

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 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 **September 30, 2023**

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____

Commission file number: **001-33216**

SONOMA PHARMACEUTICALS, INC.
(Name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of Incorporation or Organization)

68-0423298
(I.R.S. Employer identification No.)

5445 Conestoga Court, Suite 150, Boulder, CO
(Address of principal executive offices)

80301
(Zip Code)

(800) 759-9305
(Registrant's telephone number, including area code)

N/A
(Former name or former address and former fiscal year, if changed since last report)

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of Each Class</u>	<u>Trading Symbol</u>	<u>Name of Each Exchange on Which Registered</u>
Common Stock, \$0.0001 par value	SNOA	The Nasdaq Stock Market LLC

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 ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act:

Large accelerated Filer <input type="checkbox"/>	Accelerated Filer <input type="checkbox"/>
Non-accelerated Filer <input checked="" type="checkbox"/>	Smaller reporting company <input checked="" type="checkbox"/>
Emerging Growth Company <input type="checkbox"/>	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

The number of shares outstanding of the registrant's common stock, par value \$0.0001 per share, as of November 9, 2023 was 13,679,333.

SONOMA PHARMACEUTICALS, INC.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

SONOMA PHARMACEUTICALS, INC. AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
(In thousands, except share amounts)

	September 30, 2023 (Unaudited)	March 31, 2023
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 2,137	\$ 3,820
Accounts receivable, net	2,223	2,572
Inventories, net	2,513	2,858
Prepaid expenses and other current assets	4,395	4,308
Current portion of deferred consideration, net of discount	248	240
Total current assets	11,516	13,798
Property and equipment, net	433	488
Operating lease, right of use assets	350	418
Deferred tax asset	840	949
Deferred consideration, net of discount, less current portion	421	505
Other assets	75	73
Total assets	<u>\$ 13,635</u>	<u>\$ 16,231</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 987	\$ 841
Accrued expenses and other current liabilities	1,702	2,029
Deferred revenue	101	100
Deferred revenue Invekra	61	60
Short-term debt	172	431
Operating lease liabilities	216	256
Total current liabilities	3,239	3,717
Long-term deferred revenue Invekra	114	140
Withholding tax payable	4,473	4,235
Operating lease liabilities, less current portion	134	162
Total liabilities	7,960	8,254
Commitments and Contingencies (Note 5)		
Stockholders' Equity		
Convertible preferred stock, \$0.0001 par value; 714,286 shares authorized at September 30, 2023 and March 31, 2023, respectively, no shares issued and outstanding at September 30, 2023 and March 31, 2023, respectively	—	—
Common stock, \$0.0001 par value; 24,000,000 shares authorized at September 30, 2023 and March 31, 2023, respectively, 5,179,333 and 4,933,550 shares issued and outstanding at September 30, 2023 and March 31, 2023, respectively (Note 7)	1	5
Additional paid-in capital	201,210	200,904
Accumulated deficit	(192,416)	(189,514)
Accumulated other comprehensive loss	(3,120)	(3,418)
Total stockholders' equity	5,675	7,977
Total liabilities and stockholders' equity	<u>\$ 13,635</u>	<u>\$ 16,231</u>

The accompanying footnotes are an integral part of these unaudited condensed consolidated financial statements.

SONOMA PHARMACEUTICALS, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Comprehensive Loss
(In thousands, except per share amounts)
(Unaudited)

	Three Months Ended September 30,		Six Months Ended September 30,	
	2023	2022	2023	2022
Revenues	\$ 2,731	\$ 3,331	\$ 6,158	\$ 7,314
Cost of revenues	1,741	1,795	3,964	4,132
Gross profit	990	1,536	2,194	3,182
Operating expenses				
Research and development	536	200	861	406
Selling, general and administrative	1,662	2,067	3,781	4,362
Total operating expenses	2,198	2,267	4,642	4,768
Loss from operations	(1,208)	(731)	(2,448)	(1,586)
Other expense, net	(90)	(186)	(301)	(253)
Loss before income taxes	(1,298)	(917)	(2,749)	(1,839)
Income tax expense	(186)	(100)	(153)	(65)
Net loss	<u>\$ (1,484)</u>	<u>\$ (1,017)</u>	<u>\$ (2,902)</u>	<u>\$ (1,904)</u>
Net loss per share: basic and diluted	<u>\$ (0.29)</u>	<u>\$ (0.33)</u>	<u>\$ (0.57)</u>	<u>\$ (0.61)</u>
Weighted-average number of shares: basic and diluted	<u>5,164</u>	<u>3,101</u>	<u>5,051</u>	<u>3,101</u>
Other comprehensive loss				
Net loss	\$ (1,484)	\$ (1,017)	\$ (2,902)	\$ (1,904)
Foreign currency translation adjustments	(213)	(34)	298	(99)
Comprehensive loss	<u>\$ (1,697)</u>	<u>\$ (1,051)</u>	<u>\$ (2,604)</u>	<u>\$ (2,003)</u>

The accompanying footnotes are an integral part of these unaudited condensed consolidated financial statements.

SONOMA PHARMACEUTICALS, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Six Months Ended September 30,	
	2023	2022
Cash flows from operating activities		
Net loss	\$ (2,902)	\$ (1,904)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	90	59
Stock-based compensation	307	327
Deferred tax asset	144	(139)
Changes in operating assets and liabilities:		
Accounts receivable	375	(160)
Inventories	403	(447)
Deferred consideration	104	82
Prepaid expenses and other current assets	47	397
Operating lease right-of-use assets	79	21
Accounts payable	132	(558)
Accrued expenses and other current liabilities	(353)	(44)
Withholding tax payable	238	175
Operating lease liabilities	(79)	(23)
Deferred revenue	(31)	(1,149)
Net cash used in operating activities	<u>(1,446)</u>	<u>(3,363)</u>
Cash flows from investing activities:		
Purchases of property and equipment	(19)	(48)
Deposits	—	(162)
Net cash used in investing activities	<u>(19)</u>	<u>(210)</u>
Cash flows from financing activities:		
Payment on ATM agreement offering	(5)	—
Payments on PPP Loan	—	(120)
Proceeds from debt	—	15
Principal payments on short-term debt	(259)	(460)
Net cash used in financing activities	<u>(264)</u>	<u>(565)</u>
Effect of exchange rate on cash and cash equivalents	46	93
Net decrease in cash and cash equivalents	(1,683)	(4,045)
Cash and cash equivalents, beginning of period	3,820	7,396
Cash and cash equivalents, end of period	<u>\$ 2,137</u>	<u>\$ 3,351</u>
Supplemental disclosure of cash flow information:		
Cash paid for interest	<u>\$ 10</u>	<u>\$ 8</u>

The accompanying footnotes are an integral part of these unaudited condensed consolidated financial statements.

SONOMA PHARMACEUTICALS, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Changes in Stockholders' Equity
For the Six Months ended September 30, 2023 and 2022
(In thousands, except share amounts)
(Unaudited)

	Common Stock (\$0.0001 par Value)		Additional Paid in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total
	Shares	Amount				
Balance, March 31, 2023	4,933,550	\$ 5	\$ 200,904	\$ (189,514)	\$ (3,418)	\$ 7,977
Cost in connection with ATM	—	—	(5)	—	—	(5)
Employee stock-based compensation expenses	208,046	—	177	—	—	177
Foreign currency translation adjustment	—	—	—	—	511	511
Net loss	—	—	—	(1,418)	—	(1,418)
Balance, June 30, 2023	5,141,596	\$ 5	\$ 201,076	\$ (190,932)	\$ (2,907)	\$ 7,242
Adjustment to correct par value	—	(4)	4	—	—	—
Employee stock-based compensation expenses	37,737	—	130	—	—	130
Foreign currency translation adjustment	—	—	—	—	(213)	(213)
Net loss	—	—	—	(1,484)	—	(1,484)
Balance, September 30, 2023	5,179,333	\$ 1	\$ 201,210	\$ (192,416)	\$ (3,120)	\$ 5,675

	Common Stock (\$0.0001 par Value)		Additional Paid in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total
	Shares	Amount				
Balance March 31, 2022	3,100,937	\$ 2	\$ 197,370	\$ (184,363)	\$ (4,312)	\$ 8,697
Employee stock-based compensation expenses	—	—	214	—	—	214
Foreign currency translation adjustment	—	—	—	—	(65)	(65)
Net loss	—	—	—	(887)	—	(887)
Balance, June 30, 2022	3,100,937	\$ 2	\$ 197,584	\$ (185,250)	\$ (4,377)	\$ 7,959
Employee stock-based compensation expense	—	—	108	—	—	108
Stock based compensation related to issuance of restricted common stock	2,035	—	5	—	—	5
Foreign currency translation adjustment	—	—	—	—	(34)	(34)
Net loss	—	—	—	(1,017)	—	(1,017)
Balance, September 30, 2022	3,102,972	\$ 2	\$ 197,697	\$ (186,267)	\$ (4,411)	\$ 7,021

The accompanying footnotes are an integral part of these unaudited condensed consolidated financial statements.

SONOMA PHARMACEUTICALS, INC. AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements
(Rounded to nearest thousand unless specified)
(Unaudited)

Note 1. Organization and Recent Developments

Organization

Sonoma Pharmaceuticals, Inc. (the “Company”) was incorporated under the laws of the State of California in April 1999 and was reincorporated under the laws of the State of Delaware in December 2006. The Company moved its principal office to Woodstock, Georgia from Petaluma, California in June 2020 and to Boulder, Colorado in October 2022. The Company is a global healthcare leader for developing and producing stabilized hypochlorous acid (“HOCl”) products for a wide range of applications, including wound care, eye, oral and nasal care, dermatological conditions, podiatry, animal health care, and as a non-toxic disinfectant. The Company’s products reduce infections, scarring and harmful inflammatory responses in a safe and effective manner. In-vitro and clinical studies of HOCl show it to have impressive antipruritic, antimicrobial, antiviral and anti-inflammatory properties. The Company’s stabilized HOCl immediately relieves itch and pain, kills pathogens and breaks down biofilm, does not sting or irritate skin and oxygenates the cells in the area treated assisting the body in its natural healing process. The Company sells its products either directly or via partners in 55 countries worldwide.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial statements and are in the form prescribed by the Securities and Exchange Commission (the “SEC”) in instructions to Form 10-Q and Rule 10-01 of Regulation S-X. The accompanying condensed consolidated financial statements reflect all adjustments, consisting of normal recurring adjustments, considered necessary for a fair statement of the Company’s financial position, results of operations and cash flows for the periods indicated. All material intercompany accounts and transactions have been eliminated in consolidation. The accompanying condensed consolidated financial statements should be read in conjunction with the consolidated financial statements for the year ended March 31, 2023, and notes thereto included in the Company’s annual report on Form 10-K, which was filed with the SEC on June 21, 2023.

Note 2. Liquidity and Financial Condition

The Company reported a net loss of \$1,484,000 and \$1,017,000 for the three months ended September 30, 2023 and 2022, respectively, and \$2,902,000 and \$1,904,000 for the six months ended September 30, 2023 and 2022, respectively. At September 30, 2023 and March 31, 2023, the Company’s accumulated deficit amounted to \$192,416,000 and \$189,514,000, respectively. The Company had working capital of \$8,277,000 and \$10,081,000 as of September 30, 2023 and March 31, 2023, respectively. The cash balance at September 30, 2023 and March 31, 2023 was \$2,137,000 and \$3,820,000, respectively. During the six months ended September 30, 2023 and 2022, net cash used in operating activities amounted to \$1,446,000 and \$3,363,000, respectively.

Management believes that the Company has access to additional capital resources through possible public or private equity offerings, debt financings, corporate collaborations or other means; however, the Company cannot provide any assurance that other new financings will be available on commercially acceptable terms, if needed. If the economic climate in the U.S. deteriorates, the Company’s ability to raise additional capital could be negatively impacted. If the Company is unable to secure additional capital, it may be required to take additional measures to reduce costs in order to conserve its cash in amounts sufficient to sustain operations and meet its obligations. These measures could cause significant delays in the Company’s continued efforts to commercialize its products, which is critical to the realization of its business plan and the future operations of the Company. These matters raise substantial doubt about the Company’s ability to continue as a going concern. The accompanying condensed consolidated financial statements do not include any adjustments that may be necessary should the Company be unable to continue as a going concern.

Note 3. Summary of Significant Accounting Policies**Use of Estimates**

The preparation of condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent liabilities at the dates of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates. Significant estimates and assumptions include reserves and write-downs related to receivables and inventories, the valuation allowance relating to the Company's deferred tax assets, valuation of equity and the estimated amortization periods of upfront product licensing fees received from customers. Periodically, the Company evaluates and adjusts estimates accordingly.

Reclassification

During the three and six months ended September 30, 2023, the Company aligned its accounting policy and conformed its prior presentation of certain costs it views as research and development efforts. These costs are now included in research and development, whereas they were previously included in cost of revenues. During the three and six months ended September 30, 2022, the Company reclassified \$200,000 and \$400,000, respectively, from cost of revenues to research and development. The reclassification in the prior periods increased research and development and decreased cost of revenues by the same amount. The reclassification had no impact on total operating costs, earnings from operations, net earnings, earnings per share or total equity.

Net Loss per Share

The following table provides the net loss for each period along with the computation of basic and diluted net loss per share:

<i>(In thousands, except per share data)</i>	Three Months Ended September 30,		Six Months Ended September 30,	
	2023	2022	2023	2022
Numerator:				
Net loss	\$ (1,484)	\$ (1,017)	\$ (2,902)	\$ (1,904)
Denominator:				
Weighted-average number of common shares outstanding: basic and diluted	<u>5,164</u>	<u>3,101</u>	<u>5,051</u>	<u>3,101</u>
Net loss per share: basic and diluted	<u>\$ (0.29)</u>	<u>\$ (0.33)</u>	<u>\$ (0.57)</u>	<u>\$ (0.61)</u>

The computation of basic loss per share for the three and six months ended September 30, 2023, and 2022 excludes the potentially dilutive securities summarized in the table below because their inclusion would be anti-dilutive.

<i>(In thousands)</i>	Three Months Ended September 30,		Six Months Ended September 30,	
	2023	2022	2023	2022
Stock options	519	406	519	406
Warrants	103	108	103	108
Common stock units (1)	46	46	46	46
	<u>668</u>	<u>560</u>	<u>668</u>	<u>560</u>

(1) Consists of 30,668 restricted stock units and warrants to purchase 15,332 shares of common stock

Revenue Recognition

The Company recognizes revenue in accordance with Accounting Standards Codification (“ASC”), Topic 606 Revenue from Contracts with Customers (“Topic 606”). Revenue is recognized when the Company transfers promised goods or services to the customer, in an amount that reflects the consideration which the Company expects to receive in exchange for those goods or services. In determining the appropriate amount of revenue to be recognized as the Company fulfills its obligations under the agreement, the Company performs the following steps: (i) identification of the promised goods or services in the contract; (ii) determination of whether the promised goods or services are performance obligations, including whether they are distinct in the context of the contract; (iii) measurement of the transaction price, including the constraint on variable consideration; (iv) allocation of the transaction price to the performance obligations; and (v) recognition of revenue when (or as) the Company satisfies each performance obligation. The Company only applies the five-step model to contracts when it is probable that it will collect the consideration it is entitled to in exchange for the goods or services it transfers to the customer.

The Company derives the majority of its revenue through sales of its products directly to end users and to distributors. The Company also sells products to a customer base, including hospitals, medical centers, doctors, pharmacies, distributors and wholesalers. The Company has also entered into agreements to license its technology and products.

The Company considers customer purchase orders, which in some cases are governed by master sales agreements, to be the contracts with a customer. For each contract, the Company considers the promise to transfer products, each of which are distinct, to be the identified performance obligations. In determining the transaction price the Company evaluates whether the price is subject to refund or adjustment to determine the net consideration to which it expects to be entitled.

For all of the Company’s sales to non-consignment distribution channels, revenue is recognized when control of the product is transferred to the customer (i.e. when its performance obligation is satisfied), which typically occurs when title passes to the customer upon shipment but could occur when the customer receives the product based on the terms of the agreement with the customer. For product sales to its value-added resellers, non-stocking distributors and end-user customers, the Company grants return privileges to its customers, and because the Company has a long history with its customers, the Company is able to estimate the amount of product that will be returned. Sales incentives and other programs that the Company may make available to these customers are considered to be a form of variable consideration, and the Company maintains estimated accruals and allowances using the expected value method. With the movement of these sales to a full distributor model in fiscal year 2022, the Company no longer provides these arrangements although the Company still receives some returns from the period prior to the year ended March 31, 2023.

The Company has entered into consignment arrangements, in which goods are left in the possession of another party to sell. As products are sold from the customer to third parties, the Company recognizes revenue based on a variable percentage of a fixed price. Revenue recognized varies depending on whether a patient is covered by insurance or is not covered by insurance. In addition, the Company may incur a revenue deduction related to the use of the Company’s rebate program.

Sales to stocking distributors are made under terms with fixed pricing and limited rights of return (known as “stock rotation”) of the Company’s products held in their inventory. Revenue from sales to distributors is recognized upon the transfer of control to the distributor.

The Company assessed the promised goods and services in the technical support to Invekra for a ten-year period as being a distinct service that Invekra can benefit from on its own and as separately identifiable from any other promises within the contract. Given that the distinct service is not substantially the same as other goods and services within the Invekra contract, the Company accounted for the distinct service as a performance obligation.

Accounts Receivable

Trade accounts receivable are recorded net of allowances for cash discounts for prompt payment, doubtful accounts, and sales returns. Estimates for cash discounts and sales returns are based on analysis of contractual terms and historical trends.

The Company's policy is to reserve for uncollectible accounts based on its best estimate of probable credit losses in its existing accounts receivable. The Company periodically reviews its accounts receivable to determine whether an allowance for doubtful accounts is necessary based on an analysis of past due accounts and other factors that may indicate that the realization of an account may be in doubt. Other factors that the Company considers include its existing contractual obligations, historical payment patterns of its customers and individual customer circumstances, an analysis of days sales outstanding by customer and geographic region, and a review of the local economic environment and its potential impact on government funding and reimbursement practices. Account balances deemed to be uncollectible are charged to the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. The Company did not deem it necessary to record an allowance for doubtful accounts for probable credit losses at September 30, 2023 and March 31, 2023. Additionally, at September 30, 2023 and March 31, 2023 the Company has allowances of \$24,000 and \$16,000, respectively, related to potential discounts, returns, distributor fees and rebates. The allowances are included in accounts receivable, net in the accompanying condensed consolidated balance sheets.

Inventories

Inventories are stated at the lower of cost, cost being determined on a standard cost basis (which approximates actual cost on a first-in, first-out basis), or net realizable value.

Due to changing market conditions, estimated future requirements, age of the inventories on hand and production of new products, the Company regularly reviews inventory quantities on hand and records a provision to write down excess and obsolete inventory to its estimated net realizable value. The Company recorded a provision to reduce the carrying amounts of inventories to their net realizable value in the amount of \$280,000 and \$236,000 at September 30, 2023 and March 31, 2023, respectively, which is included in cost of revenues on the Company's accompanying condensed consolidated statements of comprehensive loss.

Recent Accounting Standards

Accounting standards that have been issued or proposed by the FASB, the SEC or other standard setting bodies that do not require adoption until a future date are not expected to have a material impact on the consolidated financial statements upon adoption.

Note 4. Condensed Consolidated Balance Sheet

Inventories, net

Inventories, net consist of the following:

	September 30, 2023	March 31, 2023
Raw materials	\$ 1,493,000	\$ 1,764,000
Finished goods	1,020,000	1,094,000
Inventories, net	<u>\$ 2,513,000</u>	<u>\$ 2,858,000</u>

Leases

The Company's operating leases are comprised primarily of facility leases. The Company did not have any finance leases as of September 30, 2023 and March 31, 2023. Balance sheet information related to our leases is presented below:

	September 30, 2023	March 31, 2023
Operating leases:		
Operating lease right-of-use assets	\$ 350,000	\$ 418,000
Operating lease liabilities – current	216,000	256,000
Operating lease liabilities – non- current	134,000	162,000

Other information related to leases is presented below:

Six Months Ended September 30, 2023

Operating lease cost	\$ 216,000
Other information:	
Operating cash flows from operating leases	(79,000)
Weighted-average remaining lease term – operating leases (in months)	19.3
Weighted-average discount rate – operating leases	6.00%

As of September 30, 2023, the annual minimum lease payments of our operating lease liabilities were as follows:

For Years Ending March 31,

2024 (excluding the six months ended September 30, 2023)	\$ 81,000
2025	144,000
2026	157,000
2027	9,000
Total future minimum lease payments, undiscounted	391,000
Less: imputed interest	(41,000)
Present value of future minimum lease payments	\$ 350,000

Note 5. Commitments and Contingencies

Legal Matters

The Company may be involved in legal matters arising in the ordinary course of business including matters involving proprietary technology. While management believes that such matters are currently insignificant, matters arising in the ordinary course of business for which the Company is or could become involved in litigation may have a material adverse effect on its business and financial condition of comprehensive loss.

Employment Agreements

The Company has employment agreements in place with two of its key executives. These executive employment agreements provide, among other things, for the payment of up to eighteen months of severance compensation for terminations under certain circumstances.

Amendments

On June 16, 2023, we entered into an amended and restated employment agreement with our Chief Executive Officer, Amy Trombly. The amended and restated agreement provides that, in the event of termination upon change of control either without cause or for good reason, Ms. Trombly is entitled to receive, in addition to the other benefits described therein, a lump sum severance equal to one and a half times her base salary and one and a half times her target annual bonus. All other material terms of the amended and restated agreement remain unchanged from her prior employment agreement.

On June 16, 2023, we amended and restated our employment agreement with Bruce Thornton, our Chief Operating Officer. Under the amended and restated agreement, Mr. Thornton will serve as Executive Vice President and Chief Operating Officer of the Company. Mr. Thornton will no longer receive a monthly car allowance; however, his base salary is adjusted to include such amount. The amended and restated agreement also provides that, in the event of termination upon change of control either without cause or for good reason, Mr. Thornton is entitled to receive, in addition to the other benefits described therein, to a lump sum severance equal to one and a half times his base salary and one and a half times his target annual bonus. The agreement further provides that upon termination for any reason, Mr. Thornton's outstanding and vested equity awards shall remain exercisable for 18 months following termination. Either party may terminate the employment agreement for any reason upon at least 60 days prior written notice. All other material terms of his amended and restated agreement remain unchanged from his prior employment agreement.

Bonus Grants

On June 16, 2023, the Compensation Committee of the Board of Directors approved annual bonus awards of \$162,500 for Ms. Trombly and \$150,000 for Mr. Thornton.

Equity Awards

On June 16, 2023, the Compensation Committee of the Board of Directors approved an equity award of 100,000 shares of the Company's common stock to each of Ms. Trombly and Mr. Thornton, to be issued to on June 30, 2023, at a valuation based on the five day weighted trailing average of the Company's stock price on the day of grant. In addition, the Compensation Committee also approved a one-time cash payment by the Company as reimbursement for estimated taxes payable with respect to such equity awards. On September 22, 2023, the Company paid taxes related to the common stock issuance in the amount of \$149,000.

As of September 30, 2023, with respect to these agreements, aggregated annual salaries was \$586,000 and potential severance payments to these key executives was \$1,300,000, if triggered.

Note 6. Debt

Financing of Insurance Premiums

On February 1, 2022, the Company entered into a note agreement for \$748,000 with an interest rate of 4.68% per annum with final payment on January 1, 2023. This instrument was issued in connection with financing insurance premiums. The note is payable in ten monthly installment payments of principal and interest of \$76,000, with the first installment beginning March 1, 2022.

On February 1, 2023, the Company entered into a note agreement for \$453,000 with an interest rate of 8.98% per annum with final payment on January 1, 2024. This instrument was issued in connection with financing insurance premiums. The note is payable in eleven monthly installment payments of principal and interest of \$43,000, with the first installment beginning March 1, 2023.

Note 7. Stockholders' Equity**Authorized Capital**

The Company is authorized to issue up to 24,000,000 shares of common stock with a par value of \$0.0001 per share and 714,286 shares of convertible preferred stock with a par value of \$0.0001 per share.

Note 8. Stock-Based Compensation

Stock-based compensation expense is as follows:

For the three months ended September 30, 2023 and 2022, the Company incurred \$130,000 and \$113,000 of stock-based compensation expense, respectively, and for the six months ended September 30, 2023 and 2022, the Company incurred \$307,000 and \$327,000 of stock-based compensation expense, respectively. All stock-based compensation incurred is included in selling, general and administrative expense in the accompanying condensed consolidated statements of comprehensive loss.

At September 30, 2023, there were unrecognized compensation costs of \$379,000 related to stock options which are expected to be recognized over a weighted-average amortization period of 1.04 years.

Stock options award activity is as follows:

	Number of Shares	Weighted- Average Exercise Price
Outstanding at April 1, 2023	565,000	\$ 8.84
Options granted	5,000	1.15
Options forfeited	(46,000)	34.30
Options expired	(5,000)	39.33
Outstanding at September 30, 2023	519,000	\$ 6.25
Exercisable at September 30, 2023	293,000	\$ 9.02

The aggregate intrinsic value of stock options of zero is calculated as the difference between the exercise price of the underlying stock options and the fair value of the Company's common stock, or \$0.77 per share at September 30, 2023.

	Number of Shares	Weighted Average Award Date Fair Value per Share
Unvested restricted stock awards outstanding at April 1, 2023	—	\$ —
Restricted stock awards granted	244,000	1.06
Restricted stock awards vested	(244,000)	1.06
Unvested restricted stock awards outstanding at September 30, 2023	—	\$ —

The Company did not capitalize any cost associated with stock-based compensation.

The Company issues new shares of common stock upon exercise of stock-based awards.

Note 9. Income Taxes

At the end of each interim reporting period, the Company determines the income tax provision by using an estimate of the annual effective tax rate, adjusted for discrete items occurring in the quarter.

Our effective tax rate for the three and six months ended September 30, 2023 was (12.61)% and (5.12)%, respectively. The Company's effective tax rate for the three and six months ended September 30, 2023 differed from the federal statutory tax rate of 21% primarily due to the valuation allowance recognized against deferred tax assets in the U.S., and permanent tax adjustment of intercompany interest expense in Mexico and Netherlands.

Judgment is required in determining whether deferred tax assets will be realized in full or in part. Management assesses the available positive and negative evidence on a jurisdictional basis to estimate if deferred tax assets will be recognized and when it is more likely than not that all or some deferred tax assets will not be realized, and a valuation allowance must be established. As of September 30, 2023, the Company continues to maintain a valuation allowance in the U.S.

Note 10. Revenue Disaggregation

The Company generates revenues from products which are sold into the human and animal healthcare markets and to multiple geographic regions.

The following table presents the Company's disaggregated revenues by revenue source:

<i>(In thousands)</i>	Three Months Ended September 30,		Six Months Ended September 30,	
	2023	2022	2023	2022
Human Care	\$ 2,075	\$ 2,447	\$ 4,825	\$ 4,615
Animal Care	489	737	1,067	1,523
Service and Royalty	167	147	266	1,176
	<u>\$ 2,731</u>	<u>\$ 3,331</u>	<u>\$ 6,158</u>	<u>\$ 7,314</u>

The following table shows the Company's revenues by geographic region:

<i>(In thousands)</i>	Three Months Ended September 30,		Six Months Ended September 30,	
	2023	2022	2023	2022
United States	\$ 590	\$ 973	\$ 1,396	\$ 1,842
Europe	1,201	1,170	2,271	2,012
Asia	346	518	1,208	1,438
Latin America	260	394	747	1,444
Rest of the World	334	276	536	578
Total	<u>\$ 2,731</u>	<u>\$ 3,331</u>	<u>\$ 6,158</u>	<u>\$ 7,314</u>

The Company aligned the geographic regions reported in the Asia and Rest of World segments in fiscal year 2022 to conform to the current year presentation. For the three months ended September 30, 2022, the Company reclassified \$188,000 from Rest of World to Asia and for the six months ended September 30, 2022, the Company reclassified \$283,000 from Rest of World to Asia.

Note 11. Significant Customer Concentrations

For the three months ended September 30, 2023, customer C represented 21%, customer A represented 13%, and customer B represented 10% of net revenue. For the three months ended September 30, 2022, customer A represented 20%, customer C represented 13% and customer B represented 12% of net revenue. For the six months ended September 30, 2023, customer C represented 17%, customer B represented 12% and customer A represented 14% of net revenue. For the six months ended September 30, 2022, customer B represented 20%, customer A represented 17% and customer C represented 10% of net revenue.

At September 30, 2023, customer D represented 20%, customer C represented 13% and customer A represented 11% of our net accounts receivable balance.

At September 30, 2022, customer A represented 35% and customer D represented 20% of our net accounts receivable balance.

Note 12. Subsequent Events

On October 26, 2023, the Company entered into a placement agency agreement with Maxim Group LLC (“Maxim”), pursuant to which Maxim agreed to use its reasonable best efforts to solicit offers to purchase up to an aggregate of 8,500,000 shares of the Company’s common stock, par value \$0.0001 per share. The Company agreed to pay Maxim a cash fee equal to 8.0% of the gross proceeds from the offering, plus reimbursement of up to \$75,000 of legal fees and other expenses. Additionally, on October 26, 2023, the Company entered into a securities purchase agreement with the purchasers party thereto for the sale and issuance of an aggregate of up to 8,500,000 shares of the Company’s common stock at a public offering price of \$0.20 per share.

The closing of the offering occurred on October 30, 2023. In connection with the offering, the Company sold 8,500,000 shares of the Company’s common stock for aggregate gross proceeds of \$1,700,000 and estimated net proceeds of \$1,414,000, after deducting placement agent fees and other estimated offering expenses payable by the Company.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion of our financial condition and results of operations should be read in conjunction with the condensed consolidated financial statements and notes to those statements included elsewhere in this Quarterly Report on Form 10-Q as of September 30, 2023 and our audited consolidated financial statements for the year ended March 31, 2023 included in our Annual Report on Form 10-K, filed with the Securities and Exchange Commission on June 21, 2023.

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. When used in this report, the words "anticipate," "suggest," "estimate," "plan," "aim," "seek," "project," "continue," "ongoing," "potential," "expect," "predict," "believe," "intend," "may," "will," "should," "could," "would," "likely," "proposal," and similar expressions are intended to identify forward-looking statements.

Forward-looking statements are subject to risks and uncertainties that could cause our actual results to differ materially from those projected. These risks and uncertainties include, but are not limited to the risks described in our Annual Report on Form 10-K including: our ability to become profitable; our dependence on third-party distributors; certain tax impacts of inter-company loans between us and our Mexican subsidiary; the progress and timing of our development programs and regulatory approvals for our products; the benefits and effectiveness of our products; the ability of our products to meet existing or future regulatory standards; the progress and timing of clinical trials and physician studies; our expectations and capabilities relating to the sales and marketing of our current products and our product candidates; our ability to compete with other companies that are developing or selling products that are competitive with our products; the establishment of strategic partnerships for the development or sale of products; the risk our research and development efforts do not lead to new products; the timing of commercializing our products; our ability to penetrate markets through our sales force, distribution network, and strategic business partners to gain a foothold in the market and generate attractive margins; the ability to attain specified revenue goals within a specified time frame, if at all, or to reduce costs; the outcome of discussions with the U.S. Food and Drug Administration, or FDA, and other regulatory agencies; the content and timing of submissions to, and decisions made by, the FDA and other regulatory agencies, including demonstrating to the satisfaction of the FDA the safety and efficacy of our products; our ability to manufacture sufficient amounts of our products for commercialization activities; our ability to protect our intellectual property and operate our business without infringing on the intellectual property of others; our ability to continue to expand our intellectual property portfolio; the risk we may need to indemnify our distributors or other third parties; risks attendant with conducting a significant portion of our business outside the United States; our ability to comply with complex federal and state fraud and abuse laws, including state and federal anti-kickback laws; risks associated with changes to health care laws; our ability to attract and retain qualified directors, officers and employees; our expectations relating to the concentration of our revenue from international sales; our ability to expand to and commercialize products in markets outside the wound care market; our ability to protect our information technology and infrastructure; and the impact of any future changes in accounting regulations or practices in general with respect to public companies. These forward-looking statements speak only as of the date hereof. We expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based, except as required by law.

Our Business

We are a global healthcare leader for developing and producing stabilized hypochlorous acid, or HOCl, products for a wide range of applications, including wound care, eye, oral and nasal care, dermatological conditions, podiatry, animal health care and non-toxic disinfectants. Our products reduce infections, scarring and harmful inflammatory responses in a safe and effective manner. In-vitro and clinical studies of HOCl show it to have impressive antipruritic, antimicrobial, antiviral and anti-inflammatory properties. Our stabilized HOCl immediately relieves itch and pain, kills pathogens and breaks down biofilm, does not sting or irritate skin and oxygenates the cells in the area treated, assisting the body in its natural healing process. We sell our products either directly or via partners in 55 countries worldwide.

Business Channels

Our core market differentiation is based on being the leading developer and producer of stabilized hypochlorous acid, or HOCl, solutions. We have been in business for over 20 years, and in that time, we have developed significant scientific knowledge of how best to develop and manufacture HOCl products, backed by decades of studies and data collection. HOCl is known to be among the safest and most-effective ways to relieve itch, inflammation and burns while stimulating natural healing through increased oxygenation and eliminating persistent microorganisms and biofilms.

We sell our products based on our HOCl technology into many markets both in the U.S. and internationally. Our core strategy is to work with partners to market and distribute our products. In some cases, we market and sell our own products.

Dermatology

We have developed unique, differentiated, prescription-strength and safe dermatologic products that support paths to healing among various key dermatologic conditions. Our products are primarily targeted at the treatment of redness and irritation, the management of scars, and symptoms of eczema/atopic dermatitis. We are strategically focused on introducing innovative new products that are supported by human clinical data with applications that address specific dermatological procedures currently in demand. In addition, we look for markets where we can provide effective product line extensions and pricing to new product families.

In the United States, we partner with EMC Pharma, LLC to sell our prescription dermatology products. Pursuant to our March 2021 agreement with EMC Pharma, we manufacture products for EMC Pharma and EMC Pharma has the right to market, sell and distribute them to patients and customers for an initial term of five years, subject to meeting minimum purchase and other requirements.

In September 2021, we launched a new over-the-counter product, Regenacyn[®] Advanced Scar Gel, which is clinically proven to improve the overall appearance of scars while reducing pain, itch, redness, and inflammation. On the same day, we launched Regenacyn[®] Plus, a prescription-strength scar gel which is available as an office dispense product through physician offices.

In October 2022, we launched two new over-the-counter dermatology products in the United States, Reliefacyn[®] Advanced Itch-Burn-Rash-Pain Relief Hydrogel for the alleviation of red bumps, rashes, shallow skin fissures, peeling, and symptoms of eczema/atopic dermatitis, and Rejuvacyn[®] Advanced Skin Repair Cooling Mist for management of minor skin irritations following cosmetic procedures as well as daily skin health and hydration.

In June 2022, the Natural Products Association certified Rejuvacyn Advanced as a Natural Personal Care Product. Reliefacyn Advanced received the National Eczema Association Seal of Acceptance[™] in 2023.

In January 2023, we launched a line of office dispense products exclusively for skin care professionals, including two new prescription strength dermatology products, Reliefacyn[®] Plus Advanced Itch-Burn-Rash-Pain Relief Hydrogel and Rejuvacyn[®] Plus Skin Repair Cooling Mist. These products, along with Regenacyn[®] Plus Scar Gel, are marketed and sold directly to dermatology practices and medical spas.

In April 2023, we introduced a new pediatric dermatology and wound care product for over-the-counter use, Pediacyn[™] All Natural Skin Care & First Aid For Children.

Our consumer products are available through Amazon.com, our online store, and third-party distributors.

We sell dermatology products in Europe and Asia through distributors. In these international markets, we have a network of partners, ranging from country specific distributors to large pharmaceutical companies to full-service sales and marketing companies. We work with our international partners to create products they can market in their home country. Some products we develop and manufacture are custom label while others use branding we have already developed. We have created or co-developed a wide range of products for international markets using our core HOCl technology.

First Aid and Wound Care

Our HOCl-based wound care products are intended for the treatment of acute and chronic wounds as well as first- and second-degree burns, and as an intraoperative irrigation treatment. They work by first removing foreign material and debris from the skin surface and moistening the skin, thereby improving wound healing. Secondly, our HOCl products assist in the wound healing process by removing microorganisms. HOCl is an important constituent of our innate immune system, formed and released by the macrophages during phagocytosis. Highly organized cell structures such as human tissue can tolerate the action of our wound care solution while single-celled microorganisms cannot, making our products advantageous to other wound-irrigation and antiseptic solutions. Due to its unique chemistry, our wound treatment solution is also much more stable than similar products on the market and therefore maintains much higher levels of hypochlorous acid over its shelf life.

In the United States, we sell our wound care products directly to hospitals, physicians, nurses, and other healthcare practitioners and indirectly through non-exclusive distribution arrangements. In Europe, the Middle East and Asia, we sell our wound care products through a diverse network of distributors.

To respond to market demand for our HOCl technology-based products, we launched our first direct to consumer over-the-counter product in the United States in February 2021. Microcyn[®] OTC Wound and Skin Cleanser is formulated for home use without prescription to help manage and cleanse wounds, minor cuts, and burns, including sunburns and other skin irritations. Microcyn OTC is available without prescription through Amazon.com, our online store, and third-party distributors.

In March 2021, we received approval to market and use our HOCl products as biocides under Article 95 of the European Biocidal Products Regulation in France, Germany and Portugal. The approval applies to our products MucoClyns[™] for human hygiene to be marketed and commercialized by us, MicrocynAH[®] for animal health marketed and commercialized through our partner, Petagon Limited, and MicroSafe for disinfectant use to be marketed and commercialized through our partner, MicroSafe Group DMCC.

In June 2022, the Natural Products Association certified Microcyn OTC as a Natural Personal Care Product in the United States.

In June 2023, we announced a new application of our HOCl technology for intraoperative pulse lavage irrigation treatment, which can replace commonly used IV bags in a variety of surgical procedures. The intraoperative pulse lavage container is designed to be used in combination with a pulse lavage irrigation device, or flush gun, for abdominal, laparoscopic, orthopedic, and periprosthetic procedures. It is in trial use by hospitals in Europe, and we anticipate commercial launch in the U.S. in 2024.

Eye Care

Our prescription product Acucyn[™] is an antimicrobial prescription solution for the treatment of blepharitis and the daily hygiene of eyelids and lashes and helps manage red, itchy, crusty and inflamed eyes. It is strong enough to kill the bacteria that causes discomfort, fast enough to provide near instant relief, and gentle enough to use as often as needed. In the United States, our partner EMC Pharma sells Acucyn through its distribution network.

In September 2021, we launched Ocucyn[®] Eyelid & Eyelash Cleanser, which is sold directly to consumers on Amazon.com, through our online store, and through third party distributors. Ocucyn[®] Eyelid & Eyelash Cleanser, designed for everyday use, is a safe, gentle, and effective solution for good eyelid and eyelash hygiene.

In international markets we rely on distribution partners to sell our eye products. On May 19, 2020, we entered into an expanded license and distribution agreement with our existing partner, Brill International S.L., for our Microdacyn60[®] Eye Care HOCl-based product. Under the license and distribution agreement, Brill has the right to market and distribute our eye care product under the private label Ocudox[™] in Italy, Germany, Spain, Portugal, France, and the United Kingdom for a period of 10 years, subject to meeting annual minimum sales quantities. In return, Brill paid us a one-time fee and the agreed upon supply prices. In parts of Asia, Dyamed Biotech markets our eye product under the private label Ocucyn.

Oral, Dental and Nasal Care

We sell a variety of oral, dental, and nasal products around the world.

In late 2020, we launched a HOCl-based product in the dental, head and neck markets called Endocyn[®], a biocompatible root canal irrigant. In the U.S., we sell Endocyn through U.S.-based distributors.

In international markets, our product Microdacyn60[®] Oral Care treats mouth and throat infections and thrush. Microdacyn60 assists in reducing inflammation and pain, provides soothing cough relief and does not contain any harmful chemicals. It does not stain teeth, is non-irritating, non-sensitizing, has no contraindications and is ready for use with no mixing or dilution.

Our international nasal care product Sinudox[™] based on our HOCl technology is an electrolyzed solution intended for nasal irrigation. Sinudox clears and cleans stuffy, runny noses and blocked or inflamed sinuses by ancillary ingredients that may have a local antimicrobial effect. Sinudox is currently sold through Amazon in Europe. In other parts of the world, we partner with distributors to sell Sinudox.

Podiatry

Our HOCl-based wound care products are also indicated for the treatment of diabetic foot ulcers. In the United States, we sell our wound care products directly to podiatrists, as well as hospitals, nurses, and other healthcare practitioners, and indirectly through non-exclusive distribution arrangements. In Europe, we sell our wound care products for podiatric use through a diverse network of distributors.

On April 11, 2023, we launched Podiacyn[™] Advanced Everyday Foot Care direct to consumers for over-the-counter use in the United States, intended for management of foot odors, infections, and irritations, as well as daily foot health and hygiene. Podiacyn is available through Amazon.com, our online store, and third-party distributors.

Animal Health Care

MicrocynAH[®] is an HOCl-based topical product that cleans, debrides and treats a wide spectrum of animal wounds and infections. It is intended for the safe and rapid treatment of a variety of animal afflictions including cuts, burns, lacerations, rashes, hot spots, rain rot, post-surgical sites, pink eye symptoms and wounds to the outer ear.

For our animal health products sold in the U.S. and Canada, we partner with Manna Pro Products, LLC. Manna Pro distributes non-prescription products to national pet-store retail chains and farm animal specialty stores such as Chewy.com, PetSmart, Tractor Supply, Cabela's, PetExpress, and Bass Pro Shops. In August 2022, we announced the launch of a MicrocynVS[®] line of products exclusively for veterinarians for the management of wound, skin, ear and eye afflictions in all animal species.

For the Asian and European markets, on May 20, 2019, we partnered with Petagon, Limited, an international importer and distributor of quality pet food and products for an initial term of five years. We supply Petagon with all MicrocynAH products sold by Petagon. On August 3, 2020, Petagon received a license from the People's Republic of China for the import of veterinary drug products manufactured by us. This is the highest classification Petagon and Sonoma can receive for animal health products in China.

Surface Disinfectants

Our HOCl technology has been formulated as a disinfectant and sanitizer solution for our partner MicroSafe and is sold in numerous countries. It is designed to be used to spray in aerosol format in areas and environments likely to serve as a breeding ground for the spread of infectious disease, which could result in epidemics or pandemics. The medical-grade surface disinfectant solution is used in hospitals worldwide to protect doctors and patients. In May 2020, Nanocyn[®] Disinfectant & Sanitizer received approval to be entered into the Australian Register of Therapeutic Goods, or ARTG for use against the coronavirus SARS-CoV-2, or COVID-19, and was also authorized in Canada for use against COVID-19. Nanocyn has also met the stringent environmental health and social/ethical criteria of Good Environmental Choice Australia, or GECA, becoming one of the very few eco-certified, all-natural disinfectant solutions in Australia.

Through our partner MicroSafe, we sell hard surface disinfectant products into Europe, the Middle East and Australia.

On July 31, 2021, we granted MicroSafe the non-exclusive right to sell and distribute Nanocyn in the United States provided that MicroSafe secure U.S. EPA approval. In April of 2022, MicroSafe secured the EPA approval for Nanocyn[®] Disinfectant & Sanitizer, meaning that it can now be sold in the United States as a surface disinfectant. Nanocyn was subsequently added to the EPA's list N for use against COVID-19. In June 2022, the EPA added Nanocyn to List Q as a disinfectant for Emerging Viral Pathogens, including Ebola virus, Mpox, and SARS-CoV-2, and in March 2023 the EPA added Nanocyn to Lists G and H, for use against Methicillin Resistant Staphylococcus Aureus (MRSA), Salmonella, Norovirus, Poliovirus, and as a fungicide. Nanocyn also received the Green Seal[®] Certification after surpassing a series of rigorous standards that measure environmental health, sustainability and product performance. Nanocyn is currently sold by MicroSafe in Europe, the Middle East and Australia.

Additional Information

Investors and others should note that we announce material financial information using our company website (www.sonomapharma.com), our investor relations website (ir.sonomapharma.com), SEC filings, press releases, public conference calls and webcasts. The information on, or accessible through, our websites is not incorporated by reference in this Quarterly Report on Form 10-Q.

Results of Continuing Operations

Comparison of the Three and Six Months Ended September 30, 2023 and 2022

Revenue

The following table shows our consolidated total revenue and revenue by geographic region for the three and six months ended September 30, 2023 and 2022:

	Three Months Ended September 30,		\$ Change	% Change
	2023	2022		
<i>(In thousands)</i>				
United States	\$ 590	\$ 973	\$ (383)	(39%)
Europe	1,201	1,170	31	3%
Asia	346	518	(172)	(33%)
Latin America	260	394	(134)	(34%)
Rest of the World	334	276	58	21%
Total	<u>\$ 2,731</u>	<u>\$ 3,331</u>	<u>\$ (600)</u>	<u>(18%)</u>
	Six Months Ended September 30,		\$ Change	% Change
	2023	2022		
<i>(In thousands)</i>				
United States	\$ 1,396	\$ 1,842	\$ (446)	(24%)
Europe	2,271	2,012	259	13%
Asia	1,208	1,438	(230)	(16%)
Latin America	747	1,444	(697)	(48%)
Rest of the World	536	578	(42)	(7%)
Total	<u>\$ 6,158</u>	<u>\$ 7,314</u>	<u>\$ (1,156)</u>	<u>(16%)</u>

The decrease in United States revenue for the three and six months ended September 30, 2023 of \$383,000 and \$446,000, respectively, was primarily the result of a decline in over-the-counter animal health care sales.

The increase in Europe revenue for the three and six months ended September 30, 2023 of \$31,000 and \$259,000, respectively was the result of increased demand for our products.

The decrease in Asia revenue for the three and six months ended September 30, 2023 of \$172,000 and \$230,000, respectively, was due to timing of orders. Revenues from our international distributors tend to fluctuate from period to period due to customer placement of larger but less frequent orders to benefit from quantity discounts and reduced shipping costs.

The decrease in Latin America revenue for the three months ended September 30, 2023 of \$134,000 was primarily the result of the timing of orders from our partner in Mexico. The decrease in Latin America revenue for the six months ended September 30, 2023 of \$697,000 was primarily due to service revenue recorded from selling machinery to a customer for \$750,000 in the prior period. Management expects this to be a one-time event.

The decrease in Rest of World revenue for the three and six months ended September 30, 2023 of \$58,000 and \$42,000, respectively, was primarily due to timing of customer orders.

Cost of Revenue and Gross Profit

The cost of revenue and gross profit metrics for the three and six months ended September 30, 2023 and 2022 are as follows:

	Three Months Ended September 30,		Change	% Change
	2023	2022		
<i>(In thousands, except for percentages)</i>				
Cost of Revenues	\$ 1,741	\$ 1,795	\$ (54)	(3)%
Cost of Revenue as a % of Revenues	64%	54%		
Gross Profit	\$ 990	\$ 1,536	\$ (546)	(36)%
Gross Profit as a % of Revenues	36%	46%		

	Six Months Ended September 30,		Change	% Change
	2023	2022		
<i>(In thousands, except for percentages)</i>				
Cost of Revenues	\$ 3,964	\$ 4,132	\$ (168)	(4)%
Cost of Revenue as a % of Revenues	64%	56%		
Gross Profit	\$ 2,194	\$ 3,182	\$ (988)	(31)%
Gross Profit as a % of Revenues	36%	44%		

The decrease in gross profit margin of \$546,000 for the three months ended September 30, 2023 as compared to the prior period, was primarily due to a decrease in revenue in the current period when compared to the prior year period.

The decrease in gross profit margin of \$988,000 for the six months ended September 30, 2023, as compared to the prior period, was primarily due to service revenue recorded from selling machinery to a customer for \$750,000 in the prior period, which management expects to be a one-time event.

Research and Development Expense

The research and development expense metrics as of September 30, 2023 and 2022 are as follows:

	Three Months Ended September 30,		Change	% Change
	2023	2022		
(In thousands, except for percentages)				
Research and Development Expense	\$ 536	\$ 200	336	168%
Research and Development Expense as a % of Revenues	20%	6%		

	Six Months Ended September 30,		Change	% Change
	2023	2022		
(In thousands, except for percentages)				
Research and Development Expense	\$ 861	\$ 406	455	112%
Research and Development Expense as a % of Revenues	14%	6%		

Increases in research and development expenses for the three and six months ended September 30, 2023 of \$336,000 and \$455,000, respectively, were due to increased product development and regulatory efforts.

Selling, General and Administrative Expense

The selling, general and administrative expense metrics are as follows:

	Three Months Ended September 30,		Change	% Change
	2023	2022		
(In thousands, except for percentages)				
Selling, General and Administrative Expense	\$ 1,662	\$ 2,067	\$ (405)	(20)%
Selling, General and Administrative Expense as a % of Revenues	61%	62%		

	Six Months Ended September 30,		Change	% Change
	2023	2022		
(In thousands, except for percentages)				
Selling, General and Administrative Expense	\$ 3,781	\$ 4,362	\$ (581)	(13)%
Selling, General and Administrative Expense as a % of Revenues	61%	60%		

The decline in selling, general and administrative expense for the three and six months ended September 30, 2023 of \$405,000 and \$581,000, respectively, was the result of ongoing efforts to contain expenses across all parts of the company.

Other Expense, net

Other expense, net for the three and six months ended September 30, 2023 was \$90,000 and \$301,000, respectively, compared to \$186,000 and \$253,000, respectively, for the three and six months ended September 30, 2022. The changes in in other expense, net primarily relates to exchange rate fluctuations.

Income tax expense

Income tax expense for the three and six months ended September 30, 2023 was \$186,000 and \$153,000, respectively. Income tax expense for the three and six months ended September 30, 2022 was \$100,000 and \$65,000, respectively.

Net Loss

The following table provides the net loss for each period along with the computation of basic and diluted net loss per share:

(In thousands, except per share data)	Three Months Ended September 30,		Six Months Ended September 30,	
	2023	2022	2023	2022
Numerator:				
Net loss	\$ (1,484)	\$ (1,017)	\$ (2,902)	\$ (1,904)
Denominator:				
Weighted-average number of common shares outstanding: basic and diluted	5,164	3,101	5,051	3,101
Net loss per share: basic and diluted	\$ (0.29)	\$ (0.33)	\$ (0.57)	\$ (0.61)

Liquidity and Capital Resources

We reported a net loss of \$1,484,000 and \$1,017,000 for the three months ended September 30, 2023 and 2022, respectively, and \$2,902,000 and \$1,904,000 for the six months ended September 30, 2023 and 2022, respectively. At September 30, 2023 and March 31, 2023, our accumulated deficit amounted to \$192,416,000 and \$189,514,000, respectively. As of September 30, 2023, we had cash and cash equivalents of \$2,137,000 compared to \$3,351,000 on September 30, 2022. Since our inception, substantially all of our operations have been financed through sales of equity securities. Other sources of financing that we have used to date include our revenues, royalty payments from licensing our products, as well as various loans and the sale of certain assets to Invektra, Petagon, and Microsafe.

On October 26, 2023, we entered into a placement agency agreement with Maxim Group LLC ("Maxim"), pursuant to which Maxim agreed to use its reasonable best efforts to solicit offers to purchase up to an aggregate of 8,500,000 shares of our common stock, par value \$0.0001 per share. We agreed to pay Maxim a cash fee equal to 8.0% of the gross proceeds from the offering, plus reimbursement of up to \$75,000 of legal fees and other expenses. Additionally, on October 26, 2023, we entered into a securities purchase agreement with the purchasers party thereto for the sale and issuance of an aggregate of up to 8,500,000 shares of our common stock at a public offering price of \$0.20 per share.

The closing of the offering occurred on October 30, 2023. In connection with the offering, we sold 8,500,000 shares of the our common stock for aggregate gross proceeds of \$1,700,000 and estimated net proceeds of \$1,414,000, after deducting placement agent fees and other estimated offering expenses.

The following table presents a summary of our consolidated cash flows for operating, investing and financing activities for the six months ended September 30, 2023 and 2022, as well as balances of cash and cash equivalents and working capital:

(In thousands)	Six Months Ended September 30,	
	2023	2022
Net cash used in:		
Operating activities	\$ (1,446)	\$ (3,363)
Investing activities	(19)	(210)
Financing activities	(264)	(565)
Effect of exchange rates on cash	46	93
Net change in cash and cash equivalents	(1,683)	(4,045)
Cash and cash equivalents, beginning of the period	3,820	7,396
Cash and cash equivalents, end of the period	\$ 2,137	\$ 3,351
Working capital ⁽¹⁾ , end of period	\$ 8,277	\$ 8,866

(1) Defined as current assets minus current liabilities

Net cash used in operating activities during the six months ended September 30, 2023 was \$1,446,000, primarily due to a net loss of \$2,902,000, offset by a decrease in accounts receivables of \$375,000, a decrease in inventory of \$403,000 and stock compensation of \$307,000.

Net cash used in operating activities during the six months ended September 30, 2022 was \$3,363,000, primarily due to a net loss of \$1,904,000, and a decrease in deferred revenue of \$1,149,000.

Net cash used by investing activities was \$19,000 for the six months ended September 30, 2023, primarily related to purchases of equipment.

Net cash used by investing activities was \$210,000 for the six months ended September 30, 2022, primarily related to long term deposits and purchases of equipment.

Net cash used by financing activities was \$264,000 for the six months ended September 30, 2023, primarily due to principal payments on short-term debt.

Net cash used by financing activities was \$565,000 for the six months ended September 30, 2022, primarily due to principal payments on short-term debt of \$460,000 and payments on PPP loan of \$120,000.

We expect revenues to fluctuate and may incur losses in the foreseeable future and may need to raise additional capital to pursue our product development initiatives, to penetrate markets for the sale of our products and continue as a going concern. We cannot provide any assurances that we will be able to raise additional capital.

Management believes that we have access to capital resources through possible public or private equity offerings, debt financings, corporate collaborations or other means; however, we cannot provide any assurance that new financing will be available on commercially acceptable terms, if at all. If the economic climate in the U.S. deteriorates, our ability to raise additional capital could be negatively impacted. If we are unable to secure additional capital, we may be required to take additional measures to reduce costs in order to conserve our cash in amounts sufficient to sustain operations and meet our obligations. These measures could cause significant delays in our continued efforts to commercialize our products, which is critical to the realization of our business plan and our future operations. These matters raise substantial doubt about our ability to continue as a going concern.

Material Trends and Uncertainties

We rely on certain key customers for a significant portion of our revenues. A small number of customers may represent a significant portion of our total revenues in any given period. These customers may not consistently purchase our products at a particular rate over any subsequent period.

We are exposed to risk from decline in foreign currency for both the Euro and the Mexico Peso versus the U.S. dollar. Most recently there has been a sharp decline in the Euro versus the U.S. dollar which has impacted our financial results.

As we have previously discussed in our annual report on Form 10-K filed with the SEC on June 21, 2023, we face a substantial Mexico tax liability, intercompany debt, unpaid technical assistance charges and accrued interest. These amounts are not due until 2027. At this time, management believes there are sufficient assets on the balance sheet to more than cover any tax obligation without interrupting our operations or business. We have engaged tax professionals to review all options to limit our exposure to these amounts and to proceed in a manner that is most advantageous to us.

The effects of the recent pandemic continue to impact economies worldwide, and we are closely watching inflation, increased volatility within financial markets, shipping costs, supply chain issues and labor costs. Any impact to our business operations, customer demand and supply chain due to increased shipping costs may ultimately impact sales. We continue to evaluate our end-to-end supply chain and assess opportunities to refine the impact on sales. Currently, most of our customers pay for shipping expenses, including increased shipping costs, if any. We have not yet faced labor shortages however it is possible we may have difficulties retaining and finding qualified employees in a tight labor market in the future. Furthermore, overall inflation tendencies may put pressure on our product pricing and/or costs.

We also closely monitor overall economic conditions, consumer sentiment and the prospect of a recession in the United States which may impact our financial results.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent liabilities at the dates of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates. Significant estimates and assumptions include reserves and write-downs related to receivables and inventories, the recoverability of long-lived assets, the valuation allowance related to our deferred tax assets, valuation of equity and derivative instruments, debt discounts, valuation of investments and the estimated amortization periods of upfront product licensing fees received from customers.

Off-Balance Sheet Transactions

We currently have no off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

As a smaller reporting company, we are electing scaled disclosure reporting obligations and therefore are not required to provide the information required by this Item.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

We carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of our most recent fiscal quarter. Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were not effective as of September 30, 2023.

Notwithstanding the material weaknesses reported in our 10-K, management believes the consolidated financial statements included in this Quarterly Report on Form 10-Q present fairly, in all material respects, our financial condition, results of operations and cash flows at and for the periods presented in accordance with U.S. generally accepted accounting principles.

Management's Remediation Measures

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in the Exchange Act Rule 13a-15(f) and 15d-15(f). Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in the *2013 Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation, our management concluded that our internal control over financial reporting was not effective as of September 30, 2023. We concluded this because of the errors we found in our Form 10-Q for the quarter ended June 30, 2020 that were restated in our Form 10-Q/A filed on November 17, 2020. We have determined that there were inadequate spreadsheet controls, a lack of separation of duties with preparation and review of the reported numbers, and inadequate analysis of revenue reporting among other things. We also determined during the quarter ended March 31, 2021 that there were errors related to income tax withholding accruals that required a revision in these financial statements. We believe we have taken steps to correct this, but the controls have not been tested and have not been working for a sufficient period of time to remove this weakness.

Management, with oversight from the Audit Committee of our Board of Directors, is actively engaged in remediation efforts to address the material weaknesses identified in the management's evaluation of internal controls and procedures. Management has taken a number of actions to remediate the material weaknesses described above, including the following:

- Improved monitoring and risk assessment activities to address these control deficiencies.
- Hired an interim Chief Financial Officer in April 2023 and a Controller in July 2023.
- Separated the preparation of the financial reports from review of the financial reports.
- Implemented additional process-level controls over revenue recognition of new contracts.
- Developed and delivered further internal controls training to individuals associated with these control deficiencies and enhanced training provided to all personnel who have financial reporting or internal control responsibilities in these areas. The training includes a review of individual roles and responsibilities related to internal controls, proper oversight and reemphasizes the importance of completing the control procedures.
- Did a detailed review of income taxes and our intercompany agreements which uncovered the fact that we should be accruing withholding taxes that will be paid to Mexico when intercompany interest and technical assistance payments are made to Mexico from the United States and that we will not be eligible for a tax credit in the United States because of our net operating loss positions.

These improvements are targeted at strengthening our internal control over financial reporting and remediating the material weaknesses. We remain committed to an effective internal control environment, and management believes that these actions and the improvements management expects to achieve as a result will effectively remediate the material weaknesses. However, the material weaknesses in our internal control over financial reporting will not be considered remediated until the controls operate for a sufficient period of time and management has concluded, through testing that these controls operate effectively. As of the date of filing this Quarterly Report on Form 10-Q, management is in the process of testing and evaluating these additional controls to determine whether they are operating effectively. We have hired appropriate accounting staff to establish effective internal controls and processes.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the three months ended September 30, 2023 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. We have not finished testing our controls and sufficient time has not elapsed to make the determination these controls are operating effectively.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

On occasion, we may be involved in legal matters arising in the ordinary course of our business including matters involving proprietary technology. While management believes that such matters are currently insignificant, matters arising in the ordinary course of business for which we are or could become involved in litigation may have a material adverse effect on our business, financial condition or results of comprehensive loss.

Item 1A. Risk Factors

Other than the risks set forth below, there have been no material changes from risk factors previously disclosed in our annual report on Form 10-K for the fiscal year ended March 31, 2023, as filed with the SEC June 21, 2023.

Our failure to maintain compliance with Nasdaq's continued listing requirements could result in the delisting of our common stock.

On September 22, 2023, we received a letter from The Nasdaq Stock Market LLC ("Nasdaq") indicating that we are not in compliance with Nasdaq Listing Rule 5550(a)(2), which requires companies listed on The Nasdaq Stock Market to maintain a minimum bid price of \$1 per share for continued listing. Nasdaq's letter has no immediate impact on the listing of our common stock, which will continue to be listed and traded on Nasdaq, subject to our compliance with the other continued listing requirements. Nasdaq has granted us a period of 180 calendar days, or until March 20, 2024, to regain compliance with the rule. We may regain compliance at any time during this compliance period if the minimum bid price for our common stock is at least \$1 for a minimum of ten consecutive business days.

Until Nasdaq has reached a final determination that we have regained compliance with all of the applicable continued listing requirements, there can be no assurances regarding the continued listing of our common stock or warrants on Nasdaq. The delisting of our common stock and warrants from Nasdaq would have a material adverse effect on our access to capital markets, and any limitation on market liquidity or reduction in the price of its common stock as a result of that delisting would adversely affect our ability to raise capital on terms acceptable to us, if at all.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

We did not issue any unregistered securities during the quarter ended September 30, 2023 and through November 9, 2023.

Item 3. Default Upon Senior Securities

We did not default upon any senior securities during the quarter ended September 30, 2023.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Exhibit Index

Exhibit No.	Description
3.1	<u>Restated Certificate of Incorporation of Oculus Innovative Sciences, Inc., effective January 30, 2006</u> (included as exhibit 3.1 of the Company's Annual Report on Form 10-K filed June 20, 2007, and incorporated herein by reference).
3.2	<u>Certificate of Amendment of Restated Certificate of Incorporation of Oculus Innovative Sciences, Inc., effective October 22, 2008</u> (included as exhibit A in the Company's Definitive Proxy Statement on Schedule 14A filed July 21, 2008, and incorporated herein by reference).
3.4	<u>Certificate of Amendment of Restated Certificate of Incorporation of Oculus Innovative Sciences, Inc., as amended, effective March 29, 2013</u> (included as exhibit 3.1 to the Company's Current Report on Form 8-K filed March 22, 2013, and incorporated herein by reference).
3.5	<u>Certificate of Amendment of Restated Certificate of Incorporation of Oculus Innovative Sciences, Inc., as amended, effective December 4, 2014</u> (included as exhibit 3.1 to the Company's Current Report on Form 8-K filed December 8, 2014, and incorporated herein by reference).
3.6	<u>Certificate of Amendment of Restated Certificate of Incorporation of Oculus Innovative Sciences, Inc., as amended, effective October 22, 2015</u> (included as exhibit 3.1 to the Company's Current Report on Form 8-K filed October 27, 2015, and incorporated herein by reference).
3.7	<u>Certificate of Amendment of Restated Certificate of Incorporation of Oculus Innovative Sciences, Inc., as amended, effective June 24, 2016</u> (included as exhibit 3.1 to the Company's Current Report on Form 8-K filed June 28, 2016, and incorporated herein by reference).
3.8	<u>Certificate of Amendment of Restated Certificate of Incorporation of Sonoma Pharmaceuticals, Inc., as amended, effective December 6, 2016</u> (included as exhibit 3.1 to the Company's Current Report on Form 8-K filed December 7, 2016, and incorporated herein by reference).
3.9	<u>Amended and Restated Bylaws, as amended, of Sonoma Pharmaceuticals, Inc., effective December 6, 2016</u> (included as exhibit 3.2 to the Company's Current Report on Form 8-K filed December 7, 2016, and incorporated herein by reference).
3.10	<u>Certificate of Designation of Preferences, Rights and Limitations of Series A 0% Convertible Preferred Stock, filed with the Delaware Secretary of State on April 24, 2012</u> (included as exhibit 4.2 to the Company's Current Report on Form 8-K, filed April 25, 2012, and incorporated herein by reference).
3.11	<u>Certificate of Designation of Series B Preferred Stock, effective October 18, 2016</u> (included as exhibit 3.1 to the Company's Current Report on Form 8-K filed October 21, 2016, and incorporated herein by references).
3.12	<u>Certificate of Amendment of Restated Certificate of Incorporation of Sonoma Pharmaceuticals, Inc., as amended, effective June 19, 2019</u> (included as exhibit 3.1 to the Company's Current Report on Form 8-K filed June 19, 2019, and incorporated herein by reference).
4.1	<u>Specimen Common Stock Certificate</u> (included as exhibit 4.1 to the Company's Annual Report on Form 10-K filed June 28, 2017, and incorporated herein by reference).
4.2	<u>Section 382 Rights Agreement, dated as of October 18, 2016, between Oculus Innovative Sciences, Inc. and Computershare Inc., which includes the Form of Certificate of Designation of Series B Preferred Stock as Exhibit A, the Form of Right Certificate as Exhibit B and the Summary of Rights to Purchase Preferred Stock as Exhibit C</u> (included as exhibit 4.1 to the Company's Current Report on Form 8-K filed October 21, 2016, and incorporated herein by reference).
4.3	<u>Form of Placement Agent Warrant granted to Dawson James Securities, Inc. and The Benchmark Company, LLC in connection with the March 2, 2018 public offering, dated March 6, 2018</u> (included as exhibit 4.1 to the Company's Current Report on Form 8-K filed March 6, 2018, and incorporated herein by reference).
4.4	<u>Form of Placement Agent Warrant granted to Dawson James Securities, Inc. in connection with the November 2019 public offering</u> (included as exhibit 4.1 to the Company's Current Report on Form 8-K filed on November 29, 2019, and incorporated herein by reference).

- 10.1 [Form of Indemnification Agreement between Oculus Innovative Sciences, Inc. and its officers and directors](#) (included as exhibit 10.1 to the Company's Registration Statement on Form S-1 (File No. 333-135584), as amended, declared effective on January 24, 2007, and incorporated herein by reference).
- 10.2 [Office Lease Agreement, dated May 18, 2006, between Oculus Technologies of Mexico, S.A. de C.V. and Antonio Sergio Arturo Fernandez Valenzuela](#) (translated from Spanish) (included as exhibit 10.10 to the Company's Registration Statement on Form S-1 (File No. 333-135584), as amended, declared effective on January 24, 2007, and incorporated herein by reference).
- 10.3 [Office Lease Agreement, dated July 2003, between Oculus Innovative Sciences, B.V. and Artikona Holding B.V. \(translated from Dutch\)](#) (included as exhibit 10.11 to the Company's Registration Statement on Form S-1 (File No. 333-135584), as amended, declared effective on January 24, 2007, and incorporated herein by reference).
- 10.4 [Form of Director Agreement](#) (included as exhibit 10.20 to the Company's Registration Statement on Form S-1 (File No. 333-135584), as amended, declared effective on January 24, 2007, and incorporated herein by reference).
- 10.5 [Amended and Restated Oculus Innovative Sciences, Inc. 2006 Stock Incentive Plan and related form stock option plan agreements](#) (included as exhibit 10.2 to the Company's Current Report on Form 8-K filed May 2, 2007, and incorporated herein by reference).
- 10.6 [Amendment to Office Lease Agreement, effective February 15, 2008, by and between Oculus Innovative Sciences Netherlands B.V. and Artikona Holding B.V. \(translated from Dutch\)](#) (included as exhibit 10.44 to the Company's Annual Report on Form 10-K filed June 13, 2008, and incorporated herein by reference).
- 10.7 [Oculus Innovative Sciences, Inc. 2011 Stock Incentive Plan](#) (included as exhibit A in the Company's Definitive Proxy Statement on Schedule 14A filed July 29, 2011, and incorporated herein by reference).
- 10.8† [Exclusive Sales and Distribution Agreement, dated November 6, 2015, by and between Oculus Innovative Sciences, Inc. and Manna Pro Products, LLC](#) (included as exhibit 10.1 to the Company's 8-K filed March 23, 2016 and incorporated herein by reference).
- 10.9† [Asset Purchase Agreement dated October 27, 2016, between Oculus Innovative Sciences, Inc. and Invektra, S.A.P.I de C.V.](#) (included as Exhibit 10.1 to the Company's Current Report on Form 8-K filed October 31, 2016, and incorporated herein by reference).
- 10.10† [Amendment Agreement to Acquisition Option dated October 27, 2016, by and between More Pharma Corporation S. de R.L. de C.V. and Oculus Technologies of Mexico, S.A. de C.V.](#) (included as Exhibit 10.2 to the Company's Current Report on Form 8-K filed October 31, 2016, and incorporated herein by reference).
- 10.11 [2016 Equity Incentive Plan](#) (included as exhibit A in the Company's Definitive Proxy Statement on Schedule 14A filed July 29, 2016, and incorporated herein by reference).
- 10.12 [Securities Purchase Agreement entered into by and between Sonoma Pharmaceuticals, Inc. and Montreux Equity Partners V, L.P., dated March 1, 2018](#) (included as exhibit 10.2 to the Company's Current Report on Form 8-K filed on March 6, 2018, and incorporated herein by reference).
- 10.13† [Exclusive License and Distribution Agreement entered into by and between Sonoma Pharmaceuticals, Inc. and EMS S.A., dated June 4, 2018](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on June 5, 2018, and incorporated herein by reference).
- 10.14 [Warrant Agency Agreement entered into by and among Sonoma Pharmaceuticals, Inc., Computershare, Inc. and Computershare Trust Company, N.A., dated November 21, 2018](#) (included as exhibit 10.2 to the Company's Current Report on Form 8-K filed on November 21, 2018, and incorporated herein by reference).
- 10.15+ [Asset Purchase Agreement dated May 14, 2019, between Sonoma Pharmaceuticals, Inc. and Petagon, Ltd.](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on May 22, 2019, and incorporated herein by reference).
- 10.16+ [Asset Purchase Agreement dated February 21, 2020, between Sonoma Pharmaceuticals, Inc. and MicroSafe Group, DMCC](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on February 27, 2020, and incorporated herein by reference).
- 10.17+ [License, Distribution and Supply Agreement by and between Sonoma Pharmaceuticals, Inc. and Brill International, S.L. dated May 19, 2020](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on May 26, 2020, and incorporated herein by reference).
- 10.18 [Consulting Agreement between the Company and Dr. Robert Northey, dated May 30, 2020.](#) (included as exhibit 10.2 to the Company's Current Report on Form 8-K filed on June 4, 2020, and incorporated herein by reference.)
- 10.19+ [Asset Purchase Agreement between the Company and Infinity Labs SD, Inc., dated June 24, 2020](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on June 30, 2020, and incorporated herein by reference.)

- 10.20* [Boulder Lease Agreement between the Company and Westland Development Services, Inc., dated February 19, 2021.](#)
- 10.21+ [Licensing Agreement between Sonoma Pharmaceuticals, Inc. and MicroSafe Group, effective July 27, 2020](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on August 6, 2020, and incorporated herein by reference).
- 10.22+ [Licensing and Distribution Agreement between Sonoma Pharmaceuticals, Inc. and Gabriel Science, LLC, effective December 14, 2020](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on December 17, 2020, and incorporated herein by reference).
- 10.23+ [Exclusive Supply and Distribution Agreement between the Company and EMC Pharma, LLC, dated March 26, 2021](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on March 31, 2021, and incorporated herein by reference).
- 10.24 [Amended and Restated Employment Agreement by and between the Company and Amy Trombly, dated June 16, 2023](#) (included as exhibit 10.38 to the Company's Current Report on Form 10-K filed on June 21, 2023, and incorporated herein by reference).
- 10.25 [Amended and Restated Employment Agreement by and between the Company and Bruce Thornton, dated June 16, 2023](#) (included as exhibit 10.39 to the Company's Current Report on Form 8-K filed on June 21, 2023, and incorporated herein by reference).
- 10.26 [At-The-Market Offering Agreement, by and between the Company and H.C. Wainwright & Co., LLC, dated July 30, 2021](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on July 30, 2021, and incorporated herein by reference).
- 10.27 [2021 Equity Incentive Plan](#) (included as appendix on the Company's proxy statement filed on July 29, 2021 and incorporated herein by reference).
- 10.28+4 [Exclusive License and Distribution Agreement between the Company and Dyamed Biotech Pte Ltd., dated November 4, 2021](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on November 9, 2021, and incorporated herein by reference).
- 10.29+4 [Non-Exclusive Distribution and Supply Agreement between the Company and Salus Medical, LLC dated January 19, 2022](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on January 20, 2022, and incorporated herein by reference).
- 10.30+4 [Exclusive License and Distribution Agreement between Sonoma Pharmaceuticals, Inc. and Anlicare International dated January 18, 2022](#) (included as exhibit 10.2 to the Company's Current Report on Form 8-K filed on January 20, 2022, and incorporated herein by reference).
- 10.31 [At-The-Market Offering Agreement, by and between the Company and Ladenburg Thalmann & Co. Inc., dated December 23, 2022](#) (included as exhibit 1.1 to the Company's Current Report on Form 8-K filed on December 23, 2022, and incorporated herein by reference).
- 10.32 [Sonoma Pharmaceuticals, Inc. Non-Employee Director Compensation Program and Stock Ownership Guidelines, revised by the Board of Directors on December 29, 2022](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on December 30, 2022, and incorporated herein by reference).
- 10.33+4 [Exclusive Distribution and Supply Agreement, dated January 26, 2023, by and between Sonoma Pharmaceuticals, Inc. and Daewoong Pharmaceutical Co., Ltd.](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on January 31, 2023, and incorporated herein by reference).
- 10.34 [Amendment to At-The-Market Offering Agreement, by and between the Company and Ladenburg Thalmann & Co. Inc., dated February 24, 2023](#) (included as exhibit 1.1 to the Company's Current Report on Form 8-K filed on February 24, 2023, and incorporated herein by reference).
- 10.35 [Consulting Agreement, by and between the Company and Jerome Dvorch, dated April 7, 2023](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on April 13, 2023, and incorporated herein by reference).
- 10.36 [Offer letter to John Dal Poggetto dated July 11, 2023](#) (included as exhibit 10.1 to the Company's Current Report on Form 8-K filed on July 14, 2023, and incorporated herein by reference).
- 10.37 [Consulting Agreement, by and between the Company and Jerome Dvorch Consulting, LLC, effective August 15, 2023](#) (included as exhibit 10.2 to the Company's Current Report on Form 8-K filed on July 14, 2023, and incorporated herein by reference).
- 10.38* [First Amendment to the Lease between the Company and Westland Development Services, Inc., dated June 21, 2023.](#)

14.1	Code of Business Conduct (included as Exhibit 14.1 to the Company's Current Report on Form 8-K filed on January 23, 2017, and incorporated herein by reference).
21.1	List of Subsidiaries (included as Exhibit 21.1 to the Company's Annual Report on Form 10-K on June 28, 2017, and incorporated herein by reference).
31.1*	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of Officers pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	Inline XBRL Instance Document (the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document)
101.SCH	Inline XBRL Taxonomy Extension Schema Document
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document
104	Cover Page Interactive Data File (formatted in inline XBRL, and included in exhibit 101).

* Filed herewith.

† Confidential treatment has been granted with respect to certain portions of this agreement.

‡ Certain portions of the exhibit have been omitted to preserve the confidentiality of such information. The Company will furnish copies of any such information to the SEC upon request.

+ The schedules to the exhibit have been omitted from this filing pursuant to Item 601(a)(5) of Regulation S-K. The Company will furnish copies of any such schedules to the SEC upon request.

Copies of above exhibits not contained herein are available to any stockholder, upon payment of a reasonable per page fee, upon written request to: Chief Financial Officer, Sonoma Pharmaceuticals, Inc., 5445 Conestoga Court, Suite 150, Boulder, Colorado 80301.

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.

Date: November 13, 2023

By: /s/ Amy Trombly
Amy Trombly
President and Chief Executive Officer, (Principal Executive Officer)

Date: November 13, 2023

/s/ Jerome Dvonch
Jerome Dvonch
Interim Chief Financial Officer
(Principal Financial and
Principal Accounting Officer)

LEASE AGREEMENT

BY AND BETWEEN

WESTLAND DEVELOPMENT SERVICES, INC.

("Landlord")

AND

("Tenant")

SONOMA PHARMACEUTICALS, INC.

THIS LEASE AGREEMENT ("Lease") is made effective as of February 19, 2021, by and between WESTLAND DEVELOPMENT SERVICES, INC., A COLORADO CORPORATION ("Landlord"), and Sonoma Pharmaceuticals, Inc. , A Delaware Corporation ("Tenant"). For valuable consideration, the Landlord and Tenant agree as follows:

1. PREMISES.

- 1.1. **PREMISES.** Subject to the terms and conditions of this Lease, Landlord hereby leases and delivers unto Tenant, and Tenant hereby leases and accepts from Landlord, the following space located in that certain commercial building at 5445 Conestoga Court, Boulder, Colorado 80301 ("Building"), consisting of approximately 2,766 rentable square feet ("Rentable Square Feet") in Unit No 150 and generally depicted in attached EXHIBIT A ("Premises"). Tenant acknowledges and agrees that the Rentable Square Feet of the Premises is a reasonable, good faith approximation that shall be deemed conclusive and binding on Landlord and Tenant during the Term (defined below) of this Lease.
- 1.2. **COMMON AREAS.** In addition to the Premises, Landlord hereby grants to Tenant a non- exclusive right and license to use, in common with other tenants of the Building, the various appurtenant public and/or common areas of the Building that are generally available for use by all tenants ("Common Areas"). Such Common Areas include all portions of the Building intended for shared use in common with others, including outdoor parking areas, driveways, truck and delivery areas, loading zones, landscaped areas, entryways and exits, exterior lighting, sidewalks and ramps, interior hallways, stairs, elevators, restrooms and lobby areas, and all other common elements of the Building, including utility systems and equipment serving the Building.

2. LANDLORD IMPROVEMENTS.

- 2.1. Commencing upon and subject to all terms and conditions of this Lease, Landlord, at its expense, shall cause all posters and art to be removed and the holes patched and painted so that the walls look clean and professional in the reasonable view of the Tenant, the boarded up area will be completed and the existing wood matched as best as possible so that it is reasonably acceptable to Tenant, and the Premises to be professionally cleaned and sanitized pursuant to national Covid standards. If Tenant would like to keep the fridge it will need to be purchased from Chef Ann/Boulder County Farmer's Market. The other appliances will be provided with the lease.

3. TERM.

- 3.1. **COMMENCEMENT AND TERM.** The terms and provisions of this Lease shall commence and be in full force and effect upon the Parties' execution of this Lease. As of March 1, 2021 the Initial Term of this Lease shall commence ("Commencement Date"). Such Initial Term shall commence on the Commencement Date and continue for thirty-six (36) calendar months thereafter ("Term" or "Initial Term"), unless earlier terminated according to other provisions of this Lease. The Tenant's obligation to pay Base Rent and Operating Expenses (defined in Section 4 below) shall begin on the Commencement Date and end on January 31, 2024.
- 3.1(a) **HOLDING OVER.** In the event Tenant remains in possession of all or any part of the Premises after the Expiration Date without a Renewal Term Amendment, then Tenant's occupancy of the Premises shall be deemed a month-to-month tenancy at sufferance, subject to all terms and conditions of this Lease; except that Base Rent payable during such month- to-month tenancy shall be one hundred fifty percent (150%) of the Base Rent due and payable immediately prior to the Expiration Date. Such month-to-month tenancy may be terminated by either Party upon delivery of twenty-one (21) calendar days written notice. Notwithstanding anything to the contrary set forth herein, any holdover without Landlord's consent shall be deemed an Event of Default entitling Landlord to exercise all rights and remedies set forth in Section 16 below.

4. RENT.

4.1. **BASE RENT.** During the first twelve (12) months of the Initial Term, Tenant shall pay to Landlord base annual rent for the Premises ("*Base Rent*") as follows:

4.1(a) Three thousand five hundred seventy two and 75/100 dollars (\$3,572.75) per month from February 15, 2021 to January 31, 2022;

4.1(b) Three thousand six hundred seventy nine and 93/100 dollars (\$3,679.93) per month from February 1, 2022 to January 31, 2023;

4.1(c) Three thousand seven hundred ninety and 33/100 dollars (\$3,790.33) per month from February 1, 2023 to January 31, 2024;

4.2. PAYMENT OF RENT.

4.2(a) Base Rent Installments are due and payable in good and immediately available funds in advance, without notice or demand and without any set-off or deduction, on the first (1st) business day of each calendar month during the Term; provided, however, that the Base Rent and operating expenses Installment pro rated for the first (1st) calendar month of this Lease in the amount of Five thousand two hundred and 8/100 (\$5,200.08) shall be due and payable upon lease execution.

4.2(b) In the event Landlord does not receive a Base Rent Installment or an Operating Expenses Installment (defined below) by the close of the third (3rd) business day in any calendar month, Tenant shall pay a late fee equal to five percent (5%) of the aggregate amount past due. Tenant shall pay such late fee immediately or Landlord may withdraw and apply the same from Tenant's Security Deposit (defined below). In the event of any returned check for insufficient funds, or any check that is not otherwise paid upon presentment, Tenant shall pay a returned check fee of \$25.00 in addition to any bank fee or charge incurred for any returned check. Tenant acknowledges that such late fees and returned check charges are not unreasonable.

4.2(c) Tenant's obligation to pay Base Rent Installments and Operating Expenses Installments are separate and distinct independent covenants and agreements, and such obligations are separate from and in addition to Tenant's other obligations under this Lease.

5. OPERATING EXPENSES.

5.1. **TENANT'S PRO RATA SHARE.** In addition to Base Rent, Tenant shall also pay to Landlord, without any set-off or deduction, Tenant's Pro Rata Share of Operating Expenses applicable to Landlord's operation and management of the Building and Common Areas. For purposes of this Lease, "*Tenant's Pro Rata Share*" shall be equal to the fraction, the numerator of which shall equal the Rentable Square Feet of the Premises, and the denominator of which shall equal the aggregate rentable square feet of all units in the Building. As of the date hereof, Tenant's Pro Rata Share is equal to 14.91%. For the calendar year 2020, Operating Expenses for the Building are estimated to be approximately \$7.06 per square foot annually, but that is only an estimate. The 2021 estimate will be provided by April 1, 2021.

5.2. **OPERATING EXPENSES.** For purposes of this Lease, “*Operating Expenses*” shall mean and include all costs and expenses incurred by Landlord in the course of owning, operating, managing, maintaining, repairing and insuring the Building and Common Areas, including:

- 5.2(a) real property taxes and assessments levied against the Building or Common Areas by any governmental authority having jurisdiction, including any tax, assessment, surcharge, or levy presently in effect or hereafter levied on the use, occupancy, improvement, ownership or operation of the Building or Common Areas (“*Real Estate Taxes*”) including any expense in retaining tax consultants to contest the amount or validity of any such Real Estate Taxes;
- 5.2(b) expenses incurred by Landlord in connection with operating, maintaining and repairing the Building and Common Areas, including maintenance, repair, replacement and operation of: (i) mechanical, electrical, plumbing, sewer, HVAC, life safety, hydraulic, security, and related systems and appurtenances serving the Building or Common Areas; (ii) parking areas, sidewalks, paved surfaces, landscaped areas, exterior and roof of the Building; (iii) lighting including the cost of replacement bulbs, ballasts and fixtures; (iv) carpet, painting, cleaning and upkeep of Common Areas; (v) janitorial service, window cleaning, snow removal and landscape maintenance, trash removal and recycling; and (vi) labor, equipment, services and materials used in connection with the foregoing;
- 5.2(c) expenses incurred in connection with the supply of energy and utilities for the Building and Common Areas, including natural gas, electricity, solar, other energy source, water, sanitary sewer and storm drainage services for the Building and Common Areas;
- 5.2(d) Landlord’s insurance premiums, including property damage, liability, fire and all-risk or multi-peril coverage, and loss of rent; the part of any claim required to be paid under the deductible portion of any insurance policy carried by Landlord for the Building; public liability and any other insurance carried by Landlord on the Building or as may be required by any mortgagee of the Building;
- 5.2(e) property and Building management fees currently equal to five percent (5%) of the aggregate gross rent payable under all leases related to the Building;
- 5.2(f) reasonable legal, accounting, inspection, and other professional fees (including fees for services intended to produce a reduction in Operating Expenses or to improve the efficient operation, maintenance or state of repair of the Building);
- 5.2(g) expenses of capital improvements including structural repairs and replacements made in or to the Building, in order to conform to changes (subsequent to the date of issuance of the certificate of occupancy for the Building) in any applicable laws, ordinances, rules, regulations, or orders of any governmental authority having jurisdiction over the Building (“*Required Capital Improvements*”), and the costs of any capital improvements and structural repairs and replacements that reduce Operating Expenses (“*Cost Savings Improvements*”); provided that, any expenditures for Required Capital Improvements and/or Cost Savings Improvements shall be amortized at a market rate of return over the useful life of such improvement, repair or replacement (determined by Landlord’s accountants); and further provided that the amortized amount of any Cost Savings Improvement in any calendar year will be roughly equal to the estimated reduction in Operating Expenses as a result thereof;
- 5.2(h) expenses incurred in connection with the design, installation, maintenance or repair of any monument signs or other signage for the Building.

5.2(i) “*Operating Expenses*” shall not include any of the following:

5.2(i)(i) expenses related to work that Landlord performs on behalf of other tenants for their respective units in the Building;

5.2(i)(ii) leasing commissions, advertising, and other expenses incurred with respect to leasing space in the Building;

5.2(i)(iii) expenses for repairs or other work occasioned by fire, windstorm or other insured casualty to the extent of insurance proceeds received;

5.2(i)(iv) costs of repairs or rebuilding necessitated by condemnation;

5.2(i)(v) costs or attorney’s fees incurred in connection with any dispute involving any other tenant or prospective tenant of the Building;

5.2(i)(vi) cost to repair any damage to the Building caused by Landlord;

5.2(i)(vii) fees or other compensation paid to any affiliate of Landlord for services for the Building, to the extent they exceed competitive costs for such services rendered by persons or entities of similar skill and experience who are not affiliates of Landlord;

5.2(i)(viii) other than as set forth in Section 4.2 above, the cost of structural repairs or reconstruction of any portion of the Building;

5.2(i)(ix) costs of providing utility service lines to the Building (standard core and shell) or repairing such lines if they break, other than due to acts or omissions of Tenant or its employees, agents, contractors or invitees;

5.2(i)(x) any interest on borrowed money or debt amortization, or costs incurred in connection with mortgage financing or refinancing of the Building, or incurred in connection with the sale of the Building or any change in the ownership of Landlord;

5.2(i)(xi) depreciation of the Building or any federal or state income tax on Landlord’s business.

5.2(j) **REIMBURSEMENT OF OPERATING EXPENSES.** Annually during the Term, at or around the end of the first calendar quarter of each year, Landlord shall prepare and deliver to Tenant written notice of any changes in Landlord’s budget for estimated Operating Expenses for the next calendar year, as determined by Landlord in good faith. Tenant shall pay Tenant’s Pro Rata Share of such estimated Operating Expenses in equal monthly installments in advance without notice or demand and without set-off or deduction (the “*Operating Expenses Installments*”), each of which shall be due and payable on the first (1st) business day of each calendar month during the Term together with Base Rent Installments.

5.2(k) RECONCILIATION OF OPERATING EXPENSES

5.2(k)(i) Annually during the Term, also around the end of the first calendar quarter of each year, Landlord shall deliver to Tenant a statement summarizing: (i) the actual Operating Expenses incurred for the preceding calendar year; (ii) Tenant's Pro Rata Share including the aggregate Operating Expense Installments actually paid by Tenant during such calendar year; and (iii) the amount of any difference between Tenant's Pro Rata Share of Operating Expenses and the aggregate Operating Expenses Installments actually paid by Tenant (the "*Reconciliation Statement*"). In the event that Tenant's Pro Rata Share of actual Operating Expenses exceeds the aggregate Operating Expenses Installments actually paid by Tenant, Tenant shall pay any shortfall within thirty (30) calendar days after the receipt of the Reconciliation Statement. In the event that Tenant's Pro Rata Share of actual Operating Expenses is less than the aggregate Operating Expenses Installments actually paid by Tenant, such overpayment shall either be: (x) applied by Landlord as a credit against Tenant's Base Rent Installments and/or Operating Expenses Installments, until fully applied; or (y) at Landlord's election, refunded to Tenant within thirty (30) calendar days after the date of the Reconciliation Statement.

5.2(k)(ii) Tenant shall have the right to review and verify the accuracy of the Reconciliation Statement, upon Tenant's delivery of written notice to Landlord within 30-days after the date of the Reconciliation Statement (the "*Operating Expenses Audit Notice*"). In the event Tenant does not deliver an Operating Expenses Audit Notice within such 30- day period, Tenant shall be deemed to have waived its right to review and verify the accuracy of the Reconciliation Statement, which shall thereupon be deemed final, binding and conclusive. If Tenant timely issues such notice, then Tenant shall engage its own certified public accountants ("*Tenant's Accountants*") to conduct such review of the Reconciliation Statement, to be completed at Landlord's offices within thirty (30) days after the date of the Operating Expenses Audit Notice. In the event Tenant's Accountants determine in good faith that an error or discrepancy occurred in the Reconciliation Statement, Tenant shall deliver written notice of the same to Landlord, and thereafter Landlord's Accountants and Tenant's Accountants shall cooperate in good faith to attempt to resolve any such discrepancy, failing which the parties may submit such matter to an independent certified public accountant to be mutually selected by Landlord's and Tenant's Accountants. The determination of such independent accountant shall be final, conclusive and binding upon the parties, and the amount of any shortfall or overpayment shall be resolved in accordance with the terms and conditions set forth in Section 4.4(a) above. Notwithstanding any ongoing review of a Reconciliation Statement, Tenant shall continue to pay Landlord the amount of the Operating Expenses Installments that accrue under this Lease in accordance with the terms and conditions of this Lease.

6. SECURITY DEPOSIT.

- 6.1. **AMOUNT OF SECURITY.** Landlord acknowledges receipt from Tenant of five thousand two hundred and no/100 dollars (\$5,200.00) ("*Security Deposit*") to be held by Landlord as collateral security, and not prepaid rent, for the full, faithful and timely performance by Tenant of all covenants, conditions and obligations in this Lease. Landlord may hold the Security Deposit in a separate deposit account, or may commingle the Security Deposit with Landlord's other funds, but shall have no obligation to pay or account for any interest. The amount of the Security Deposit, less any amounts withheld or deducted, shall be repaid without interest to Tenant within sixty (60) calendar days after expiration or termination of this Lease, provided that no uncured Event of Default has occurred hereunder and provided that Tenant returns the Premises in the reasonably good physical condition required by this Lease. Landlord may from time to time draw upon and apply all or part of the Security Deposit as may be necessary to compensate Landlord for any Event of Default hereunder, including without limitation, any damage to the Premises. If the Security Deposit is applied for such purposes during the Term, then Tenant, promptly upon Landlord's demand, shall pay to Landlord the amount required to restore the Security Deposit to its original amount. The Security Deposit shall not be deemed to be liquidated damages or a cap on damages related to any Event of Default.
- 6.2. **NO LIABILITY FOR SECURITY DEPOSIT UPON SALE.** In the event of a sale or transfer of Landlord's estate or interest in the Building, and upon the delivery of prior written notice to Tenant specifying the name, address and contact information for the purchaser or transferee, Landlord shall have the right to transfer the Security Deposit to such purchaser or transferee, and upon such transfer Landlord shall thereupon be released by Tenant from all liability for the return of the Security Deposit. No mortgagee or purchaser of the Building at any foreclosure proceeding shall be liable to Tenant for any or all of such Security Deposit unless Landlord has actually delivered the same in cash or by credit to such mortgagee or purchaser, and if Landlord has not actually delivered the same in cash or by credit, Landlord shall remain liable to Tenant for the Security Deposit.

7. USE OF PREMISES; HOURS.

- 7.1. **USE.** The Premises shall be used and occupied by Tenant for administrative office purposes and related uses associated with shipping and receiving of dermatology, wound care and other Rx and OTC products. No other or different use shall be made of the Premises without the prior written consent of Landlord. Notwithstanding anything to the contrary set forth herein, the Premises shall not be used: (a) for any illegal purpose, or in violation of any regulation of any governmental authority, or contrary to the regulations or directives of Landlord's insurance carriers; or (b) in any manner that interferes with the quiet enjoyment of the Building or Common Areas or any other tenant's use of the Building. Tenant shall not conduct, suffer or permit any unlawful activity, or place any equipment in or about the Premises or Common Areas that may in any way increase the rate or cause the cancellation of fire insurance or other insurance on the Building. If any use of the Building, Premises or Common Areas by Tenant causes any such increase, then the full amount of such increase shall be included in Tenant's Pro Rata Share of Operating Expenses.
- 7.2. **PROHIBITED USE.** Tenant may not conduct any of the following uses in the Premises or Building: N/A.
- 7.3. **BUILDING HOURS.** The Building hours of operation are 8:00 a.m. to 6:00 p.m. Monday through Friday and 8:00 a.m. to 1:00 p.m. on Saturdays, but not including customarily observed government and banking holidays such as New Year's Day, Fourth of July, Thanksgiving Day, Christmas Day, e.g., or such other holidays as may be customarily established and observed. These are the hours when property management services will be available.

8. MAINTENANCE OF PREMISES.

- 8.1. **TENANT'S OBLIGATIONS.** Tenant hereby accepts the Premises and all systems and equipment serving the Premises in their "as-is" condition and repair, and during the Term at Tenant's sole cost and expense shall maintain the Premises in good working order, repair and condition, and, upon the Expiration Date or the effective date of any earlier termination of this Lease, shall surrender and deliver the Premises and all keys, locks and other fixtures in as good order, repair and condition as the Premises were on the Commencement Date, ordinary wear and tear excepted. Except as set forth in Section 8.2 below, Tenant acknowledges that Landlord shall have no obligation to perform such maintenance or replacements or otherwise make any repairs in or to the Premises.
- 8.2. **LANDLORD'S OBLIGATIONS.** Notwithstanding anything to the contrary set forth in Section 7.1 above, Landlord shall at its expense maintain the structural components of the Building Core and Shell, and the Common Areas, in good working order, repair and condition during the Term.
- 8.3. **TENANT DAMAGE.** Tenant shall be solely responsible for the costs and expenses associated with any maintenance, repair or replacement of any damaged part, item or component of the Building or Common Areas resulting from the acts or omissions of Tenant, its employees, agents, representatives or invitees. Tenant shall reimburse Landlord for the costs and expenses incurred by Landlord in connection therewith within thirty (30) days after Tenant's receipt of Landlord's invoice for the same.

9. ALTERATIONS BY TENANT.

- 9.1. **LANDLORD CONSENT REQUIREMENT.** Other than the Tenant Improvements, Tenant shall not make or permit any other improvements, additions, alterations, substitutions, replacements or modifications, structural or otherwise, to the Premises or Building (collectively, "*Alterations*") without having first obtained the prior written consent of Landlord, which consent shall not be unreasonably withheld, conditioned or delayed; provided, however, that Landlord may withhold its consent to any Alterations that Landlord determines in good faith may: (a) adversely affect the structural integrity or safety of the Building; (b) adversely affect the electrical, plumbing, mechanical, sewer, HVAC, life safety or security systems of the Building; (c) be visible from the exterior of the Building or from any of the Common Areas; or (d) interfere with the operation of the Building or the provision of services or utilities to other tenants in the Building. Landlord may impose any reasonable conditions applicable to the Alterations it deems in good faith to be necessary, desirable or appropriate, including without limitation: (w) the approval of plans and specifications for the Alterations; (x) approval of contractors and subcontractors to perform work related thereto, including all insurance coverage carried by such contractors; (y) Landlord's review of the progress of work and satisfactory evidence of Tenant's ability to pay for such Alterations; and (z) the requirement that, prior to the Expiration Date or effective date of any earlier termination of this Lease, Tenant shall at its expense remove any Alterations and restore the Building or Premises as applicable. Tenant shall reimburse Landlord for any out-of-pocket expenses incurred in reviewing any requested consent to any proposed Alterations whether or not such consent is granted. Landlord shall have no liability related to any design, review, or performance of work, notwithstanding Landlord's consent or approval of plans, for any Alterations. Upon reasonable prior notice and at reasonable times, Landlord shall have the right to enter the Premises and inspect the construction of any Alterations in the Premises and shall have the right to post notices of Landlord's non-liability under applicable law, or to take any further action which the Landlord may deem to be proper for the protection of the Landlord's interest in the Building and Premises.
- 9.2. **CONSTRUCTION.** Alterations shall be constructed at Tenant's sole expense in accordance with the plans and specifications approved in advance by Landlord. Tenant shall obtain all necessary permits and approvals required for construction of any Alterations and shall deliver copies of the same to Landlord prior to commencement of any such construction. The Alterations shall comply with all applicable laws, building codes, fire codes, insurance requirements and the provisions of this Lease. If any mechanic's or materialman's lien is threatened or filed against the Premises or the Building in connection with the construction of Alterations, Tenant shall, at its sole cost and expense, promptly obtain the release and discharge of such lien by paying off or bonding over such lien.
- 9.3. **REMOVAL.** In the event any Alterations are constructed without the prior written consent of Landlord, Landlord may require Tenant to correct or remove such Alterations at Tenant's expense.
- 9.4. **TITLE.** All Alterations installed or located in the Premises shall immediately become the property of Landlord, and shall remain upon and be surrendered to Landlord with the Premises upon the Expiration Date or the effective date of any earlier termination of this Lease, unless Landlord instructs Tenant to remove such Alterations and restore the Building and Premises.

10. UTILITIES AND SERVICES.

- 10.1. **BUILDING STANDARD SERVICES.** The following Building-standard services and utilities are available to serve the Premises: (a) domestic water and sanitary sewer; (b) heated or cooled air (as applicable) and standard usage electrical current; (c) the use of passenger elevators during regular building hours, if installed in the Building (available except in case of emergency or repair); and (d) Common Area janitorial and general maintenance services. Tenant acknowledges that Landlord shall have no responsibility whatsoever to supply, install, maintain or pay for any other or additional service(s) or utilities including data cabling, telephone or fibre optic lines, or electronic, communication, or other utility service to the Premises.

- 10.2. **ADDITIONAL SERVICES.** In the event Tenant requires additional services, supply, or utilities for the Premises, in addition to Building-standard services, Tenant shall be responsible for and pay directly all costs and expenses related to extending, connecting, supplementing or otherwise upgrading existing Building-standard core and shell system(s), unless such costs and expenses are allowed to be paid from any TI Allowance. Tenant acknowledges and agrees that Landlord shall have no obligation to incur costs or expenses for additional services or to perform any work related to supplements of upgrades as part of Landlord's Work under this Lease.
- 10.3. **INTERRUPTION IN UTILITY SERVICE.** Unless solely attributable to or caused by Landlord's direct negligent act or omission, no interruption, curtailment, stoppage or suspension of Building utility service or system shall render Landlord liable in any respect for damages to person, property or business, nor shall the same be the basis for: (a) any abatement, reduction or rebate of Base Rent Installments or Operating Expenses Installments; (b) relieving Tenant from any of Tenant's obligations hereunder; or (c) for any claim that Landlord constructively evicted or otherwise disturbed or interfered with Tenant's use, possession or quiet enjoyment of the Premises. Notwithstanding the foregoing, Landlord shall upon receiving notice of any interruption exercise reasonable diligence to address and attempt to remedy any such interruption.
- 10.4. **PREMISES UTILITIES AND SERVICES.** Landlord shall bill tenant monthly for its pro rata share of utilities that are not separately metered including gas, electricity, water, wastewater, telephone, communications, internet services, trash removal, recycling, composting and janitorial services. The Premises shall be separately metered such that Tenant shall separately contract with applicable local public authorities, utilities, or third-party vendors, as the case may be, for the furnishing of and payment for all utilities including gas, electricity, water, wastewater, telephone, communications and internet services, and including trash removal, recycling, and janitorial services specific to the Premises. Tenant shall directly pay for such utilities and services, including the establishment and connection of any telecommunications or internet service, at the rates charged by such authority, utility or third-party vendor. The failure of Tenant to obtain or to continue to receive such utilities or services for any reason shall not relieve Tenant of any of its obligations under this Lease, unless such failure is solely the result of Landlord's direct negligent act or omission. Notwithstanding the foregoing, in the event Tenant fails to arrange for appropriate trash removal or janitorial services, or to maintain the Premises in good working order and condition, Landlord may contract for such services on Tenant's behalf and Tenant shall pay the cost thereof as part of Tenant's Pro Rata Share of Operating Expenses.
- 10.5. **NOTICE OF DEFECTS.** Tenant shall deliver to Landlord prompt notice of any damage, accident or defect in the Building of which Tenant becomes aware, including leaks or defects in pipes or plumbing, electrical wiring, HVAC equipment, and any matter or condition which may cause injury or damage to the Building or any person or property therein.

11. SIGNAGE.

- 11.1. **TENANT AND BUILDING SIGNAGE.** Tenant shall have the right to be listed on existing signage for the Building. Landlord and Tenant shall coordinate regarding the design and installation of Tenant's signage prior to installation of the same. Tenant's sign design shall be at Tenant's expense and comply with applicable local laws and ordinances. All signs shall be located in places approved by Landlord. The size and location of all Building signage must conform to all applicable laws and ordinances. Any and all permitted signs shall be installed and maintained by Tenant, at Tenant's sole expense.
- 11.2. **NO OTHER SIGNS.** No other sign, advertisement or notice shall be inscribed, painted, affixed or displayed on the windows or exterior walls of the Premises or on any public area of the Building, unless approved in advance by Landlord.

12. SUBLETTING OR TRANSFER.

- 12.1. **TRANSFER BY TENANT.** Tenant shall not, without the prior written consent of Landlord: (a) assign or otherwise transfer this Lease or any rights hereunder; (b) sublet the Premises or any part thereof, or permit the use of the Premises or any part thereof by any third party other than Tenant and its employees, agents and invitees; (c) mortgage or encumber this Lease; or (d) permit the assignment or other transfer of this Lease or any of Tenant's rights hereunder by operation of law (each, a "*Transfer by Tenant*"). For purposes of this Section 12 the merger or consolidation of Tenant into or with any other or different entity, or the sale of all or substantially all of Tenant's assets, or the dissolution or reorganization of Tenant, shall be a Transfer by Tenant. Any Transfer by Tenant that is not in conformance with the terms and conditions set forth in this Section 12 may be voided by Landlord and enforced as an Event of Default.
- 12.2. **LANDLORD CONSENT REQUIREMENT.** Tenant shall pay to Landlord an administrative fee in the amount of One Thousand Dollars (\$1,000.00) and shall reimburse Landlord's reasonable attorneys' fees and other out-of-pocket expenses incurred in reviewing any documents related to a proposed Transfer by Tenant, whether or not such consent is granted. In granting or withholding consent to any proposed Transfer by Tenant, Landlord shall act in good faith and be entitled to consider any factors, including: (a) the financial strength and creditworthiness of any proposed subtenant/assignee; (b) the proposed use of the Premises by any proposed subtenant/assignee; (c) the requirements of any lender of Landlord for the Building; and (d) the risk factors and/or commercial reasonableness of any proposed business terms.
- 12.3. **LANDLORD RIGHTS REGARDING SUBLEASES AND ASSIGNMENTS.**
- 12.3(a) In the event Tenant desires to sublet all or any portion of the Premises (the "*Proposed Sublet Space*"), Tenant shall provide written notice to Landlord and Landlord shall have the right to recover the Proposed Sublet Space and lease it directly to the proposed subtenant. In such event, the parties shall enter into an amendment to this Lease to reflect the reduction in the Rentable Square Feet, Base Rent, Operating Expenses and Tenant's Pro Rata Share.
- 12.3(b) In the event Tenant proposes to assign and transfer this Lease, Landlord shall have the right to terminate this Lease and lease the Premises directly to the proposed assignee.
- 12.3(c) Landlord's option to amend or terminate this Lease shall be exercisable by written notice to Tenant within thirty (30) days following Landlord's receipt of written notice that Tenant desires to assign this Lease or to sublease any specified Proposed Sublet Space. If Landlord exercises such rights, then such amendment or termination shall be effective as of the effective date of any Landlord-approved assignment or subletting. If Landlord does not exercise its right to recover possession of the Proposed Sublet Space or to terminate this Lease, then Tenant shall be entitled to seek an acceptable subtenant for the Proposed Sublet Space, for a sublease term no longer than that set forth in Tenant's notice.
- 12.3(d) Any proposed sublease shall be in a form acceptable to Landlord and shall incorporate all terms and conditions of this Lease. The consent by Landlord to any Transfer by Tenant shall not be construed as a waiver, release or discharge of Tenant from any obligation under this Lease, unless expressly agreed in writing by Landlord (it being understood that Tenant shall remain primarily liable as principal), nor shall the collection or acceptance of rent from any assignee, transferee, subtenant or occupant constitute waiver, release or discharge of Tenant. No consent by Landlord to any Transfer by Tenant in any one instance shall constitute a waiver of the need for Landlord's consent thereafter.
- 12.3(e) To the extent that Tenant receives any amount of rent, value, or other consideration for the Premises, under any Transfer by Tenant involving a sublease, assignment, or other arrangement involving any subtenant, licensee, transferee, or occupant, which exceeds the amount of Base Rent reserved in this Lease, then Tenant shall pay fifty percent (50%) of such amount to Landlord as Additional Rent, payable to Landlord at the same time and manner required for the payment of Base Rent.

13. INSURANCE.

13.1. **TENANT'S INSURANCE.** Tenant shall procure and maintain at its expense, at all times during the Term and any Renewal Term, the following minimum insurance coverage:

- 13.1(a) Commercial general liability insurance endorsing and naming Landlord as additional insured, against any and all claims for bodily injury and/or property damage occurring in or about the Premises arising during the Term of Tenant's use and occupancy of the Premises. Such insurance shall have combined single limit of not less than One Million Dollars (\$1,000,000) per occurrence and not less than Two Million Dollar (\$2,000,000) aggregate, and excess umbrella liability insurance of at least One Million Dollars (\$1,000,000). Such liability insurance shall be primary and not contributing to any other insurance and in no event shall the limits of such insurance be considered as limiting the liability of Tenant;
- 13.1(b) Personal property insurance insuring all of Tenant's equipment, trade fixtures, inventory, business personal property and other contents located in the Premises against all perils including special form (all risk) coverage. Such insurance shall be written on a replacement cost basis equal to one hundred percent (100%) of full insurable replacement value;
- 13.1(c) Workers' compensation insurance as required by Colorado law, and business interruption coverage if desired by Tenant;
- 13.1(d) Such other insurance as Landlord deems commercially reasonable and necessary, or as may be required by Landlord's beneficiaries or mortgagees under any deed of trust or mortgage encumbering the Building.

13.2. POLICY REQUIREMENTS.

- 13.2(a) Tenant's insurance policies shall be issued by licensed and qualified insurers authorized to do business in the State of Colorado, and written certificates of insurance (certified copies of the policies may be required) including endorsements shall be delivered to Landlord prior to any occupancy by Tenant and annually thereafter;
- 13.2(b) Each policy of insurance shall require at least thirty (30) days prior written notice to Landlord regarding any cancellation or modification of coverage;
- 13.2(c) All insurance policies shall be endorsed with a subrogation clause, substantially as follows: "This insurance shall not be invalidated should the insured waive, in writing prior to any loss, any and all right of recovery against any party for loss occurring to the property described therein." The parties to this Lease hereby waive claims for recovery from the other party for any loss or damage (whether or not caused by negligence of the other party, and notwithstanding anything to the contrary in this Lease) to any property insured under valid insurance policies of such party, to the extent of the collectible recovery under such insurance.

13.3. **LANDLORD'S INSURANCE.** Landlord shall procure and maintain, as part of Operating Expenses payable by Tenant pursuant to Section 4 above, the following insurance coverage for the Building:

- 13.3(a) Property insurance for the Building and improvements and covering all perils including special form (all risk) coverage. Such coverage shall be written on a replacement cost basis as determined by Landlord or otherwise as required by Landlord's beneficiaries or mortgagees of any deed of trust or mortgage encumbering the Building;
- 13.3(b) Commercial general liability insurance against any and all claims for bodily injury and property damage occurring in or about the Building and Common Areas, in at least the minimum amounts required by Landlord's beneficiaries or mortgagees of any deed of trust or mortgage encumbering the Building;
- 13.3(c) Such other insurance as Landlord deems necessary and prudent, or as may be required by Landlord's beneficiaries or mortgagees of any deed of trust or mortgage encumbering the Building;
- 13.3(d) Tenant acknowledges that Landlord's insurance does not cover in any respect, any of Tenant's equipment, trade fixtures, inventory, business personal property or other contents located in the Premises.

14. LIABILITY OF LANDLORD AND TENANT.

- 14.1. **NO LANDLORD LIABILITY.** Neither Landlord nor any of its employees, officers, managers, agents or representatives shall have any liability to Tenant, or to Tenant's employees, officers, directors, managers, agents, contractors, subtenants, invitees or customers, for any damage, injury, loss, claim or demand based on or arising out of: (a) the repair or maintenance of any portion of the Premises, Building or Common Areas; (b) interruption in the use of the Premises, Common Areas or any equipment therein; (c) any accident or damage resulting from use or operation of elevators, HVAC, electrical, sewer, plumbing systems, and related equipment; (d) termination of this Lease by reason of damage to the Premises or the Building; (e) fire, robbery, theft, vandalism, mysterious disappearance or other casualty; (f) acts or omissions on the part of any other tenant of the Building or of any other person or entity; (g) interruption or disruption of any utilities or services otherwise contemplated elsewhere in this Lease; and (h) leakage in any part of the Premises, Building or Common Areas from wind, water, rain, ice or snow that may leak into or flow from any part of the Premises or the Building, or from drains, pipes or plumbing fixtures in the Premises, Building or Common Areas. Any property placed by Tenant in or about the Premises or Building shall be at the sole risk of Tenant, and Landlord shall not in any manner be responsible therefor. Notwithstanding the foregoing, Landlord shall not be released from liability to Tenant for and to the extent of any loss, injury or damage caused by Landlord's willful misconduct or gross negligence. In no event, however, shall Landlord have any liability to Tenant for business interruption or loss to Tenant's business or any indirect loss or consequential damage.
- 14.2. **TENANT INDEMNIFICATION.** Tenant shall reimburse Landlord for, and shall indemnify, protect, defend and hold Landlord, its employees, officers, managers, agents and representatives harmless from and against, any and all costs, damages, claims, demands, liabilities, expenses (including reasonable attorneys' fees and costs), suffered by or claimed against Landlord, directly or indirectly, based on, arising out of, or related to: (a) Tenant's use and occupancy of the Premises, Building or Common Areas; (b) any act or omission of Tenant, its employees, officers, directors, managers, agents, representatives, contractors, subtenants or invitees in the Premises, Building, or Common Areas; or (c) any Event of Default of Tenant hereunder.
- 14.3. **LIMITATION ON LANDLORD LIABILITY.** Notwithstanding anything to the contrary set forth in this Lease, Tenant shall look solely to the estate of Landlord in and to the Building, in the event of any claim against Landlord arising out of this Lease. Tenant agrees that the liability of Landlord arising out of this Lease, the relationship of Landlord and Tenant, or Tenant's use of the Premises, shall be limited to such estate of Landlord in and to the Building. No properties or assets of Landlord other than the estate of Landlord in and to the Building, and no property owned by any individual partner or shareholder of Landlord, shall be subject to any claim, demand, levy, execution or other enforcement, or for the satisfaction of any other remedy claimed by Tenant, arising out of or in connection with this Lease or Tenant's use of the Premises.

15. DAMAGE OR DESTRUCTION.

- 15.1. **RESTORATION OF THE PREMISES.** If the Premises or any part thereof shall be damaged as a result of any casualty event, Tenant shall deliver prompt notice to Landlord. In the event Landlord has determined in good faith that the Premises can be restored to the condition required by this Lease within the nine (9) month period after the date of such casualty, Landlord shall commence the restoration of the Premises, provided Tenant shall make any available insurance proceeds available to Landlord in accordance with Tenant's insurance obligations set forth in Section 12.1 above (subject to any prior rights of any Mortgagee in and to such proceeds). In addition, Tenant shall repair and restore, at Tenant's sole expense, all Alterations in the Premises. If the Premises are unusable, in whole or in part, during such restoration, the Rent shall be proportionately abated to the extent and for the period that the Premises are unusable. Notwithstanding the foregoing, if any such casualty is the fault of Tenant or its employees, managers, agents, representatives, contractors or invitees, Tenant shall not be entitled to any abatement of Rent after a casualty event.

15.2. **TERMINATION OF THIS LEASE.** If Landlord has determined in good faith that the Premises cannot be restored within the nine (9) month period after the date of such casualty, Landlord shall deliver to Tenant written notice of the same, and thereafter Landlord and Tenant shall each have the right to terminate this Lease upon the delivery of written notice to the other party within thirty (30) days after the date of Landlord's notice to Tenant, in which event this Lease shall terminate as of the date of such casualty and the Rent and Operating Expenses shall be prorated and apportioned as of the date of such casualty. If neither party exercises such right of termination, the Premises shall be restored as provided in Section 15.1 above.

15.3. **TOTAL DESTRUCTION.** If the Building generally is so severely damaged by fire or other casualty (although the Premises may not be affected) that Landlord shall decide not to rebuild or reconstruct the Building, then this Lease and the tenancy hereunder shall terminate on the date specified by Landlord in a notice given within thirty (30) days after the date of such casualty.

16. CONDEMNATION.

16.1. **COMPLETE TAKING.** If the whole of the Premises shall be lawfully condemned or taken in any manner for any public use, this Lease and the tenancy hereby granted shall cease and terminate as of the date of vesting of title in the condemning authority. If only part of the Premises shall be so condemned or taken, then, effective at the vesting of title in the condemning authority, the Base Rent Installments and Operating Expenses Installments shall be abated in proportion to the area of the Premises so condemned or taken. If only a part of the Building shall be condemned or taken and the remainder, in Landlord's reasonable judgment, requires substantial reconstruction or is no longer economically suitable for rental (whether or not the Premises shall be affected), the Landlord may, at Landlord's option, terminate this Lease and the tenancy hereby granted as of the date of such vesting of title, by notifying Tenant in writing of such termination within thirty (30) days following the date on which Landlord shall receive notice of vesting of title.

16.2. **PARTIAL TAKING.** If such condemnation or taking materially deprives Tenant of: (i) access to the Premises and Landlord shall not have provided or undertaken steps to provide other means of access; or (ii) the use of more than thirty percent (30%) of the Rentable Square Feet of the Premises, Tenant may, at Tenant's option, by delivery of notice in writing to Landlord within sixty (60) days following the date on which Tenant shall have received notice of vesting of title, terminate this Lease and the tenancy hereby granted as of the date of vesting of title. If neither Landlord nor Tenant elects to terminate this Lease, this Lease shall be and remain unaffected by such condemnation or taking, except that the Rent shall be abated in proportion to and to the extent of any condemned portion. If only a part of the Premises shall be condemned or taken and this Lease is not terminated, Landlord shall, with reasonable diligence and at its expense, structurally restore the remaining portion of the Premises to substantially the same condition as it was prior to such condemnation or taking.

16.3. **CONDEMNATION AWARD.** In the event of any condemnation or taking of all or a part of the Building or the Premises, Landlord shall be entitled to receive the entire award, including any award made for the lost value of the Lease and estate granted. Tenant hereby expressly assigns to Landlord any and all right, title and interest of Tenant now or hereafter arising in and to any such award, and Tenant shall be entitled to receive no part of such award. Notwithstanding, in any such condemnation proceeding Tenant may submit a separate claim, if allowable as such, against the condemning authority for Tenant's claimed damages, so long as any award made to Tenant does not reduce the award otherwise payable to Landlord.

17. DEFAULT.

17.1. **EVENT OF DEFAULT.** Any of the following shall constitute an event of default ("*Event of Default*") under this Lease:

- 17.1(a) If Tenant shall fail to pay any amount due under this Lease on the applicable due date, and such payment default shall remain uncured for three (3) business days thereafter.
- 17.1(b) If Tenant shall fail to observe or perform any of the covenants, conditions and agreements of this Lease to be performed by Tenant, and such failure shall continue in whole or in part during the thirty (30) calendar day period after notice to Tenant; provided, however, that if such failure is not reasonably capable of being cured within such thirty (30) day period, then the cure period may be extended for up to sixty (60) days total, provided that Tenant has promptly commenced and diligently pursues appropriate cure.
- 17.1(c) If Tenant or any guarantor of this Lease shall: (a) make an assignment for the benefit of creditors; (b) acquiesce in a petition in any court in bankruptcy, reorganization, liquidation or insolvency proceedings; (c) seek, consent to, or acquiesce in the appointment of any trustee, receiver or liquidator of Tenant or of all or any part of Tenant's assets; (d) file a petition seeking an order for relief under the Bankruptcy Code, as now or hereafter amended or supplemented, or by filing any petition under any other present or future federal, state or other statute or law for the same or similar relief; or (e) fail to win the dismissal, discontinuation or vacating of any involuntary bankruptcy proceeding within sixty (60) calendar days after such proceeding is initiated.
- 17.1(d) Any amounts unpaid hereunder for more than thirty (30) calendar days after the due date shall bear interest until paid at the rate of one and one-half percent (1.5%) per month from the date of default until paid in full, and such interest shall be due and payable on the due date for the next succeeding Base Rent Installment.

17.2. **REMEDIES.** If an Event of Default occurs, and is not timely cured by Tenant in full, then Landlord may do any of the following at its option:

- 17.2(a) Terminate this Lease by written notice to Tenant, whereupon this Lease shall end and all rights of Tenant hereunder shall expire and terminate, and everything herein required on the part of Landlord to be done and performed shall cease, but Tenant shall remain liable as provided below.
- 17.2(b) With or without terminating this Lease, Landlord may enter upon and take possession of the Premises and remove Tenant and any other person who may be occupying the Premises or any part thereof, without being liable for damages or liability for such entry. Landlord may make such commercially reasonable alterations and repairs as, in Landlord's absolute discretion, may be necessary to relet the Premises, and may relet the Premises or any part thereof, without notice to Tenant, for such rent and for such use, and for such period of time and subject to such terms and conditions as Landlord, in its absolute discretion, may deem advisable, and receive the rent therefor. Tenant shall pay to Landlord, on demand, any deficiency that may arise by reason of any such reletting, and shall be liable for any and all expenses (including attorneys' fees, brokerage fees, and all re-letting costs) incurred by Landlord in reentering and repossessing the Premises, in making good any default of Tenant, in painting, altering, repairing, dividing or demising the Premises, in protecting and preserving the Premises, and reletting the Premises. Tenant shall remain liable to Landlord for the sum of all Base Rent Installments and Operating Expenses Installments contracted- for under this Lease, as the measure and benefit of Landlord's bargain. Landlord shall not be liable for any failure to relet the Premises or any part thereof or for any failure to collect any rent due upon any such reletting. Notwithstanding, Landlord agrees to pursue reletting of the Premises with commercially reasonable diligence, and Landlord may at any time thereafter elect to terminate this Lease for such prior default.
- 17.2(c) If Landlord elects to terminate this Lease pursuant to Section 17(a) above, Landlord shall nevertheless be entitled to recover from Tenant, and Tenant shall pay to Landlord on demand, as liquidated damages for Tenant's default, an amount equal to the difference between: (i) all contracted-for Rent and other sums that would be payable under this Lease from the date of default, for the remainder of the then-unexpired Term in the absence of termination; and (ii) Tenant's obligation to pay rent pursuant to this lease over the same period. Nothing herein shall be construed to affect or prejudice Landlord's right to claim and recover in full, unpaid rent and any other amounts accrued prior to termination of this Lease.

17.3. **DEFAULT BY LANDLORD.** In the event of any claimed default on the part of Landlord, Tenant shall deliver written notice to Landlord detailing such claim and Landlord shall have thirty (30) calendar days in which to commence to cure such claimed default. Notice to Landlord of any such default shall also be delivered to any lender under a Deed of Trust affecting the Building, provided that Tenant has first been notified (by way of Assignment of Rents or Subordination, Non-Disturbance and Attornment Agreement, or otherwise) of the name and address of such lender. Tenant further agrees that if Landlord shall fail to commence to cure such default within thirty days, then such lender shall have an additional reasonable time in which to commence cure, provided that appropriate cure is commenced and pursued with reasonable diligence. In no event will Landlord or any lender be responsible for any consequential damages claimed by Tenant as a result of any claimed Landlord default, including, but not limited to, lost profits or business interruption.

18. SUBORDINATION.

18.1. **SUBORDINATION INSTRUMENT.** This Lease is subject and subordinate to the lien of any and all mortgages (including deeds of trust and similar security instruments) that may now or hereafter encumber the Building, as well as any and all renewals, extensions, modifications, or refinancings thereof; provided, however, that if the lender under any such security instrument shall require this Lease to be superior and paramount to such instrument, then Tenant agrees to promptly execute, acknowledge and deliver, if requested by Landlord or any such lender, customary and reasonable subordination, non-disturbance and attornment instruments.

18.2. **ATTORNMENT.** Tenant agrees that, if any proceedings are brought for the foreclosure of any security instrument encumbering the Building, then Tenant, if requested to do so by the purchaser at the foreclosure sale, shall recognize such purchaser as Landlord under this Lease, and shall make all payments required hereunder to such new landlord without deduction or set-off; provided, however, that such new landlord shall execute and deliver to Tenant a non-disturbance agreement with respect to Tenant's occupancy of the Premises.

18.3. **LENDER REQUIRED AMENDMENTS TO THIS LEASE.** If, in connection with obtaining temporary, construction or permanent financing for the Building, any lender shall request reasonable modifications of this Lease as a condition to such financing, Tenant agrees that it shall not unreasonably withhold, delay or defer the execution of minor amendments or modifications of this Lease; provided that such modifications shall not increase the financial obligations of Tenant hereunder, nor increase tenant's performance obligations, nor materially or adversely affect Tenant's rights hereunder or interfere with Tenant's use and enjoyment of the Premises.

19. ESTOPPEL CERTIFICATE.

19.1. Tenant shall, without charge, at any time and from time to time, within ten (10) calendar days after Landlord's request, execute and deliver a written estoppel certificate certifying, as of the date of such certificate, the following: (a) whether or not this Lease is unmodified and in full force and effect (or if modified, that the Lease is in full force and effect as modified and setting forth such modifications); (b) whether or not the Term has commenced and the status of any Renewal Term; (c) the amount of Base Rent Installments currently due and payable by Tenant; (d) that no Base Rent Installments have been paid more than thirty (30) days in advance; (e) whether or not Tenant is in possession of the Premises and is currently operating its business therein; (f) that Tenant has no knowledge of any uncured defaults by Landlord or Tenant under this Lease (or, if Tenant has such knowledge, specifying the same in detail); (g) the address to which notices to Tenant should be sent; and (h) any other information reasonably requested by Landlord.

20. LANDLORD'S ENTRY. During the Term, Landlord may enter the Premises after giving 24 hours notice at reasonable hours for any reasonable purpose (and within the last twelve (12) months of the Term, to exhibit the Premises to prospective purchasers, lenders or tenants), to inspect the Premises to verify that Tenant is complying with all obligations hereunder, to make repairs, alterations or improvements to the Premises or other space in or on the Building, if such entry in the Premises is necessary therefor, to install or service Building systems, to perform janitorial or maintenance services, and to post such notices as Landlord may reasonably require to protect its rights. Landlord and its representatives shall have the authority to take such materials and equipment onto the Premises as may be necessary for accomplishing the purposes set forth in this Section. In the event of an emergency, Landlord shall have access to the Premises at any time without notice.

21. HAZARDOUS MATERIALS.

21.1. **DEFINITION.** “*Hazardous Materials*” means any and all pollutants, contaminants, toxic or hazardous wastes, or other similar substances the removal of which is required, or the presence, use, or volume of which is regulated, restricted, prohibited or penalized by any “*Environmental Law*,” which term shall mean any federal, state or local law or regulation issued by a governmental authority related to land, water or air pollution or protecting the environment.

21.2. **NO HAZARDOUS MATERIALS.** Landlord represents that it presently has no actual notice or specific knowledge about the presence of any Hazardous Materials in the Premises that may violate any Environmental Law. Tenant shall not use, generate, dispose, store or transport any Hazardous Materials in the Building, Premises, or Common Areas, such as may violate any Environmental Law, and in the event that such laws, rules or regulations require Tenant to remove or otherwise remedy the existence of any such Hazardous Materials associated with the Premises (except for existing base Building improvements and systems), then Tenant agrees to remove or remedy such condition at Tenant's sole expense. In that event, Tenant further agrees to fully indemnify, defend, and save Landlord harmless from and against any loss, claim, damage, cost and/or liability related thereto, and further, Tenant shall cause its contractors to certify that no such violation has or shall occur in connection with the installation of any Alterations.

22. MISCELLANEOUS PROVISIONS.

22.1. **LANDLORD ASSIGNMENT.** Landlord may freely sell, assign or otherwise transfer all or any portion of its interest under this Lease or in the Premises or Building, and in the event of any such transfer, the party originally executing this Lease as Landlord shall be relieved of any and all Landlord obligations under this Lease from and after the date of such transfer. Tenant shall thereafter attorn to the transferee as Landlord with the same effect as though such transferee had been the original Landlord, provided that the transferee assumes and agrees to carry out all the obligations of Landlord under this Lease.

22.2. **NOTICES.** All notices shall be personally delivered or sent by recognized overnight courier or by certified mail, return receipt requested, postage prepaid. All notices to the respective parties shall be addressed as follows:

If to Landlord: Westland Development Services, Inc.
Attn: Peter Aweida, President
1644 Conestoga Street, Suite 7
Boulder, Colorado 80301

If to Tenant: _____ To Tenant at the Premises _____

and a copy to: Sonoma Pharmaceuticals, Inc.
Chief Financial Officer
645 Molly Lane, Suite 150
Woodstock, Georgia 30189

Either party may, by like written notice, designate a new address or recipient to which such notices shall be directed.

22.3. **NO WAIVER.** All rights and remedies set forth herein are separate, distinct and cumulative. No failure by a party to exercise any right, and no custom, practice, or course of dealing of the parties at variance with the terms hereof shall constitute a waiver of such party's right to demand exact compliance with the terms hereof. Receipt by Landlord of any Rent or other amounts payable hereunder with knowledge of an Event of Default, or acceptance by Landlord of partial payments or partial performance, shall not constitute a waiver or release of any such Event of Default. No waiver by a party of any provision hereof shall be valid unless written, and a waiver so given once shall not be deemed a waiver for any subsequent occasion.

- 22.4. **GOVERNING LAW.** This Lease shall be governed by and construed pursuant to the laws of Colorado. Any action or proceeding arising from or related to this Lease shall be brought only in the District Court, County of Boulder, State of Colorado. In the event of any litigation or proceeding between the parties relating to this Lease or the Premises, the prevailing party shall be awarded all reasonable attorneys' fees, costs and expenses. The parties each hereby waive and release all rights to a trial by jury in any claim, action, proceeding or counterclaim arising out of or in any way connected with this Lease or the Premises.
- 22.5. **SUCCESSORS.** All of the covenants, agreements, terms, conditions, provisions and undertakings in this Lease shall inure to the benefit of, and shall extend to and be binding upon, the parties hereto and their respective legal representatives, successors and assigns, subject to the provisions of this Lease restricting assignment and subletting.
- 22.6. **SEVERABILITY.** If any term, covenant or condition of this Lease shall to any extent be held invalid or unenforceable, then the remainder of this Lease shall not be affected and each remaining term, covenant or condition shall be enforced to the fullest extent permitted by law.
- 22.7. **No RECORDING.** Neither this Lease nor any memorandum hereof shall be recorded.
- 22.8. **No BROKERS.** Landlord and Tenant each represent that they had no dealings with any real estate broker, agent, or other finder with respect to this Lease except: Gregory Glass of Gibbons White, Inc.
- 22.9. **TENANT REPRESENTATIONS.** Each individual executing this Lease on behalf of Tenant hereby represents and warrants that: (a) he or she is duly authorized to execute and deliver this Lease; (b) Tenant is duly organized, is qualified to do business in the State of Colorado, is in good standing under the laws of the State of Colorado, has the power and authority and has obtained all necessary consents to enter into and perform this Lease; and (c) all action required to authorize Tenant to enter into this Lease has been duly taken, and that this Lease is the legally binding obligation of Tenant according to its terms.
- 22.10. **COMPLETE AGREEMENT.** This Lease, including all Exhibits, is intended by the parties as the final expression of their agreement for the Premises and as a complete and exclusive statement of the terms thereof. All negotiations, considerations and representations between the parties are incorporated and no discussions or course of prior dealings between the parties or their affiliates shall be relevant or admissible to determine the meaning of any terms of this Lease. No representations, understandings or agreements have been made or relied upon in making this Lease other than those specifically set forth herein. This Lease can only be modified by a writing signed by all of the parties hereto.
- 22.11. **NAME OF THE BUILDING.** Subject to Tenant's rights of quiet enjoyment as set forth elsewhere herein, Landlord shall have the right at any time to change the name of the Building, to increase the size of the Building by adding additional real property thereto, to construct other buildings or improvements on any portion of the existing Building, or to change the character of or to make alterations of or additions to the Building; however, Landlord covenants that the quality of the Building shall remain substantially similar to its quality on the date of this Lease (normal wear and tear excepted). In the event any such additional buildings are constructed or Landlord increases the size of the Building, Tenant acknowledges that such construction may cause occasional noise and temporary interference. In the event of new construction affecting the Building, Landlord and Tenant shall execute an amendment to this Lease which incorporates any necessary modifications, additions, and adjustments to Tenant's Pro Rata Share. Tenant shall not use the Building's name for any purpose other than as part of its business address.

IN WITNESS, the parties hereto have executed this Lease effective on the date written above.

Landlord:
WESTLAND DEVELOPMENT SERVICES, INC.

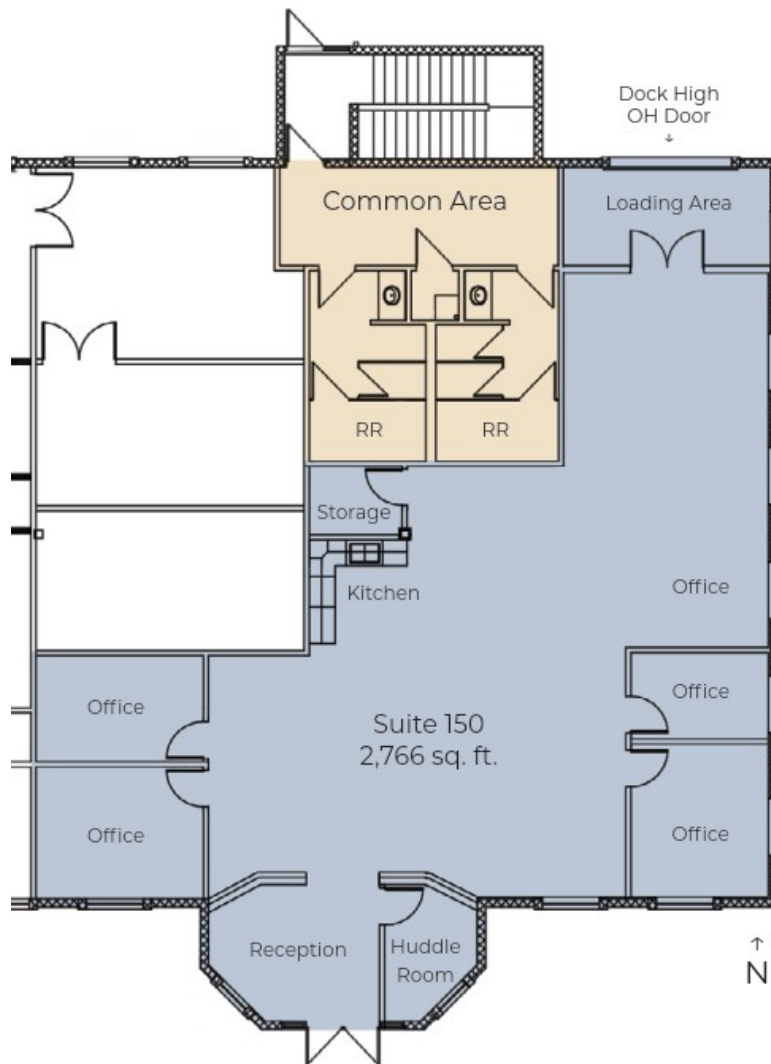
Tenant:
Sonoma Pharmaceuticals, Inc.

By: /s/ Peter A. Aweida
Peter A. Aweida, as President
Date: 2/22/2021

By: /s/ Amy Trombly
Amy Trombly, as CEO
Date: 2/22/2021

EXHIBIT A

THE PREMISES



Lease Amendment

This First Amendment to the Lease (this “First Amendment”) is made June 21, 2023, by and between WESTLAND DEVELOPMENT SERVICES, INC., a Colorado Corporation, (the “Landlord”), and SONOMA PHARMACEUTICALS, INC., a(n) Delaware Corporation (the “Tenant”).

RECITALS

- A. The Landlord and the Tenant entered into that certain Lease, dated February 19, 2021 (the “Original Lease”) with respect to the premises described therein (the “Premises”), covering approximately 2,766 square feet of the Premises, known as 5445 Conestoga Court, Unit(s)/Suite(s) 150, Boulder, Colorado.
- B. The Landlord and Tenant desire to extend the term of the Lease, alter the Base Rent payable under the Lease; and
- C. Make other amendments to the Original Lease as provided in this First Amendment.

AGREEMENT

NOW, THEREFORE, for good and valuable consideration, the receipt and sufficiency of which are acknowledged, the Landlord and the Tenant covenant and agree as follows:

- 1. LEASE TERM. Tenant wishes to extend the term of the Lease for an additional 2-year term (the “Renewal Term”). The Renewal Term shall end on January 31, 2026.
- 2. RENT. Base Rent for the Premises shall be amended as follows:
 - A. Three-thousand five-hundred seventy-two and 75/100 dollars (\$3,572.75) per month from February 1, 2024 through January 31, 2025;
 - B. Three-thousand six-hundred seventy-nine and 93/100 dollars (\$3,679.93) per month from February 1, 2025 through January 31, 2026;
- 3. OPERATING EXPENSES. Tenant shall continue to pay Tenant’s Pro Rata Share (14.91%) of Operating Expenses in the manner provided in the Original Lease.
- 4. LANDLORD WORK. Landlord shall make improvements to the common restrooms within the first six months of the Renewal Term. Tenant accepts their Leased Premises in their “as-is” condition, and the Tenant is not entitled to any improvement by the Landlord or to any other allowance, concession, or credit from Landlord for improvements.
- 5. STATUS OF LEASE OBLIGATIONS. The Tenant acknowledges and certifies that as of the date hereof, the Landlord has performed all covenants and obligations on the part of the Landlord to be performed under the Lease and that the Tenant has no claims or right of offset against the Landlord or the rentals reserved under the Original Lease as amended by this First Amendment.
- 6. RATIFICATION. The Tenant ratifies and confirms the Original Lease as amended this First Amendment. Except as amended this First Amendment, all of the terms and conditions of the Original Lease shall remain in full force and effect.
- 7. SUCCESSORS AND ASSIGNS. This Agreement shall be binding upon and shall inure to the benefit of the heirs, personal representatives, successors, and permitted assigns of the respective parties hereto.
- 8. COUNTERPARTS; SIGNATURE BY FACSIMILE. This Agreement may be executed in one or more counterparts, each of which shall be deemed an original, and all of which together shall constitute one and the same instrument. The parties agree that signatures transmitted by facsimile shall be binding as if they were original signatures.

IN WITNESS WHEREOF, the Landlord and the Tenant have executed this First Amendment as of the day and year first above written.

LANDLORD:

WESTLAND DEVELOPMENT SERVICES, INC.,

a Colorado Corporation

By: /s/ Peter Aweida

Name: Peter Aweida

Title: President

TENANT:

SONOMA PHARMACEUTICALS, INC.

a Delaware Corporation

By: /s/ Amy Trombly

Name: Amy Trombly

Title: Chief Executive Officer

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002
(18 U.S.C. SECTION 1350)**

I, Amy Trombly, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Sonoma Pharmaceuticals, Inc. for the quarter ended September 30, 2023;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 13, 2023

By: /s/ Amy Trombly
Amy Trombly
Chief Executive Officer
(Principal Executive Officer)

**CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002
(18 U.S.C. SECTION 1350)**

I, Jerome Dvonch, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Sonoma Pharmaceuticals, Inc. for the quarter ended September 30, 2023;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 13, 2023

By: /s/ Jerome Dvonch
Jerome Dvonch
Interim Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)

**CERTIFICATION PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002
(18 U.S.C. SECTION 1350)**

Pursuant to section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of section 1350, chapter 63 of title 18, United States Code), the undersigned officers of Sonoma Pharmaceuticals, Inc., a Delaware corporation (the "Company"), do hereby certify, to such officers' knowledge, that:

The Quarterly Report on Form 10-Q for the quarter ended September 30, 2023 (the "Form 10-Q") of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 13, 2023

By: /s/ Amy Trombly
Amy Trombly
Chief Executive Officer
(Principal Executive Officer)

Date: November 13, 2023

By: /s/ Jerome Dvonch
Jerome Dvonch
Interim Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)