997 Pharmadyne was merged into Manufacturer and ceased to exist as a separate corporation. The parties wish to terminate the Distribution Agreement and their respective rights and obligations thereunder.

NOW, THEREFORE, in consideration of the mutual promises contained in this Termination Agreement, the parties agree as follows:

1. *The Distribution Agreement is hereby terminated and of no further force and effect; provided, however, that Sections 12 (Manufacturer's Warranties and Representations; Indemnification), 13 (Distributor's Representations, Indemnification), and 19 (Confidential Information) shall survive termination as contemplated in the Distribution Agreement.*

2. *Manufacturer agrees to repurchase all inventory of the Product in the possession of CNS as of the date of this Termination Agreement, provided that all such Product has at least 50% (one year) of its original shelf life and is new, unused and not materially damaged, and in full, unopened cases (such inventory of Product and Product returns are collectively referred to hereafter as the "Repurchased Product"). The repurchase shall be completed no later than September 30, 1998. The purchase price for the Repurchased Product shall be the original invoice purchase price paid by CNS for the Product. (Refer to Exhibit A)*

3. *Manufacturer is hereby authorized to sell the Repurchased Product with the CNS mark and/or packaging; provided, however, that unless otherwise agreed to in writing, Manufacturer shall not be authorized to include the CNS mark on any product sold after April 30, 1999.*

4. *CNS shall bear responsibility for any Product that was initially purchased from CNS or through its broker network, and that is returned by such brokers or retailers. Manufacturer shall bear responsibility for any Product returned by brokers or retailers that was shipped directly from and invoiced by Manufacturer. CNS and Manufacturer agree that responsibility for specific product returns shall be established based on product lot number identification. To the extent that any of such returned Product is damaged or defective and such retailer or broker is then purchasing the Product from Manufacturer, Manufacturer shall replace such damaged or defective Product.*

   Manufacturer is not assuming, and CNS shall bear all responsibility for, any contractual obligations it entered into prior to the date of this Agreement, including without limitation, commissions to CNS' brokers and all other obligations under CNS' agreements with its brokers. Manufacturer shall be entitled to negotiate such broker agreements for the Product, as it deems appropriate.

   CNS shall bear responsibility for any financial commitments that it or its brokers made prior to the date of this Agreement (e.g. advertising, co-op, slotting fees and the like). CNS has represented to Manufacturer that there

are no such outstanding financial commitments as of the date of this Agreement.

5. *The parties shall cooperate with each other in announcing to the public and to retailers of the Product the direct role Manufacturer will take in marketing and distributing the Product as a consequence of the termination of the Distribution Agreement, it being the objective of the parties to make the transition of the marketing and distribution of the Product from CNS to Manufacturer as smooth as reasonably possible. CNS and Manufacturer shall also cooperate in jointly releasing to the public information positively reflecting the nature of this transition.*

6. *The "TheraPatch" Internet web site domain developed by CNS and Manufacturer shall be transferred to and become the sole property of Manufacturer as of the date of this Termination Agreement.*

7. *As additional consideration for the foregoing, the parties hereby release any and all claims of any nature that they may have against each other and their respective principals, officers, directors, and agents arising out of the Distribution Agreement. Nothing in this paragraph 7 shall preclude a claim based on breach of this Termination Agreement.*

8. *This Termination Agreement shall be governed by and construed in accordance with the laws of the State of Minnesota; it constitutes the entire agreement between the parties on the subject matter hereof and supersedes all prior negotiations and discussions, written or oral, between the parties; and no provision shall be modified, amended, waived or supplemented by any means other than a written instrument which refers to this Termination Agreement and is signed by the parties hereto. The parties further agree that, from time to time they will execute and deliver to one another such further instruments and take such other action as may be reasonably requested to effect the intentions of the parties as indicated in this Termination Agreement.*

IN WITNESS WHEREOF, the parties have entered this Termination Agreement effective as of the date first written above.

CNS, INC.

By */s/ David J. Byrd*

Its *Chief Financial Officer*

Title

LECTEC CORPORATION

By */s/ Rodney A. Young*

Rodney A. Young

Its *Chairman, CEO & President*

Title

EXHIBIT A

SCHEDULE OF REPURCHASED PRODUCT AND CALCULATION OF AMOUNT TO BE PAID TO CNS BY MANUFACTURER:

Quantity of cases on hand in CNS warehouse of TheraPatch as of July 30th, 1998	*(Confidential treatment has been requested)*
Original invoice price per case paid by CNS as per Section 2 of this termination agreement	*(Confidential treatment has been requested)*
Total	*(Confidential treatment has been requested)*

EXHIBIT 21.01

Subsidiaries of the Company

LecTec International Corporation

Incorporated in the state of Minnesota

Registered office:	*10701 Red Circle Drive* *Minnetonka, MN 55343*
Corporate office:	*55-11 Curacao Gade* *P. O. Box 309420* *Charlotte Amalie* *St. Thomas, Virgin Islands 00803-9420*
Records office:	*C/O Chase Trade, Inc.* *55-11 Curacao Gade* *P. O. Box 309420* *Charlotte Amalie* *St. Thomas, Virgin Islands 00803-9420*

EXHIBIT 23.01

CONSENT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

We have issued our report dated August 12, 1998 accompanying the consolidated financial statements included in the Annual Report of LecTec Corporation on Form 10-K for the year ended June 30, 1998. We hereby consent to the incorporation by reference of said report in the Registration Statements of LecTec Corporation on Form S-3 (File No. 333-40183, effective November 17, 1997) and Forms S-8 (File No. 33-121780, effective April 21, 1987, File No. 33-45931, effective February 21, 1992, File No. 333-46283, effective February 13, 1998 and File No. 333-46289, effective February 13, 1998).

/s/Grant Thornton LLP

Minneapolis, Minnesota
September 23, 1998

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