

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2001.

☐ 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: (952) 933-2291

Indicate by check mark whether the registrant (1) has filed all reports required
to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during
the preceding 12 months (or for such shorter period that the registrant was
required to file such reports), and (2) has been subject to such filing
requirements for the past 90 days.

Yes ☒ No ☐

The number of shares outstanding of the registrant's common stock as of May 14,
2001 was 3,915,676 shares.

LECTEC CORPORATION

FORM 10-Q FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2001

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PART I - FINANCIAL INFORMATION

ITEM 1 - CONDENSED FINANCIAL STATEMENTS AND NOTES TO CONDENSED
FINANCIAL STATEMENTS

LECTEC CORPORATION

CONDENSED BALANCE SHEETS

<TABLE>

<CAPTION>

	March 31 2001	June 30, 2000
	(Unaudited)	
<S>	<C>	<C>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 48,384	\$ 100,171
Trade receivables and other, net of allowances of \$590,239 and \$369,531 at March 31, 2001 and June 30, 2000	2,385,244	2,645,710
Inventories		
Raw materials	1,572,035	1,649,544
Work-in-process	33,824	23,201
Finished goods	625,144	574,941
	2,231,003	2,247,686
Prepaid expenses and other	366,209	242,543
Total current assets	5,030,840	5,236,110
PROPERTY, PLANT AND EQUIPMENT - AT COST, NET	2,382,119	3,039,088
OTHER ASSETS		
Patents and trademarks, less accumulated amortization of \$1,344,875 and \$1,293,871 at March 31, 2001 and June 30, 2000	269,219	199,351
	\$ 7,682,178	\$ 8,474,549

</TABLE>

See accompanying notes to the condensed financial statements.

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LECTEC CORPORATION
CONDENSED BALANCE SHEETS - CONTINUED

<TABLE>

<CAPTION>

	March 31, 2001	June 30, 2000
	(Unaudited)	
<S>	<C>	<C>
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Note payable to bank	\$ 435,667	\$ 837,542
Current maturities of long-term obligations	22,471	22,562
Accounts payable	2,372,113	1,910,551
Accrued expenses	1,044,315	792,894
Customer deposits	75,000	160,000
Total current liabilities	3,949,566	3,723,549
LONG-TERM OBLIGATIONS, LESS CURRENT MATURITIES	834,639	31,184
COMMITMENTS AND CONTINGENCIES	--	--
SHAREHOLDERS' EQUITY		
Common stock, \$.01 par value: 15,000,000 shares authorized; 3,915,676 shares and 3,904,465 shares issued and outstanding at March 31, 2001 and June 30, 2000	39,157	39,045
Additional paid-in capital	11,332,829	11,316,260
Accumulated other comprehensive income	--	4,845
Accumulated deficit	(8,474,013)	(6,640,334)
	2,897,973	4,719,816
	\$ 7,682,178	\$ 8,474,549

</TABLE>

See accompanying notes to the condensed financial statements.

LECTEC CORPORATION
CONDENSED STATEMENTS OF OPERATIONS
(Unaudited)

<TABLE>
<CAPTION>

	Three months ended March 31,		Nine months ended March 31,	
	2001	2000	2001	2000
<S>	<C>	<C>	<C>	<C>
Net sales	\$ 4,171,778	\$ 3,934,825	\$ 12,417,156	\$ 10,243,282
Cost of goods sold	2,735,137	2,423,164	7,987,711	6,729,326
Gross profit	1,436,641	1,511,661	4,429,445	3,513,956
Operating expenses				
Sales and marketing	1,109,867	1,240,070	3,404,438	2,838,770
General and administrative	708,984	643,948	2,168,891	1,891,821
Research and development	219,236	264,896	660,759	844,860
	2,038,087	2,148,914	6,234,088	5,575,451
Loss from operations	(601,446)	(637,253)	(1,804,643)	(2,061,495)
Other income (expenses)				
Interest expense	(44,932)	(6,732)	(117,850)	(8,808)
Gain on sale of assets	103,624	--	103,624	--
Other, net	(1,027)	657	(14,810)	28,526
Loss before income taxes	(543,781)	(643,328)	(1,833,679)	(2,041,777)
Income taxes	--	--	--	--
Net loss	\$ (543,781)	\$ (643,328)	\$ (1,833,679)	\$ (2,041,777)
Net loss per share - basic and diluted	\$ (0.14)	\$ (0.17)	\$ (0.47)	\$ (0.53)
Weighted average shares outstanding - basic and diluted	3,915,676	3,890,494	3,909,457	3,882,746

</TABLE>

See accompanying notes to the condensed financial statements.

LECTEC CORPORATION
CONDENSED STATEMENTS OF CASH FLOWS
(UNAUDITED)

<TABLE>
<CAPTION>

	Nine Months Ended March 31,	
	2001	2000
<S>	<C>	<C>
Cash flows from operating activities:		
Net loss	\$ (1,833,679)	\$ (2,041,777)
Adjustments to reconcile net loss to net cash used in operating activities:		
Gain on sale of assets	(103,624)	0
Depreciation and amortization	493,004	707,237
Changes in operating assets and liabilities:		
Trade and other receivables	260,466	(189,367)
Inventories	16,683	(351,013)
Prepaid expenses and other	(145,695)	(58,970)
Accounts payable	461,562	547,028
Accrued expenses and other	257,529	359,268
Customer deposits	(85,000)	--

Net cash used in operating activities	(678,754)	(1,027,594)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property, plant and equipment	(311,407)	(326,215)
Investment in patents and trademarks	(120,872)	(71,539)
Net proceeds from sale of tape equipment	630,000	--
Other	11,076	--
	-----	-----
Net cash provided by (used in) investing activities	208,797	(397,754)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Issuance of common stock	16,681	26,815
Net borrowings (repayments) of line of credit	(401,875)	412,418
Proceeds from long-term borrowing	820,000	--
Repayment of long-term obligations	(16,636)	--
	-----	-----
Net cash provided in financing activities	418,170	439,233
	-----	-----
Net decrease in cash and cash equivalents	(51,787)	(986,115)
Cash and cash equivalents at beginning of period	100,171	1,022,025
	-----	-----
Cash and cash equivalents at end of period	\$ 48,384	\$ 35,910
	=====	=====
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest expense	\$ 116,530	\$ 5,233
Income taxes	2,000	--

</TABLE>

See accompanying notes to the condensed financial statements.

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LECTEC CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED FINANCIAL STATEMENTS
(UNAUDITED)

(1) GENERAL

The accompanying condensed financial statements include the accounts of LecTec Corporation (the "Company") as of and for the three and nine month periods ended March 31, 2001 and 2000. The Company's condensed financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and should be read in conjunction with its Annual Report on Form 10-K and its Annual Report to Shareholders for the fiscal year ended June 30, 2000. The interim condensed financial statements are unaudited and in the opinion of management, reflect all adjustments necessary for a fair presentation of results for the periods presented. Results for interim periods are not necessarily indicative of results for the year.

(2) NET LOSS PER SHARE

The Company's basic net loss per share amounts have been computed by dividing net loss by the weighted average number of outstanding common shares. The Company's diluted net loss per share amounts have been computed by dividing net loss by the weighted average number of outstanding common shares and common share equivalents, when dilutive. Options and warrants to purchase 1,037,570 and 976,705 shares of common stock with a weighted average exercise price of \$5.26 and \$5.83 were outstanding during the three months ended March 31, 2001 and 2000, but were excluded because they were antidilutive. Options and warrants to purchase 1,012,246 and 1,054,530 shares of common stock with a weighted average exercise price of \$5.57 and \$6.19 were outstanding during the nine months ended March 31, 2001 and 2000, but were excluded because they were antidilutive.

(3) COMPREHENSIVE INCOME (LOSS)

For the quarter and nine months ended March 31, 2001 there were no items which the Company is required to recognize as components of comprehensive income (loss), therefore comprehensive income (loss) was the same as net loss.

(4) SEGMENTS

The Company operates its business in one reportable segment - the manufacture and sale of products based on advanced skin interface technologies. Each of the Company's major product lines has similar economic characteristics, technology, manufacturing processes, and regulatory environments. Customers and distribution and marketing strategies vary within major product lines as well as overlap between major product lines. The Company's executive decision makers evaluate sales performance based on the total sales of each major product line

and profitability on a total company basis, due to shared infrastructures, to make operating and strategic decisions. Net sales by major product line were as follows:

<TABLE>
<CAPTION>

	Three months ended March 31,		Nine months ended March 31,	
	2001	2000	2001	2000
<S>	<C>	<C>	<C>	<C>
Therapeutic consumer products	\$ 2,260,761	\$ 1,420,812	\$ 7,246,976	\$ 3,203,546
Conductive products	1,939,017	1,988,864	5,042,744	5,493,225
Medical tape products	(28,000)	525,149	127,436	1,546,511
	\$ 4,171,778	\$ 3,934,825	\$12,417,156	\$10,243,282

</TABLE>

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(5) NOTE PAYABLE TO BANK

In November 1999, the Company entered into a secured line of credit with a maximum borrowing of \$2,000,000. In September 2000, the line of credit was increased to allow borrowing of up to \$2,800,000. The credit agreement expires in November 2001 and includes interest computed at the prime rate plus three percentage points (effective rate of 11% at March 31, 2001). The line of credit is secured by the Company's receivables, inventory and equipment. The credit agreement contains certain restrictive covenants which require the Company to maintain, among other things, specified levels of net worth and not to exceed specified cumulative losses. The Company was in compliance with all covenants as of March 31, 2001.

(6) LONG-TERM OBLIGATION

In December 2000, the Company entered into a mortgage agreement with gross proceeds of \$820,000. The principal balance of the mortgage is due in December 2002. Monthly payments of interest are computed at the prime rate plus five percentage points (effective rate of 13% at March 31, 2001). The mortgage is secured by the Company's real property.

(7) DISPOSITION OF ASSETS

In March 2001, the Company sold its medical tape manufacturing equipment and other related assets. Net proceeds from the sale were \$630,000 consisting of the purchase price of \$700,000 less transaction costs of \$70,000. The Company realized a gain on the sale of \$103,624. The sale of the medical tape equipment finalized the Company's plan to exit the medical tape business which was adopted at the end of fiscal year 2000. Adoption of this plan originally resulted in a charge of \$645,000 during fiscal year 2000 related to the write-down of the medical tape equipment to its estimated fair market value at June 30, 2000.

(8) AGREEMENT TO SELL ASSETS

In November 2000, the Company entered into an agreement to sell the Company's diagnostic electrode and electrically conductive adhesive hydrogel business assets which are used to produce the Company's conductive products. Under the agreement, the Company received \$7,250,000 in cash upon closing of the transaction, subject to adjustment for changes in the net assets at the time of closing. The agreement was approved by the shareholders of the Company at its Annual Meeting of Shareholders on April 17, 2001. The closing occurred on April 30, 2001. The Company will recognize a gain of approximately \$4,400,000 in the fourth quarter of fiscal year 2001 related to this transaction.

(9) INCOME TAXES

The provision for income taxes for the three months and nine months ended March 31, 2001, has been offset principally by a valuation allowance for deferred taxes.

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PART I - FINANCIAL INFORMATION

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

QUARTERS AND NINE MONTHS ENDED MARCH 31, 2001 AND 2000

RESULTS OF OPERATIONS

Net sales for the third quarter of fiscal 2001 were \$4,171,778 compared

to net sales of \$3,934,825 for the third quarter of fiscal 2000, an increase of 6.0%. The increase was primarily the result of increased therapeutic consumer product sales which more than offset decreased medical tape sales. Therapeutic consumer product sales increased by 59.1% from \$1,420,812 to \$2,260,761 while conductive product sales decreased by 2.5% from \$1,988,864 to \$1,939,017 and medical tape product sales decreased by 105.3% from \$525,149 to (\$28,000). The therapeutic consumer product sales increase was primarily the result of sales of the new Triaminic(R) vapor product to Novartis Consumer Health, Inc. The Company expects conductive product sales to decrease in the remainder of fiscal 2001 due to the sale of assets used to produce the conductive products. As part of this asset sale, the Company entered into a Manufacturing and Supply Agreement with the buyer. Under the terms of this Agreement the Company will continue to produce conductive products for the buyer for a period of up to nine months. For the first six months of the Agreement the Company will sell the conductive products to the buyer at cost. During the last three months of the Agreement the Company will sell the products to the buyer at cost plus ten percent. Under the Agreement, sales of conductive products, at decreased levels, will potentially continue through January 2002. The decrease in medical tape product sales was due to the exit of the medical tape business.

Net sales for the first nine months of fiscal 2001 were \$12,417,156 compared to net sales of \$10,243,282 for the first nine months of fiscal 2000, an increase of 21.2%. The increase was primarily the result of increased therapeutic consumer product sales which more than offset decreased conductive and medical tape sales. Therapeutic consumer product sales increased by 126.2% from \$3,203,546 to \$7,246,976 while conductive product sales decreased by 8.2% from \$5,493,225 to \$5,042,744 and medical tape product sales decreased by 91.8% from \$1,546,511 to \$127,436. The therapeutic consumer product sales increase was primarily the result of sales of the new vapor product to Novartis Consumer Health, Inc as well as sales of the new acne product to Johnson & Johnson Consumer Products Worldwide. The decrease in conductive product sales was primarily the result of softening customer demand associated with the announced sale of the conductive business. The decrease in medical tape product sales was due to the exit of the medical tape business.

Gross profit for the third quarter of fiscal 2001 was \$1,436,641, compared to \$1,511,611 for the third quarter of fiscal 2000, a decrease of 5.0%. Gross profit as a percent of net sales for the third quarter of fiscal 2001 was 34.4% compared to 38.4% for the third quarter of fiscal 2000. The decrease in gross profit for the quarter resulted primarily from increased sales to a consumer contract therapeutic customer, higher labor costs associated with overtime, and higher purchased raw material costs. This decrease was partially offset by an increase in gross profit related to increased sales volume and the favorable impact of a change in the sales mix toward LecTec branded therapeutic consumer products.

Gross profit for the first nine months of fiscal 2001 was \$4,429,445 compared to \$3,513,956 for the first nine months of fiscal 2000, an increase of 26.1%. Gross profit as a percent of net sales for the first nine months of fiscal 2001 was 35.7% compared to 34.3% for the first nine months of fiscal 2000. The increase in gross profit for the nine months resulted primarily from an increase in gross profit related to increased sales volume and the favorable impact of a change in the sales mix toward higher-margin therapeutic consumer products. These items more than offset a decrease in gross profit related to the costs associated with resolving a packaging issue that occurred in the current nine months, as well as, a decrease in gross profit related to labor costs associated with higher production volumes and increased overtime related to production of therapeutic patch products. The packaging issue resulted when one of the Company's vendors supplied packaging material that did not meet required specifications. The

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Company is currently obtaining packaging material that does meet required specifications from the same vendor.

Sales and marketing expenses were \$1,109,867 and \$1,240,070 during the third quarters of fiscal 2001 and 2000, and as a percentage of net sales, were 26.6% and 31.5% respectively. The decrease in sales and marketing expenses for the quarter was primarily due to a decrease of \$196,000 in media advertising expenses related to the absence of a TV ad campaign for TheraPatch vapor products that was run in the second quarter of fiscal 2001 rather than in the third quarter as in fiscal 2000, and a decrease of \$145,000 in retail slotting fees which more than offset an increase of \$132,000 in cooperative advertising.

Sales and marketing expenses were \$3,404,438 and \$2,838,770 during the first nine months of fiscal 2001 and 2000, and as a percentage of net sales, were 27.4% and 27.7% respectively. The increase in sales and marketing expenses for the first nine months was primarily due to an increase of \$484,000 in media advertising expenses related to ad campaigns.

General and administrative expenses were \$708,984 and \$643,948 during the third quarters of fiscal 2001 and 2000, and as a percentage of net sales, were 17.0% and 16.4% respectively. The increase in general and administrative expenses for the quarter was primarily due to an increase in travel and lodging expense of \$39,000.

General and administrative expenses were \$2,168,891 and \$1,891,821,

during the first nine months of fiscal 2001 and 2000, and as a percentage of net sales, were 17.5% and 18.5% respectively. The increase in general and administrative expenses for the nine months was primarily due to increased consulting expense of \$83,000, increased accrued corporate bonus expense of \$97,000, and increased employment fees of \$69,000.

Research and development expenses for the third quarters of fiscal 2001 and 2000 were \$219,236 and \$264,896, and as a percentage of net sales, were 5.3% and 6.7% respectively. The decrease in research and development expenses for the quarter was primarily due to a decrease in test run expense of \$24,000

Research and development expenses were \$660,759 and \$844,860 during the first nine months of fiscal 2001 and 2000, and as a percentage of net sales, were 5.3% and 8.2% respectively. The decrease in research and development expenses for the nine months was primarily due to a decrease in test run expense of \$64,000, and a decrease in contract labor expense of \$53,000.

Interest expense increased in the third quarter of fiscal 2001 to \$44,932 from \$6,732 in the third quarter of fiscal 2000. Interest expense increased in the first nine months of fiscal 2001 to \$117,850 from \$8,808 in the first nine months of fiscal 2000. Both of the fiscal 2001 increases resulted primarily from interest expense associated with increased borrowings under the line of credit and interest expense associated with the mortgage. During the third quarter of fiscal 2001 the Company recorded a gain on sale of assets of \$103,624 related to the sale of the medical tape manufacturing equipment.

The Company recorded a loss before income taxes of \$543,781 in the third quarter of fiscal 2001 compared to a loss before income taxes of \$643,328 for the third quarter of fiscal 2000. The Company recorded a loss before income taxes of \$1,833,679 in the first nine months of fiscal 2001 compared to a loss before income taxes of \$2,041,777 for the first nine months of fiscal 2000. The decrease in loss for the current year third quarter was primarily the result of the gain on the sale of the medical tape manufacturing equipment. The decrease in loss for the first nine months was primarily the result of increased gross profit that resulted from increased sales volume, the gain on the sale of the medical tape manufacturing equipment, and the exit from the medical tape business. The increased gross profit more than offset an increase in operating expenses related to advertising expenses associated with retail sales of the Company's TheraPatch products.

The provision for income taxes in the third quarter and first nine months of fiscal 2001 and 2000 has been offset principally by a valuation allowance for deferred taxes.

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

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents decreased by \$51,787 to \$48,384 during the first nine months of fiscal 2001. Accounts receivable decreased by \$260,466 to \$2,385,244 during the first nine months of fiscal 2001. The higher accounts receivable balance at June 30, 2000 was primarily due to significant initial sales, with extended terms, to a TheraPatch customer in the fourth quarter of fiscal 2000. Inventories decreased by \$16,683 to \$2,231,003. Accounts payable of \$2,372,113 at March 31, 2001 increased by \$461,562 during the first nine months primarily due to increased payables related to increased manufacturing production and increased advertising expenses related to the TheraPatch product line. Capital spending for manufacturing equipment and plant improvements totaled \$311,356 during the first nine months of fiscal 2001. The Company entered into a purchase commitment for production machinery in the amount of \$154,482 during the first nine months of fiscal 2001. This purchase commitment will be fulfilled sometime in the first quarter of fiscal year 2002.

The Company had working capital of \$1,081,274 and a current ratio of 1.3 at March 31, 2001 compared to working capital of \$1,512,561 and a current ratio of 1.4 at June 30, 2000.

The Company finalized a \$2,000,000 asset-based line of credit in November, 1999. In September 2000, the line of credit was increased to allow borrowing of up to \$2,800,000. Borrowings outstanding on the line of credit were \$435,667 as of March 31, 2001. The Company was in compliance with all covenants as of March 31, 2001.

In December 2000, the Company entered into a mortgage agreement with gross proceeds of \$820,000.

Management believes that existing cash and cash equivalents, internally-generated cash flow, the existing secured line of credit including the line of credit increase, the mortgage loan, and the sale of the Company's diagnostic electrode and electrically conductive adhesive hydrogel business assets will be sufficient to support anticipated operating and capital spending requirements through fiscal year 2002 and contribute to the funding of longer-term growth and expansion of the business. Maintaining adequate levels of working capital depends in part upon the success of the Company's products in the marketplace, the relative profitability of those products and the Company's

ability to control operating expenses. Funding of the Company's operations in future periods may require additional investments in the Company in the form of equity or debt. There can be no assurance that the Company will achieve desired levels of sales or profitability, or that future capital infusions will be available.

FORWARD-LOOKING STATEMENTS

From time to time, in reports filed with the Securities and Exchange Commission (including this Form 10-Q), 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 TheraPatch brand strategy; impact of interruptions to production; dependence on key personnel; need for regulatory approvals; changes in governmental regulatory requirements or accounting pronouncements; ability to satisfy funding requirements for operating needs, expansion or capital expenditures; and the matters discussed on our "Cautionary Statements" filed as Exhibit 99.1 to form 10-Q for the quarter ended December 31, 2000.

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PART I - FINANCIAL INFORMATION

ITEM 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company has no history of, and does not anticipate in the future, investing in derivative financial instruments, derivative commodity instruments or other such financial instruments. Transactions with international customers are entered into in U.S. dollars with the exception of TheraPatch sales to Canadian customers, precluding the need for foreign currency hedges. These Canadian sales have not been material.

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PART II

OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

None.

Item 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

Not applicable.

Item 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

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

The Regular Annual Meeting of Shareholders of the Company was held on April 17, 2001. The following matters were voted on by Shareholders:

1. Approval of the sale of certain assets used in the Company's conductive products division pursuant to the Asset Purchase Agreement dated November 17, 2000, among the Company, The Ludlow Company LP and Sherwood Services AG.
2. The election of six directors to serve on the Board of Directors for a term of one year and until their successors are duly elected and qualified.
3. The ratification of the appointment of Grant Thornton LLP as the Company's independent auditor for the Company's current fiscal year.

The results of the voting on these matters were as follows:

1. Approval of the sale of certain assets used in the Company's conductive products division pursuant to the Asset Purchase Agreement dated November 17, 2000, among the Company, The Ludlow Company LP and Sherwood Services AG:

For	Against	Abstain	Non-Vote	Total
-----	-----	-----	-----	-----
2,353,375	33,173	9,564	1,191,852	3,587,964

2. Board of Directors:

	For	Withhold Authority	Total
---	---	-----	-----
Lee M. Berlin	3,537,564	50,400	3,587,964
Alan C. Hymes, M.D.	3,537,564	50,400	3,587,964
Bert J. McKasy	3,537,564	50,400	3,587,964
Marilyn K. Speedie, Ph.D.	3,537,564	50,400	3,587,964
Donald C. Wegmiller	3,537,564	50,400	3,587,964
Rodney A. Young	3,533,611	54,353	3,587,964

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3. Appointment of Grant Thornton LLP as independent auditor for the Company:

For	Against	Abstain	Non-Vote	Total
-----	-----	-----	-----	-----
3,525,689	20,340	41,935	-	3,587,964

Item 5. OTHER INFORMATION

None.

Item 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) EXHIBITS

Item No.	Item	Method of Filing
-----	-----	-----
10.1	Asset Purchase Agreement dated March 13, 2001 by and among The National Medical Products Co. Ltd. and LecTec Corporation.	Filed herewith

(b) REPORTS ON FORM 8-K

On March 21, 2001 the Company filed a report on Form 8-K in connection with the signing of an Asset Purchase Agreement dated March 13, 2001 by and among The National Medical Products Co. Ltd. and LecTec Corporation.

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SIGNATURES

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

LECTEC CORPORATION

Date May 15, 2001 /s/ Rodney A. Young

Rodney A. Young, Chief Executive
Officer & President

Date May 15, 2001 /s/ Douglas J. Nesbit

Douglas J. Nesbit, Chief Financial
Officer & Secretary
(Principal Financial Officer)

EXHIBIT INDEX

Exhibits

- - - - -

- 10.1 *Asset Purchase Agreement dated March 13, 2001 by and among The
National Medical Products Co. Ltd., and LecTec Corporation.*

ASSET PURCHASE AGREEMENT

THIS AGREEMENT made as of March 13, 2001 (this "Agreement") by and among The National Medical Products Co. Ltd., a Saudi Arabian corporation (the "Purchaser"), and LecTec Corporation, a Minnesota corporation (the "Seller"). The Purchaser and Seller are referred to collectively herein as the "Parties." Capitalized terms used in this Agreement shall have the meanings given to them upon their first use or in Section 10 herein.

W I T N E S S E T H

WHEREAS, the Seller has been engaged in the business (the "Business") of the research, development, design, manufacture, marketing, distribution and sale of medical tape products of various types and configurations for the world market, including the United States healthcare market (hospitals and alternate care), the United States consumer market and the international wound dressing healthcare market; and

WHEREAS, the Seller desires to sell and assign and the Purchaser desires to buy, on the terms and conditions set forth in this Agreement, the assets and properties of the Seller associated with the Business as set forth herein;

NOW, THEREFORE, in consideration of the premises and of the mutual promises herein made, and in consideration of representations, warranties, and covenants herein contained, the Parties hereto agree as follows:

Section 1. Purchase and Sale of Purchased Assets.

- (a) Subject to and upon the terms and conditions of this Agreement, the Seller agrees to sell, assign, transfer and convey to the Purchaser and the Purchaser agrees to purchase from the Seller, on the date hereof, all of the Seller's right, title and interest, as of the date hereof, in and to the following assets of the Seller (the "Purchased Assets") to the extent employed solely in the Business:
 - (i) The following machinery and equipment, documentation, operation manuals and operator's records of the Seller (collectively, "Equipment"):
 - A. The tape coating equipment.
 - B. Handling machinery related to the tape coating equipment.
 - C. A tape converter manufactured by Deacro Industries Ltd. of Mississauga, Ontario, designated as a model DA 503, serial number 1116.
 - D. The following equipment manufactured by Arsoma GmbH of Cleeburg, Germany and designated as follows:
 - Model EM 260 Slitter Assy, no serial number
 - Model CD 250 Core Dispenser, serial number CD250-31
 - Model RS 250 Rewind Station, serial number RS250-23
 - Model TR 250 Turret Rewinder, serial number TR250-29
 - Model EM 510 Slitter Assy, serial number

EM510-20

- Model CD 450 Core Dispenser, serial number CD450-20
- Model RS 450 Roll Stacker, serial number RS450-20
- Model TR 450 Turret Rewinder, serial number TR450-20

E. All documentation, operation manuals and operator's records relating to the foregoing.

(ii) All of the following described intellectual property (the "Intellectual Property"), including the goodwill associated therewith, licenses and sublicenses granted and obtained with respect thereto, and rights thereunder, remedies against infringements thereof, and rights to protection of interests therein under the laws of all jurisdictions, owned or registered in the name of the Seller, or its affiliates:

A. Patent # US 4,696,854

B. Patent # US 5,810,756

C. The trademark "ISOCLEAR"

D. The trademark "SUPERPORE"

(iii) All former customer lists and customer contacts of the Seller directly related to the Business.

(iv) The Seller's claims and rights against third parties relating to the Purchased Assets, including, without limitation, rights under manufacturers' and vendors' warranties.

(b) Notwithstanding anything in Section 1(a) to the contrary, the assets and properties to be transferred by the Seller to the Purchaser pursuant hereto (and the term "Purchased Assets" as used herein) shall not include any assets and properties which are not referred to in Sections 1(a)(i) through 1(a)(iv) above.

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(c) The parties acknowledge and agree that on the date hereof, title to all of the Purchased Assets described in Section 1(a)(i) through 1(a)(iv) shall be conveyed to the Purchaser.

Section 2. No Assumption of Seller Liabilities.

Notwithstanding any implication to the contrary contained in this Agreement, the Purchaser shall not assume, pay or in any way be liable or responsible for any of the debts, liabilities or obligations of the Seller arising in connection with the operation of the Business prior to the date hereof.

Section 3. Purchase Price.

The Purchaser shall purchase and the Seller shall sell the Purchased Assets for the sum of Seven Hundred Thousand Dollars (USD\$700,000) (the "Purchase Price"). The Purchase Price shall be delivered to Seller by wire transfer or certified check simultaneously with the execution of this Agreement.

Section 4. Closing, Closing Deliveries.

(a) The closing of the transactions contemplated herein (the "Closing") shall take place simultaneously with the signing of this Agreement (the "Closing Date").

- (b) *Simultaneously with the signing of this Agreement, Seller shall deliver the following to Purchaser:*
- (i) *The Purchased Assets;*
 - (ii) *A bill of sale and/or assignment relating to the Purchased Assets in a form reasonably satisfactory to the Purchaser; and*
 - (iii) *Such other documents relating to the transactions contemplated hereby which are reasonably requested by the Purchaser.*
- (c) *Simultaneously with the signing of this Agreement, Purchaser shall deliver the following to Seller:*
- (i) *The Purchase Price;*
 - (ii) *Such other documents relating to the transactions contemplated hereby which are reasonably requested by the Purchaser.*

Section 5. Representations and Warranties of the Seller.

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The Seller hereby represents and warrants to the Purchaser that, except for those matters discussed in Section 8(e) of this Agreement, the statements contained in this Section 5 are correct and complete as of the date of this Agreement.

- (a) *Due Organization. The Seller is a corporation duly organized, validly existing and in good standing under the laws of the State of Minnesota. The Seller has all requisite corporate power and authority to own, lease and operate its properties, to carry on its business as presently conducted by it, to enter into this Agreement and to consummate the transactions contemplated hereby, except where the failure to have such corporate power would not reasonably be likely to have a Material Adverse Effect.*
- (b) *Authorization. The execution and delivery by the Seller of this Agreement and the performance of its obligations hereunder, have been duly and validly authorized by all necessary corporate action on its part, and this Agreement is the legal, valid and binding obligation of the Seller, enforceable against it in accordance with its terms.*
- (c) *Non-Contravention. Except where the occurrence of any of the events in (i) or (ii) below would not reasonably be likely to have a Material Adverse Effect, neither the execution and delivery by the Seller of this Agreement, nor the performance by the Seller of its obligations hereunder will, or with the giving of notice or the lapse of time, or both, would:*
- (i) *conflict with, result in a breach of, or constitute a default under, any provision of the Articles of Incorporation or By-laws of the Seller;*
 - (ii) *conflict with, result in a breach of, or constitute a default under, any provision of any contract, indenture, lease, sublease, loan agreement, restriction, Lien or other obligation or liability to which the Seller is a party or by which it is bound, or result in or create in any party the right to accelerate, terminate, modify or cancel any contract, license, indenture, lease, sublease or loan agreement to which the Seller is a party or by which it, or any of its properties or assets, is affected or bound;*
 - (iii) *violate any order, writ, injunction, decree, law,*

statute, rule or regulation applicable to the Seller;
or

(iv) result in the creation or imposition of any Lien upon any of the Purchased Assets.

(d) *Title to Purchased Assets; Condition of Purchased Assets.* The Seller has good and marketable title to and possession of all of the Purchased Assets, free and clear of all Liens and no interest in or right to any of the Purchased Assets is held, legally or beneficially by any Person other than the Seller. The tangible Purchased Assets have been properly maintained and are in good operating condition, reasonable wear and

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tear excepted, and there exists no outstanding written notice of any violation of any statute relating to them.

(e) *Intellectual Property.* The Seller exclusively owns the entire right, title and interest in and to each item of Intellectual Property. To the Seller's knowledge, the use of the Intellectual Property in the conduct of the Business or the use of the Seller's know-how in the conduct of the Business do not infringe the rights of any third party.

(f) *Consents of Third Parties.* No consent, approval or agreement of any Person, court, government or other entity is required to be obtained by the Seller in connection with the execution and delivery of this Agreement or the consummation of the transactions contemplated hereby, except where the failure to obtain such consent, approval or agreement would not be reasonably likely to result in a Material Adverse Effect.

(g) *Compliance with Law; Permits.* The Seller has complied with all, and has not committed any violation of any, federal, state, local or foreign statutes, laws, rules and regulations applicable to the Purchased Assets. Except where the absence would not reasonably be likely to result in a Material Adverse Effect, the Seller holds all permits, licenses (or permissions in the nature thereof), registrations with, and consents of, governmental authorities necessary to conduct the Business and in the same manner as it has been conducted heretofore.

(h) *No Broker.* No agent, broker, person or firm acting on behalf of the Seller or any of its Affiliates, or under its authority, is or will be entitled to receive from Purchaser a financial advisory fee, brokerage commission, finder's fee or like payment in connection with this Agreement or any of the transactions contemplated hereby.

(i) *Environmental, Health and Safety Matters.* Neither this Agreement nor the consummation of the transaction that is the subject of this Agreement will result in any obligations for site investigation or cleanup, or notification to or consent of government agencies or third parties, pursuant to any of the so-called "transaction-triggered" or "responsible property transfer" laws.

Section 6. Representations and Warranties of the Purchaser.

The Purchaser hereby represents and warrants to the Seller that the statements contained in this Section 6 are correct and complete as of the date of this Agreement.

(a) *Due Organization.* Purchaser is a corporation duly organized, validly existing and in good standing under the laws of Saudi Arabia. The Purchaser has all requisite power and authority to enter into this Agreement and to consummate the transactions contemplated hereby and thereby.

- (b) *Authorization.* The execution and delivery by the Purchaser of this Agreement and the performance by it of its obligations hereunder, have been duly and validly authorized by all necessary action on its part, and this Agreement is the legal, valid and binding obligation of the Purchaser, enforceable against it in accordance with its terms.
- (c) *Non-Contravention.* Neither the execution nor delivery of this Agreement by the Purchaser nor the performance by the Purchaser of its obligations hereunder will, or with the giving of notice or the lapse of time, or both, would:
 - (i) conflict with, result in a breach of, or constitute a default under, any provision of the Purchaser's articles of incorporation or by-laws, or of any contract, indenture, lease, sublease, loan agreement, Lien or other obligation or liability to which the Purchaser is a party or by which it is bound; or
 - (ii) violate any order, writ, injunction, decree, law, statute, rule or regulation applicable to or by which it or its properties are bound.
- (d) *Litigation.* There is no litigation, arbitration, claim, governmental or other investigation or proceeding (formal or informal) involving the transactions contemplated hereby pending or, to the best knowledge of the Purchaser, threatened, against the Purchaser and to the best knowledge of the Purchaser there exists no bases or grounds for any of the foregoing.
- (e) *No Broker.* No agent, broker, person or firm acting on behalf of the Purchaser or under its authority, is or will be entitled to a financial advisory fee, brokerage commission, finder's fee or like payment in connection with this Agreement or any of the transactions contemplated hereby.
- (f) *Consents of Third Parties.* No consent, approval or agreement of any Person, party, court, government or entity is required to be obtained by the Purchaser in connection with the execution and delivery of this Agreement or the consummation of the transactions contemplated hereby.

Section 7. Indemnification.

- (a) The Parties shall be entitled to rely upon the representations and warranties of the other party set forth in Section 5 and Section 6 of this Agreement, and except as otherwise specifically provided herein, such representations and warranties shall survive the Closing and remain in full force and effect for a period of eighteen (18) months after the Closing (other than the representations and warranties set forth in Sections 5(b) and 6(b) (Authorization), which shall survive until sixty (60) days after the expiration of the applicable statutes of limitations, and the representations and warranties set forth in Section 5(e) (Title to Purchased Assets), which shall survive indefinitely).

- (b) The Seller, hereby agrees to indemnify and hold harmless the Purchaser, the Purchaser's Affiliates and their respective officers, directors, employees, stockholders, agents and representatives (collectively, the "Purchaser Indemnified Parties"), from and against any loss, liability, claim, damage or expense (including costs of litigation and reasonable legal fees and expenses) (a "Loss") suffered or incurred by the

Purchaser Indemnified Party based upon, arising out of or resulting from any of the following:

- (i) The failure of the Seller to transfer to the Purchaser good and sufficient title to the Purchased Assets, free and clear of all Liens;
 - (ii) Any breach of any representation or warranty of the Seller contained in this Agreement; and
 - (iii) Any breach of any covenant of the Seller contained in this Agreement requiring performance after the Closing Date.
- (c) The Purchaser hereby agrees to indemnify and hold harmless the Seller, the Seller's Affiliates and their respective officers, directors, employees, stockholders, agents and representatives (collectively, the "Seller Indemnified Parties"), from and against any Loss suffered or incurred by any such Seller Indemnified Party based upon, arising out of or resulting from any of the following:
 - (i) Any breach of any representation or warranty of the Purchaser contained in this Agreement; and
 - (ii) Any breach of any covenant of the Purchaser contained in this Agreement requiring performance after the Closing Date
- (d) The Purchaser Indemnified Parties and the Seller Indemnified Parties (the "Indemnified Parties") shall bring a claim for indemnification hereunder in good faith and in a timely manner consistent with good commercial practices.
- (e) After the Closing Date, the rights set forth in this Section 7 shall be each party's sole and exclusive remedies against the other parties hereto for misrepresentations or breaches of covenants contained in this Agreement. Notwithstanding the foregoing, nothing herein shall prevent any of the parties hereto from bringing an action based upon allegations of fraud or other intentional breach of an obligation of or with respect to the other parties in connection with this Agreement. In the event such action is brought, the Purchaser, on the one hand, and the Seller and on the other hand, shall bear their own fees and expenses in connection with such action.
- (f) Notwithstanding anything in this Agreement to the contrary, the amount of any Losses for which indemnification is provided under this Section 7 shall be reduced by (i) any related recoveries actually received by an Indemnified Party under insurance policies, (ii) any other related payments actually received by an Indemnified Party from third parties and (iii) any Tax benefits actually realized or received by an

Indemnified Party or any of their Affiliates, in each case, on account of the matter resulting in such Losses or the payment of such Losses.

- (g) Anything to the contrary notwithstanding, neither the Purchaser Indemnified Parties, on the one hand, nor the Seller Indemnified Parties, on the other hand, shall be entitled to recovery from the Indemnifying Party with respect to any inaccuracy or breach of any representation or warranty in Sections 5 or 6 hereof, as applicable, (i) unless and until the aggregate amount of such Losses suffered, sustained or incurred by the Purchaser Indemnified Parties or the Seller Indemnified Parties, as the case may be, by reason of such inaccuracy or breach, shall exceed USD\$200,000 calculated on a

cumulative and not on a per item basis (the "Basket Amount"), and then only with respect to the excess over the Basket Amount, or (ii) in an aggregate amount in excess of USD\$700,000 (the "Cap").

Section 8. Additional Covenants and Agreements.

(a) Tax Matters.

(i) The Seller shall be solely responsible for and shall indemnify and hold harmless the Purchaser for all Taxes with respect to Purchased Assets which are due and payable up to and including the Closing Date, and the Purchaser shall be responsible for and indemnify and hold harmless the Seller for all Taxes with respect to the Purchased Assets which are due and payable after the Closing Date, except that any Taxes imposed upon the ownership of Purchased Assets which relate to a period commencing prior to the Closing Date and ending after the Closing Date, shall be prorated such that Taxes for the period prior to the Closing Date shall be the responsibility of the Seller and Taxes for the period after the Closing Date shall be the responsibility of the Purchaser.

(ii) The Purchaser and the Seller recognize their mutual obligations pursuant to Section 1060 of the Code to timely file IRS Form 8594 with each of their respective federal income tax returns. The Purchaser and the Seller agree to allocate the Purchase Price among the Purchased Assets in accordance with the provisions of Section 1060 of the Code and the Treasury Regulations thereunder.

Unless otherwise required by a determination within the meaning of Section 1313 of the Code (or a counterpart provision of foreign, state or local law), all foreign, federal, state and local income tax returns filed by the Purchasers and the Seller shall be filed consistently with the allocations reflected in this Section 8(a)(ii).

(b) **Transfer of Purchased Assets.** The Parties agree that simultaneously with the execution of this Agreement title to the Purchase Assets and Risk of Loss with

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respect to the Purchased Assets shall pass to Purchaser. Purchaser shall physically remove the Purchased Assets from Seller's premises within sixty days of the date hereof. Purchaser acknowledges that any and all expenses associated with the removal of the Purchased Assets from the Seller's Premises shall be borne by Purchaser. Purchaser hereby (i) indemnifies Seller for any Loss incurred by Seller in connection with the Purchased Assets during the time that the Purchased Assets remain on the premises of Seller (ii) releases Seller from any Loss incurred by Seller with respect to the Purchased Assets during the time that the Purchased Assets remain on the premises of Seller.

(c) **Transition Services.** For a period of two weeks from the date hereof, Seller shall provide training at Seller's facilities with respect to the manufacturing processes of the Purchased Assets, to the extent reasonably requested by Purchaser. After two weeks from the date hereof and prior to the six month anniversary hereof, Seller shall be available for up to ten hours per month, by telephone or video conference, to answer questions with respect to the manufacturing processes of the Purchased Assets.

- (d) **Covenant Not to Compete.** For a period of five years from and after the Closing Date, the Seller will not engage directly or indirectly in the Business that the Seller conducts or conducted as of the Closing Date in any geographic area in which the Seller conducts or conducted that Business as of the Closing Date; provided, however, that no owner of less than 1% of the outstanding stock of any publicly traded corporation shall be deemed to engage solely by reason thereof in any of its businesses. If the final judgment of a court of competent jurisdiction declares that any term or provision of this Section 8(d) is invalid or unenforceable, the Parties agree that the court making the determination of invalidity or unenforceability shall have the power to reduce the scope, duration, or area of the term or provision, to delete specific words or phrases, or to replace any invalid or unenforceable term or provision with a term or provision that is valid and enforceable and that comes closest to expressing the intention of the invalid or unenforceable term or provision, and this Agreement shall be enforceable as so modified after the expiration of the time within which the judgment may be appealed.
- (e) **Release of Liens.** The Parties acknowledge that the Purchased Assets are subject to Liens in favor of Wells Fargo Bank Minnesota, N.A. and Wells Fargo Business Credit, Inc. The Seller undertakes to obtain from each of the foregoing, as soon as practicable after the Closing Date, a waiver letter consenting to the transactions contemplated hereby. In the event that the Seller is unable to obtain such consents, the transactions contemplated hereby will be deemed null and void, and the Seller will take back the Purchased Assets and return the Purchase Price to the Purchaser along with interest calculated at a rate of 8% per annum.

Section 9. Remedies; Specific Performance.

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The Seller acknowledges and agrees that the Purchased Assets are unique and that the Purchaser will be irreparably harmed in the event that this Agreement, including the obligations of the Seller to sell and deliver the Purchased Assets to the Purchaser are not specifically enforced. The parties further agree it is impossible to measure in money the damage which will accrue by reason of a refusal by the Seller to perform such obligations under this Agreement. Therefore, in the event that the Purchaser shall institute any action to enforce such obligations, the Seller hereby acknowledges that the Purchaser does not have an adequate remedy at law and that injunctive or other equitable relief (in addition to any other remedy to which it may be entitled, at law or in equity) will not constitute any hardship upon the Seller.

Section 10. Definitions.

As used in this Agreement, the following terms shall have the meanings ascribed to them below:

- (a) "Affiliate" means, when used with reference to a specified party, (i) any entity that, directly, or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with, the specified party, and (ii) any entity of which the specified party is, directly or indirectly, the owner of an equity interest of ten (10) percent or more.
- (b) "Code" means the Internal Revenue Code of 1986, as amended, including the rules and regulations thereunder, as well as any successor or substitute provisions thereto.
- (c) "knowledge" means, with respect to the Seller, the actual knowledge after due inquiry (or what would reasonably be the knowledge if due inquiry were made) of any executive officer

(determined in accordance with Rule 16a-1(f) under the Exchange Act) of the Seller and with respect to the Purchaser, the actual knowledge after due inquiry (or what would reasonably be the knowledge if due inquiry were made) of any executive officer (determined in accordance with Rule 16a-1(f) under the Exchange Act) of the Purchaser, as the case may be.

- (d) "Lien" means any mortgage, lien, pledge, restriction, charge, security interest, claims, encumbrance, or rights, title and interest of others.
- (e) "Material Adverse Effect" means any circumstance, event, occurrence, change or effect that, individually or in the aggregate, materially and adversely affects the Purchased Assets taken as a whole; provided, however, that none of the following shall be deemed in themselves, either alone or in combination, to constitute, and none of the following shall be taken into account in determining whether there has been or will be a Material Adverse Effect: (a) any adverse change, effect, event, occurrence, state of facts or development attributable to conditions affecting the industries in which the Seller participates as a whole, the economy of the United States as a whole or foreign economies in any locations where the Seller has material operations or sales, (b) any adverse change, effect, event, occurrence, state of facts or development arising from or relating to any change in accounting

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requirements or principles or any change in applicable laws, rules or regulations or the interpretation thereof, (c) any adverse change, effect, event, occurrence, state of facts or development arising from any action taken by the Purchaser or any of its directors, officers, employees, agents or Affiliates, other than the execution and delivery of this Agreement and any permitted public announcement thereof.

- (f) "Person" means any individual, general partnership, limited partnership, corporation, limited liability company, joint venture, trust, business trust, cooperative, association, governmental entity (or any department, agency, or political subdivision thereof), or other form of organization.

Section 11. Expenses.

Whether or not the transactions contemplated by this Agreement are consummated, each party will pay its respective expenses, including all fees and expenses of counsel, accountants and other advisors, incurred in connection with the origination, negotiation, execution and performance of this Agreement.

Section 12. Further Assurances.

The parties agree that, on and after the Closing Date, each shall take all reasonable action and execute any commercially reasonable documents, instruments or conveyances which may be reasonably necessary or advisable to carry out any of the provisions hereof. All such actions and assistance shall be taken and rendered at the sole cost and expense of the requesting party.

Section 13. No Public Announcement.

The Purchaser and the Seller agree that the existence, nature and terms and conditions of this Agreement and discussions between the parties regarding the transactions contemplated hereby are, and shall be treated as, confidential by the parties. Accordingly, each party agrees that it (a) will make no public comment concerning or announcement of the transactions contemplated hereby; (b) will respond to all inquiries concerning the transactions contemplated hereby by stating that it is such company's policy not to comment on such inquiries; (c) will take reasonable steps to restrict knowledge of the transactions contemplated hereby to those who need to know; and (d) will notify the other

parties of any rumor external to the parties of the transactions contemplated hereby. Notwithstanding the foregoing, the Purchaser acknowledge and agree that the Seller, as a public company, is subject to certain disclosure requirements under applicable securities laws. For this reason, the Seller reserves the right to disclose the existence of and the status and terms of negotiations at any time it is advised by its counsel that securities laws or the rules of any stock market on which its shares are traded require such disclosure, and the Seller shall have the right to issue a press release regarding the transactions contemplated hereby upon the signing of this Agreement, provided that the text of any such press release shall be reasonably acceptable to the Purchaser.

Section 14. Entire Agreement.

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This Agreement contains the entire agreement among the Parties hereto as to the subject matter hereof, and supersedes all prior agreements and understandings between them relating thereto, written or oral, to the extent they have related in any way to the subject matter hereof.

Section 15. Amendments and Waivers.

This Agreement may not be amended or modified, except by a writing executed by the Party against which such amendment or waiver is sought to be enforced. No extension of time for, or waiver of the performance of, any obligation of any Party hereto shall be effective unless it is made in a writing signed by the Party granting such extension or waiver. Unless it specifically states otherwise, no waiver shall constitute or be construed as a waiver of any default, misrepresentation, breach of warranty or covenant hereunder, or subsequent breach or non-performance.

Section 16. Notices.

Any notice, request, demand, waiver, consent, approval or other communication which is required or permitted to be given pursuant to this Agreement shall be in writing and shall be given in person or by facsimile or by certified or registered first-class mail or internationally recognized express courier delivery service addressed as follows:

If to the Purchaser: The National Medical Products Co., Ltd.
2nd Industrial City
P.O. Box 7681
Riyadh 11472
Saudi Arabia
Fax: 00 966 1 498 5607
Attn: Fahad Al Moammar, President

with copies to: Andre Granger, Vice President Operations
The National Medical Products Co., Ltd.
Fax: 00 966 1 498 5607

Mark J. Vieno, Esq.
2116 Second Avenue South
Minneapolis, MN 55404

If to the Seller: LecTec Corporation
10701 Red Circle Drive
Minnetonka, MN 55343
Attention: Rodney A. Young

with a copy to: Dorsey & Whitney, LLP
220 South Sixth Street
Minneapolis, MN 55402

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Attention: Timothy S. Hearn, Esq.

Any such address may be changed by any party by written notice to the other parties given in accordance herewith. Any notice shall be deemed to be given three (3) days after being placed for delivery so addressed with postage or other charges prepaid, provided, however, that any written notice actually received by any party in less than three (3) days shall be deemed to be given, for all purposes of this Agreement, at the time it is received. Notice given by facsimile shall be deemed given upon electronic confirmation of delivery.

Section 17. Governing Law; Consent to Jurisdiction.

This Agreement is made and shall be governed and construed in accordance with the laws of the State of Minnesota, without giving effect to any choice or conflicts of laws principles thereof. This Agreement may be enforced in any federal court or state court sitting in Minnesota; and the parties hereto consent to the jurisdiction and venue of any such court and waive any argument that venue in such forum is not convenient.

Section 18. Successors and Assigns.

This Agreement shall be binding upon and inure to the benefit of the Parties named herein and their respective successors and permitted assigns. No Party may assign either this Agreement or any of its rights, interests, or obligations hereunder without the prior written approval of the other Party; PROVIDED HOWEVER, that the Purchaser may (i) assign any or all of its rights and interests hereunder to one or more of its Affiliates and (ii) designate one or more of its Affiliates to perform its obligations hereunder (in any or all of which cases the Purchaser nonetheless shall remain responsible for the performance of all of its obligations hereunder).

Section 19. Captions.

Section headings and other captions are supplied herein for convenience only and shall not be deemed a part of this Agreement for any purpose.

Section 20. Counterparts.

This Agreement may be executed in any number of counterparts, each of which shall be deemed an original for all purposes, and all of which together shall constitute one agreement. A facsimile signature followed by an original signature shall be sufficient to execute this Agreement.

Section 21. Severability.

If any term or provision of this Agreement, or the application thereof to any Person or circumstance, shall to any extent be invalid or unenforceable under applicable law, the remainder of this Agreement, or the application of such term or provision to Persons or circumstances other than those as to which it is invalid or unenforceable under applicable law, shall not be affected thereby and each term and provision of this Agreement shall be valid and enforced to the fullest extent permitted by applicable law.

Section 22. No Third Party Beneficiaries.

Nothing in this Agreement shall confer any rights or remedies upon any person or entity that is not a party or permitted assignee of a party to this Agreement, except Indemnified Parties (as defined in Section 17).

Section 23. Construction

The Parties have participated jointly in the negotiation and drafting of this Agreement. In the event an ambiguity or question of intent or interpretation arises, this Agreement shall be construed as if drafted jointly by the Parties and no presumption or burden of proof shall arise favoring or disfavoring any Party by virtue of the authorship of any of the provisions of this Agreement. Any reference to any federal, state, local, or foreign statute

or law shall be deemed also to refer to all rules and regulations promulgated thereunder, unless the context requires otherwise. The word "including" shall mean including without limitation. The Parties intend that each representation, warranty, and covenant contained herein shall have independent significance. If any Party has breached any representation, warranty, or covenant contained herein in any respect, the fact that there exists another representation, warranty, or covenant relating to the same subject matter (regardless of the relative levels of specificity) which the Party has not breached shall not detract from or mitigate the fact that the Party is in breach of the first representation, warranty, or covenant.

Section 24. Bulk Sales Laws.

The parties hereby waive compliance with the provisions of all applicable bulk sales laws (if any are applicable).

* * * * *

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IN WITNESS WHEREOF, the parties hereto have duly executed and delivered this Agreement as of the day and year first above written.

THE NATIONAL MEDICAL PRODUCTS CO., LTD.

By /s/ Fahad Al Moammar

Its: President

LECTEC CORPORATION

By /s/ Rodney A. Young

Its: Chairman, Chief Executive Officer
and President

[Signature Page to Asset Purchase Agreement]

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