

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2003, or

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

For the transition period from NA to NA.

Commission File Number 0-16106

APA OPTICS, INC.

(Exact name of Registrant as specified in its charter)

MINNESOTA 41-1347235
(State or other jurisdiction of (I.R.S. Employer Identification No.)
incorporation or organization)

2950 N.E. 84TH LANE, BLAINE, MINNESOTA 55449
(Address of principal executive offices and zip code)

(763) 784-4995
(Registrant's telephone number, including area code)

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 the filing requirement for the past 90 days.

Yes X No ---

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

Class:	Outstanding at June 30, 2003
Common stock, par value \$.01	11,872,331

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

<TABLE>
<CAPTION>

APA OPTICS, INC.
CONSOLIDATED CONDENSED BALANCE SHEETS

	(Unaudited) June 30, 2003	March 31, 2003
<S>	<C>	<C>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 18,309,434	\$ 22,235,686
Accounts receivable, net of allowance of uncollectible accounts of \$20,644 at June 30, 2003 and March 31, 2003	1,237,484	468,576
Inventories, net	2,062,061	1,398,203
Prepaid expenses	166,882	134,045
Bond reserve funds	-	75,000
Total current assets	21,775,861	24,311,510
Property, plant and equipment, net	4,333,534	3,989,344
Bond reserve funds	342,557	340,629
Bond placement costs	13,771	20,013
Patents, net of accumulated amortization	92,737	85,362
Goodwill	2,778,296	2,500,296
Other	592,660	586,542
	3,820,021	3,532,842

Total assets	\$ 29,929,416	\$ 31,833,696
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term debt	\$ 1,714,305	\$ 1,846,922
Accounts payable	317,132	454,804
Accrued expenses	377,769	286,267
	-----	-----
Total current liabilities	2,409,206	2,587,993
Long-term debt	146,416	326,760
Shareholders' equity:		
Common stock	118,723	118,723
Additional paid-in capital	52,001,681	52,001,681
Accumulated deficit	(24,746,610)	(23,201,461)
	-----	-----
Total shareholders' equity	27,373,794	28,918,943
	-----	-----
Total liabilities and shareholders' equity	\$ 29,929,416	\$ 31,833,696
	=====	=====

</TABLE>

SEE ACCOMPANYING NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

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<TABLE>
<CAPTION>

APA OPTICS, INC.
CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended June 30,	
	2003	2002
	-----	-----
<S>	<C>	<C>
Revenues	\$ 1,566,992	\$ 72,451
Costs and expenses:		
Cost of sales	1,867,881	753,720
Research and development	144,189	355,712
Selling, general and administrative	1,070,952	321,579
	-----	-----
	3,083,022	1,431,011
	-----	-----
Loss from operations	(1,516,030)	(1,358,560)
	25,451	
Other income		133,092
Other expense	(54,570)	(27,276)
	-----	-----
	(29,119)	105,816
	-----	-----
Loss before income taxes	(1,545,149)	(1,252,744)
Income taxes	250	250
	-----	-----
Net loss	\$ (1,545,399)	\$ (1,252,994)
	=====	=====
Net loss per share:		
Basic and diluted	(\$0.13)	(\$0.11)
	=====	=====
Weighted average shares outstanding:		
Basic and diluted	11,872,331	11,875,840
	=====	=====

</TABLE>

SEE ACCOMPANYING NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

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<TABLE>
<CAPTION>

APA OPTICS, INC.
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS

(Unaudited)

	Three Months Ended June 30,	
	2003	2002
<S>	<C>	<C>
OPERATING ACTIVITIES		
Net loss	\$ (1,545,149)	\$ (1,252,994)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	182,176	156,551
Deferred compensation expense	30,919	13,402
Changes in operating assets and liabilities:		
Accounts receivable	(768,908)	(27,707)
Inventories	(663,858)	25,143
Prepaid expenses	(69,871)	38,321
Accounts payable and accrued expenses	(46,170)	(51,841)
Other	-	42,927
Net cash used in operating activities	(2,880,864)	(1,056,198)
INVESTING ACTIVITIES		
Purchases of property and equipment	(526,366)	(56,360)
Purchase price paid in excess of market value	(278,000)	-
Investment in patents	(7,375)	-
Net cash used in investing activities	(811,741)	(56,360)
FINANCING ACTIVITIES		
Bond reserve funds	79,314	51,250
Repurchase of common stock	-	(1,287)
Repayment of long-term debt	(312,961)	(422,651)
Net cash provided by (used in) financing activities	(233,647)	(372,688)
Increase (decrease) in cash and cash equivalents	(3,926,252)	(1,485,246)
Cash and cash equivalents at beginning of period	22,235,686	31,606,403
Cash and cash equivalents at end of period	\$18,309,434	\$30,121,157

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SEE ACCOMPANYING NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

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NOTES TO CONDENSED FINANCIAL STATEMENTS

NOTE 1. BASIS OF PRESENTATION

The accompanying condensed financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. For further information, refer to the financial statements and footnotes thereto included in the Company's annual report on Form 10-K for the year ended March 31, 2003.

In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Certain reclassifications of previously reported amounts have been made to conform to the current period presentation.

NOTE 2. NET LOSS PER SHARE

Basic and diluted net loss per share has been computed by dividing the net loss by the weighted average number of shares outstanding during the period. Common stock options and warrants to purchase 991,197 and 775,872 shares of common stock with a weighted average exercise price of \$9.91 and \$9.01 were outstanding at June 30, 2003 and 2002, respectively, but were excluded from calculating the three months diluted net loss per share because they were antidilutive.

NOTE 3. LAND

The Company acquired land in Aberdeen, SD as part of a financing package provided by the Aberdeen Development Corporation to locate a manufacturing facility in that city. Ownership of the land was contingent upon the Company remaining in the facility through June 23, 2002. After satisfying the contingent

requirement, the Company added \$67,760 (the assessed value of the land for tax purposes) to its balance sheet and increased additional-paid-in capital by a like amount.

NOTE 4. STOCK OPTION GRANT

On August 22, 2002 the Company granted 2,500 options to every current employee with the exception of Anil Jain, the Chief Executive Officer and Ken Olsen, Vice President and Secretary. A total of 122,500 options were granted at the fair market value of the stock on the day of grant. The options are 60% exercisable when the Company achieves certain financial objectives and 40% exercisable when the Company achieves certain operational objectives set forth in the Company's Short-Term Incentive Plan. Accordingly, these options are treated as variable awards, and changes in their value will be reflected in sales, general and administrative expense until the options are exercised or expire.

NOTE 5. ACQUISITION

The Company acquired the assets of Americable, Inc. on June 27, 2003. The purchase price and assets acquired are as follows:

Accounts receivable	\$	594,000
Inventory		638,000
Property, plant and equipment		450,000

Assets purchased		1,682,000
Goodwill		278,000

Purchase price	\$	1,960,000
		=====

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NOTE 6. ADOPTION OF NEW ACCOUNTING PRONOUNCEMENTS

In September 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This statement supercedes SFAS 121 and was effective April 1, 2002 for the Company. This statement did not have a material effect on the financial statements of the Company, but could have a future effect in the event that asset impairment occurs.

In April 2002, FASB issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections." The Company believes the adoption of SFAS No. 145 will not have a material effect on the Company's financial position or results of operations.

In June 2002, FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 requires the recognition of a liability for a cost associated with an exit or disposal activity when the liability is incurred versus the date the Company commits to an exit plan. In addition, SFAS No. 146 states the liability should be initially measured at fair value. The requirements of SFAS No. 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company believes the adoption of SFAS No. 146 will not have a material effect on the Company's financial position or results of operations. In December 2002, FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure." This statement amends FASB Statement No. 123, "Accounting for Stock-Based Compensation", to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. It also amends the disclosure requirements to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation. The transition provisions of this statement are effective for fiscal years ending after December 15, 2002 and the disclosure provisions are effective for annual financial statements for fiscal years ending after December 15, 2002 and the first interim period beginning after December 15, 2002. The Company believes the adoption of SFAS No. 148 will not have a material effect on the Company's financial position or results of operations.

In November 2002, FASB issued Interpretation 45 (FIN 45), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others." This statement clarifies the initial accounting and disclosure requirements of SFAS 5 for certain guarantees. The initial recognition and measurement provisions are effective for guarantees issued or modified after December 31, 2002 and the disclosure requirements are effective for financial statements of interim or annual periods ending after December 15, 2002. The Company believes the adoption of FIN 45 will not have a material effect on the Company's financial position or results of operations.

Statements in this Report about future sales prospects and other matters to occur in the future are forward looking statements and are subject to uncertainties due to many factors, many of which are beyond our control. These factors include, but are not limited to, the continued development of our products, acceptance of those products by potential customers, our ability to sell such products at a profitable price, and our ability to fund our operations. For further discussion regarding these factors, see "Factors That Influence Future Results."

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OVERVIEW

We design, manufacture, source from third parties, and market a variety of fiber optic and copper components to the data communication and telecommunication industries. We are also active in the design, manufacture and marketing of ultraviolet (UV) detection and measurement devices, optical components and in research and development in the area of Gallium Nitride (GaN) based transistors.

Our primary internally manufactured products include standard and custom fiber optic assemblies, copper cable assemblies, value added fiber optics frames, panels and modules. These products are manufactured by our wholly owned subsidiary APA Cables & Networks, Inc. (APACN) who acquired certain assets of Computer System Products, Inc. ("CSP") on March 14, 2003 and certain assets of Americable, Inc. ("Americable") on June 27, 2003. Several of the items discussed under "Results of Operations" show significant changes from the comparable period in the preceding fiscal year as a result of the acquisition of CSP. We expect to see similar changes in the second quarter of fiscal 2004 as a result of our acquisition of Americable.

We outsource from third parties passive optical splitters, arrayed waveguides (AWGs) and wavelength division multiplexers (WDMs) based on Thin Film Filter (TFF) technology, which we combine with our internally manufactured products to create value added components for our customers. The majority of our outsourced product providers are located offshore.

Most companies in the communications industry have been affected by the slowdown in telecommunications equipment spending. Decreased demand and competition have put downward pressure on margins. This downward pressure is likely to continue and we will need to reduce operating costs and improve efficiencies to remain competitive in the marketplace.

We cannot predict whether we will be able to compete with our existing or new products or with current and future competitors. We believe that technological change, the convergence of Internet, data, video and voice on a single broadband network, the possibility of regulatory changes and industry consolidation or new entrants will continue to cause rapid evolution in the competitive environment. The full scope and nature of changes are difficult to predict at this time. Increased competition could lead to price cuts, reduced profit margins and loss of market share, which may seriously harm our business, operating results and financial condition.

Our consumer GaN based product, the SunUVPersonal UV Monitor (SunWatch) is ready for production. As of June 30, 2003, and currently, we are working with our manufacturing facility in China to address yield and production capacity issues. Our goal is to increase production to meet demand for the 2003 holiday season. Our ability to meet this objective is dependent upon depends on our ability to solve production related issues.

Our industrial GaN based product, the TrUVMetertm, required additional engineering to meet the accuracy and reliability specifications for key markets in sterilization, curing and scientific measurement. As of June 30, 2003 reliability tests were in progress and field-testing will follow this process prior to introduction.

RESULTS OF OPERATIONS

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REVENUES

Revenues for the quarter ended June 30, 2003, were \$1,566,992, reflecting over a twenty-fold increase from the comparable period in the preceding fiscal year. The increase is attributable to revenues generated by our wholly owned subsidiary APACN, which produced \$1,512,368 in revenues for the quarter. There are no corresponding revenues from APACN in the comparable period in the preceding fiscal year. We expect revenues to increase again in the second quarter of fiscal 2004 when the results of operations reflect the acquisition of Americable.

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COST OF SALES

Cost of sales increased \$1,114,161 to \$1,867,881 for the quarter ended June 30, 2003, reflecting a 148% increase from the comparable period in the preceding fiscal year. The increase is due primarily to the volume increase attributable to APACN. Gross margins for APACN for the current quarter were \$316,564 or 21%. Overall gross margins were negative in both periods. We expect cost of sales to increase again in the second quarter of fiscal 2004 when the results of operations reflect the acquisition of Americable, Inc. We expect gross margins for APACN to gradually improve over the balance of fiscal 2004 as we consolidate the operations of APACN and Americable, Inc. and eliminate duplicate expenses. We expect overall gross margins to improve as well, but to remain negative through the end of fiscal 2004.

RESEARCH AND DEVELOPMENT EXPENSES

Research and development expenses decreased by \$211,523 to \$144,189 for the quarter ended June 30, 2003 compared to the same period for the preceding fiscal year. This represents a decrease of 59%. The decrease is the result of decreased research activity related to our fiber optic products. The majority of the decrease is due to a reduction in salaries and other related expenses. We expect research and development expenses to remain stable for the balance of fiscal 2004.

SELLING, GENERAL AND ADMINISTRATIVE

Selling, general and administrative expenses increased \$699,411 for the quarter ended June 30, 2003, reflecting a 249% increase compared to the same period in the preceding fiscal year. The increase was primarily due to the acquired operations of APACN, which incurred expenses of \$519,415 for the quarter. Nearly half the total is employee related. The majority of the increase of \$229,958 is related to non-recurring uncapitalized transaction costs for the acquisitions of CSP and Americable.

LOSS FROM OPERATIONS

The loss from operations was \$1,516,030, an increase of \$157,470 or 12% for the quarter ended June 30, 2003 over the comparable period in fiscal 2003. The increased loss in the quarter was the result of operating losses at APACN, which totaled \$202,851 for the period. We expect the losses to decrease over the balance of fiscal 2004 as we realize cost savings and efficiencies related to the consolidation of the operations of APACN and Americable.

OTHER INCOME AND EXPENSE

Other income decreased \$107,641 or 81% for the quarter ended June 30, 2003, from the comparable period in fiscal 2003. The decrease was primarily due to a decrease in interest income due to a decline in interest rates earned on the investment of company funds. Other expenses increased \$27,294 or 100% from the same period in the prior fiscal year. The decreases were due to the combination of a decline in the rate of interest earned on short-term investments and a lower average cash balance, as cash was consumed to fund operations, capital investment, debt service and acquisitions. Unless short-term interest rates increase, we anticipate continuing decreases in interest income as a result of the use of cash in operations, for capital expansion and for debt service.

NET LOSS

The net loss for the quarter ended June 30, 2003, was \$1,545,399 (or \$0.13 per basic and diluted share), an increase of \$292,405 or 23% from the net loss reported for the same period in fiscal 2003. The increased net loss was primarily attributable to losses at APACN.

LIQUIDITY AND CAPITAL RESOURCES

APA's cash and cash equivalents consist primarily of money market funds, U.S. Government instruments or other government instruments with original maturities of less than three months. The balance of cash and cash equivalents

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at June 30, 2003 is \$18,309,434 compared to \$22,235,686 at March 31, 2003. The decrease in cash was primarily the result of the acquisition of the assets of Americable, Inc. and the use of cash to fund operations.

We used net cash of \$811,741 in investing activities in the quarter compared to \$56,360 used in the same period of the preceding fiscal year. Of this amount, \$456,357 was used to purchase assets and \$278,000 was paid for goodwill in connection with our acquisition of Americable. We also invested \$70,009 during the quarter for computer and production equipment. We anticipate a total of approximately \$750,000 in capital expenditures in fiscal 2004, primarily for equipment. We expect to invest in equipment to support the HFET research and development activities over the next several quarters.

Net cash used in financing activities in the quarter totaled \$233,647. We used \$312,961 for the scheduled reduction of debt and a reduction in bond reserve funds generated \$79,314. During the same period in fiscal 2003 we used \$372,688 in financing activities, of which \$422,651 was used for the scheduled reduction of debt, \$51,250 was generated from the reduction of bond reserve funds and \$1,287 was used to repurchase common stock of the company.

We believe we have sufficient funds for operations for at least the next twelve months.

Our contractual obligations and commitments are summarized in the table below (in 000's):

<TABLE>
<CAPTION>

	Total	Less than 1 Year	1-3 years	4-5 years	After 5 years
<S>	<C>	<C>	<C>	<C>	<C>
Long-term debt	\$1,861	\$ 1,615	\$ 70	\$ 36	\$ 140
Operating leases	908	337	571	-	-
Total Contractual Cash Obligations	\$2,769	\$ 1,952	\$ 641	\$ 36	\$ 140

</TABLE>

Application of Critical Accounting Policies

We have reviewed our use of estimates in applying our accounting policies and determined that significant changes in our various estimates would not have a material impact on the presentation of our financial condition, changes in financial condition or results of operations. Accordingly, we do not consider any of our estimates to be "critical estimates" as defined in the rules of the Securities and Exchange Commission. See Note A of Notes to Financial Statements under Item 8 of our Report on Form 10-K for our fiscal year ended March 31, 2003 for descriptions of the use of estimates in our accounting policies. Our management and the audit committee of our board of directors have discussed our use of estimates and have approved our disclosure relating to it in this report.

In Note 7 of this report, the effect of recent promulgations of the Financial Accounting Standards Board (FASB) on the Company is described. We believe the adoption of Statements of Financial Accounting Standards (SFAS) Nos. 144, 145, 146 and 148, and Interpretation 45 (FIN 45) will not have a material effect on the Company's financial position or results of operations.

FACTORS THAT MAY INFLUENCE FUTURE RESULTS

The statements contained in this report on Form 10-Q that are not purely historical are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including, without limitations, statements regarding the Company's expectations, hopes, beliefs, anticipations, commitments, intentions and strategies regarding the future.

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Forward-looking statements include, but are not limited to, statements contained in "Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations." Actual results could differ from those projected in any forward-looking statements for the reasons, among others, detailed below. We believe that many of the risks detailed here are part of doing business in the industry in which we compete and will likely be present in all periods reported. The fact that certain risks are characteristic to the industry does not lessen the significance of the risk. The forward-looking statements are made as of the date of this Form 10-Q and we assume no obligation to update the forward-looking statements or to update the reasons why actual results could differ from those projected in the forward-looking statements.

Unless we generate significant revenue growth, our expenses and negative cash flow will significantly harm our financial position.

We have not been profitable since fiscal 1990. As of June 30, 2003, we had an accumulated deficit of \$24.7 million. We may incur operating losses for the foreseeable future, and these losses may be substantial. Further, we may continue to incur negative operating cash flow in the future. We have funded our operations primarily through the sale of equity securities and borrowings. We have significant fixed expenses and we expect to continue to incur significant and increasing manufacturing, sales and marketing, product development and administrative expenses. As a result, we will need to generate significantly higher revenues while containing costs and operating expenses if we are to achieve profitability.

Declining average selling prices for our fiber optic products will require us to

reduce production costs to effectively compete and market these products

Since the time we first introduced our fiber optic components to the marketplace we have seen the average selling price of fiber optic components decline. We expect this trend to continue. To achieve profitability in this environment we must continually decrease our costs of production. In order to reduce our production costs, we will continue to pursue one or more of the following:

- Seek lower cost suppliers of raw materials or components.
- Work to further automate our assembly process.
- Develop value-added components based on integrated optics.
- Seek offshore sources for assembly services.

We will also seek to form strategic alliances with companies that can supply these services. Decreases in average selling prices also require that we increase unit sales to maintain or increase our revenue. There can be no guarantee that we will achieve these objectives. Our inability to decrease production costs or increase our unit sales could seriously harm our business, financial condition and results of operations.

We believe our success in competing with other manufacturers of fiber optic and copper components and assemblies will depend primarily on our manufacturing and marketing skills, the price, quality and reliability of our products, our delivery capabilities and our control of operating expenses. We have experienced and anticipate experiencing increasing pricing pressures from our current and future competitors as well as general pricing pressure from our customers as part of their cost reduction efforts. Competition may also be affected by consolidation among suppliers in this industry which may increase their resources. As a result, other competitors may be able to respond more quickly to new or emerging technologies and changes in customer requirements.

We cannot predict whether we will be able to compete with our existing or new products or with current and future competitors. We believe that technological change, the convergence of Internet, data, video and voice on a single broadband network, the possibility of regulatory changes and industry consolidation or new entrants will continue to cause rapid evolution in the competitive environment. The full scope and nature of changes are difficult to predict at this time. Increased competition could lead to price cuts, reduced profit margins and loss of market share, which may seriously harm our business, operating results and financial condition.

Demand for our products is subject to significant fluctuation. Market conditions in the telecommunications market in particular may harm our financial condition.

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Demand for our products is dependent on several factors, including capital expenditures in the communications industry. Capital expenditures can be cyclical in nature and result in protracted periods of reduced demand for component parts. Similarly, periods of slow economic expansion or recession can result in periods of reduced demand for our products. The current economic slowdown has been more profound in the telecommunications market resulting in a significant reduction in capital expenditures for products such as our DWDMs and our fiber optic components. It is impossible to predict how long the slowdown will last. Such periods of reduced demand will harm our business, financial condition and results of operations. Changes to the regulatory requirements of the telecommunications industry could also affect market conditions, which could also reduce demand for our fiber optic components.

We may be required to rapidly increase our manufacturing capacity to deliver our products to our customers in a timely manner.

Manufacturing of our products is a complex and precision process. We have limited experience in rapidly increasing our manufacturing capacity or in manufacturing products at high volumes. If demand for our products increases, we will be required to hire, train and manage additional manufacturing personnel and improve our production processes in order to increase our production capacity. There are numerous risks associated with rapidly increasing capacity, including:

- Difficulties in achieving adequate yields from new manufacturing lines,
- Difficulty maintaining the precision manufacturing processes required by our products while increasing capacity,
- The inability to timely procure and install the necessary equipment, and
- Lack of availability of qualified manufacturing personnel.

If we apply our capital resources to expanding our manufacturing capacity in anticipation of increased customer orders, we run the risk that the projected increase in orders will not be realized. If anticipated levels of customer

orders are not received, we will not be able to generate positive gross margins and profitability.

Our dependence on outside manufacturers may result in product delivery delays.

We purchase components that are incorporated into our products from outside vendors. If these vendors fail to supply us with components or completed assemblies on a timely basis, or if the quality of the supplied components or completed assemblies is not acceptable, we could experience significant delays in shipping our products. Any significant interruption in the supply or support of any components or completed assemblies could seriously harm our sales and our relationships with our customers.

Our products may have defects that are not detected before delivery to our customers.

Some of our products are designed to be deployed in large and complex optical networks and must be compatible with other components of the system, both current and future. In addition, our products may not operate as expected over long periods of time. Our customers may discover errors or defects in our products only after they have been fully deployed. If we are unable to fix errors or other problems, we could lose customers, lose revenues, suffer damage to our brand and reputation, and lose our ability to attract new customers or achieve market acceptance. Each of these factors would negatively impact cash flow and would seriously harm our business, financial condition and results of operations.

We must introduce new products and product enhancements to increase revenue.

The successful operation of our business depends on our ability to anticipate market needs and develop and introduce new products and product enhancements that respond to technological changes or evolving industry standards on a timely and cost-effective basis. Our products are complex, and new products may take longer to develop than originally anticipated. These products may contain defects or have unacceptable manufacturing yields when

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first introduced or as new versions are released. Our products could quickly become obsolete as new technologies are introduced or as other firms introduce lower cost alternatives. We must continue to develop leading-edge products and introduce them to the commercial market quickly in order to be successful. Our failure to produce technologically competitive products in a cost-effective manner and on a timely basis will seriously harm our business, financial condition and results of operations.

Our markets are characterized by rapid technological changes and evolving standards.

The markets we serve are characterized by rapid technological change, frequent new product introductions, changes in customer requirements and evolving industry standards. In developing our products, we have made, and will continue to make, assumptions with respect to which standards will be adopted within our industry. If the standards that are actually adopted are different from those that we have chosen to support, our products may not achieve significant market acceptance.

Our products may infringe on the intellectual property rights of others

Our products are sophisticated and rely on complicated manufacturing processes. We have received multiple patents on aspects of our design and manufacturing processes and we have applied for several more. Third parties may still assert claims that our products or processes infringe upon their intellectual property. Defending our interests against these claims, even if they lack merit, may be time consuming, result in expensive litigation and divert management attention from operational matters. If such a claim were successful, we could be prevented from manufacturing or selling our current products, be forced to redesign our products, or be forced to license the relevant intellectual property at a significant cost. Any of these actions could harm our business, financial condition or results of operations.

Acquisitions or investments could have an adverse affect on our business

We completed acquisitions of the assets of Computer System Products, Inc. and Americable, Inc. in March 2003 and June 2003 respectively, as part of our strategy to expand our product offerings, develop internal sources of components and materials, and acquire new technologies. We intend to continue reviewing acquisition and investment prospects. There are inherent risks associated with making acquisitions and investments including but not limited to:

- Challenges associated with integrating the operations, personnel, etc., of an acquired company;
- Potentially dilutive issuances of equity securities;
- Reduced cash balances and or increased debt and debt service costs;
- Large one-time write-offs of intangible assets;
- Risks associated with geographic or business markets different than

- those we are familiar with; and
- Diversion of management attention from current responsibilities.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Our exposure to market risk for changes in interest rates relates primarily to our investment portfolio. We invest in short-term securities of high credit issuers with maturities ranging from overnight up to 24 months. The average maturity of the portfolio does not exceed 12 months. The portfolio includes only marketable securities with active secondary or resale markets to ensure liquidity. We have no investments denominated in foreign country currencies and, therefore, our investments are not subject to foreign exchange risk.

ITEM 4. CONTROLS AND PROCEDURES.

- a. Evaluation of disclosure controls and procedures. The Company's chief executive officer and chief financial officer have concluded that the Company's disclosure controls and procedures (as defined in Exchange Act Rule 13a-14(c)) are sufficiently effective to ensure that the information required to be disclosed by the Company in the reports it files under the Exchange Act is gathered, analyzed and disclosed with

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adequate timeliness, accuracy and completeness, based on an evaluation of such controls and procedures conducted within 90 days prior to the date hereof.

- b. Changes in internal controls. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect these controls subsequent to the date of the evaluation referred to above.

PART II

ITEMS 1 THROUGH 5. NOT APPLICABLE

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

(a) Exhibits.

- Exhibit 10.8 - Sublease with Newport Corporation
- Exhibit 31.1 - Chief Executive Officer's Certification
- Exhibit 32.2 - Chief Financial Officer's Certification
- Exhibit 32.1 - Chief Executive Officer's certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- Exhibit 32.2 - Chief Financial Officer's certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(b) Reports on Form 8-K.

A report on Form 8-K dated May 23, 2003, reported the acquisition of the assets of Computer System Products, Inc.

A report on Form 8-K dated June 30, 2003, reported the acquisition of the assets of Americable, Inc.

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.

APA OPTICS, INC.

8/8/03

/s/ Anil K. Jain

Date

Anil K. Jain
President and
Chief Executive Officer
(Principal executive officer)

13

8/8/03

/s/ David R. Peters

Date

David R. Peters
Chief Financial Officer
(Principal financial and accounting officer)

SUBLEASE

THIS SUBLEASE, made and entered into this 30 day of June, 2003, between Newport Corporation, a Nevada corporation ("SUBLESSOR") and APA Optics, Inc., a Minnesota corporation ("SUBLESSEE").

RECITALS:

A. A lease ("PRIME LEASE") dated December 22, 1995, was made and entered into between Bass Lake Properties Partnership, L.L.P., as Landlord, and Newport Corporation, as Tenant, and whereas Bass Lake Properties Realty has succeeded to interest of the Landlord pertaining to Premises described as 5480 Nathan Lane, City of Plymouth, County of Hennepin, State of Minnesota and which Prime Lease and all Amendments are attached hereto as Exhibit A.

B. The parties hereto desire that the Sublessor sublet to the Sublessee and that the Sublessee take from the Sublessor the portion of the Premises leased under the Prime Lease containing approximately 37,020 square feet of rentable area (hereinafter referred to as the "Sublet Area") as depicted on Exhibit B, attached hereto and made a part hereof.

NOW, THEREFORE, in consideration of the foregoing premises and of the mutual covenants hereinafter contained, but subject to the consent thereto by Landlord, the Sublessor does hereby sublet to the Sublessee and the Sublessee does hereby rent and take from Sublessor, the Sublet Area, subject to the following terms and conditions:

1. Sublease Term. The term of this Sublease shall commence on that date (the -----
"Commencement Date") which is the earlier of (a) September 1, 2003 and (b) the date Sublessee takes possession of the Sublet Area, and shall terminate June 30, 2006 (the "Sublease Term"). Sublessee may take possession of the Premises at any time after approval of this Sublease by Landlord, at Sublessee's option. Without the further act or deed of the Landlord or of either party hereto the term of this Sublease shall terminate and be of no further force or effect on the date set forth above and upon such termination the Sublessee shall immediately vacate the Sublet Area leaving it in the condition which, under the terms of the Prime Lease, the Tenant thereunder is obligated to leave the same.

2. Rent and Utilities.

 - (a) Gross Rent. The Sublessee shall pay to the Sublessor Gross Rent for -----
the Sublet Area in the amount of Eighteen Thousand Twenty-Five Dollars (\$18,025.00) per month (the "Gross Rent"), in advance, on the first day of each month during the Sublease Term commencing September 1, 2003, without deduction, abatement, set-off, prior notice or demand of any kind. Except as set forth in subparagraph 2(b) below, such Gross Rent includes all taxes, operating expenses and common area maintenance charges relating to the Sublet Area.

 - (b) Utilities. From and after the Commencement Date, the Sublessee shall be responsible for all costs of "Utilities" (as hereinafter defined) provided to or used by the Sublet Area. As soon as practicable, Sublessee shall transfer all accounts relating to Utilities into Sublessee's name, and shall pay all costs of Utilities directly to the Utility companies. Sublessor shall cooperate with Sublessee in effecting such transfer. Pending such transfer, Sublessee shall pay to Sublessee, as additional rent, an amount equal to all Utility charges billed directly to Sublessor. As used herein, the term "Utilities" shall mean all services generally considered to be utilities, including but not limited to electricity, gas, [water,] trash/waste disposal, janitorial, phone service, and Internet service.

 - (c) Payment. All rent shall be paid to the Sublessor at the address set -----
forth in Paragraph 7 hereof or at such other address and/or to such other party as the Sublessor may from time to time elect by giving not less than ten (10) days advance written notice thereof to the Sublessee.

3. Use. The Sublessee may use the Sublet Area for general office, warehouse ---
and light manufacturing purposes and for no other purposes whatsoever. The

Sublessee will not use the Sublet Area or permit the Sublet Area or any part of the Property of which it is a part, to be used in violation of (a) any of the terms, covenants or conditions of the Prime Lease, or (b) any laws, ordinances, regulations or requirements of any governmental or quasi-governmental authority having jurisdiction over the Sublet Area.

4. Prime Lease.

(a) Incorporation of Prime Lease. Except as expressly provided to the

contrary herein, all of the terms, covenants, conditions, and restrictions of the Prime Lease (including Exhibits A and D through H thereto) are incorporated herein by this reference as though fully set forth at length. Sublessee takes the Sublet Area, and this Sublease is expressly made, subject to all of the terms, covenants, conditions, and restrictions of the Prime Lease. Except as modified by this Sublease, Sublessee shall comply with and be bound by all of the terms, covenants, conditions, and restrictions contained in the Prime Lease, and shall perform all of Sublessor's obligations under the Prime Lease. When the context requires, each reference in the Prime Lease to Lessor shall be deemed to refer to Sublessor, and each reference therein to Lessee shall be deemed to refer to Sublessee. As between Sublessor and Sublessee, any inconsistency between the terms of the Prime Lease and the terms of this Sublease shall be governed by the terms of this Sublease. Sublessee acknowledges and represents that it has received and reviewed the Prime Lease. If the Prime Lease is terminated, this Sublease shall terminate simultaneously and any unearned rent paid in advance shall be refunded to Sublessee. Sublessee shall be bound to Sublessor (in addition to Landlord) under the same terms and conditions of the Prime Lease as if the Prime Lease had been an instrument executed between Sublessor and Sublessee, but subject to the terms and conditions of this Sublease.

(b) Variations from Prime Lease. Sections 4, 5, 6, 9 and 25 of the Prime

Lease, Exhibit E to the Prime Lease and Sections 1-5, 7 and 8 of Exhibit H to the Prime Lease shall not apply to this Sublease.

(c) Performance Under Prime Lease. Sublessor's performance under this

Sublease shall be subject to the following provisions:

(i) Sublessee recognizes that Sublessor is not in a position to render any of the services or to perform any of the obligations required of the Landlord by the terms of the Prime Lease. Therefore, notwithstanding anything to the contrary contained in this Sublease, Sublessee agrees that performance by Sublessor of its obligations hereunder are conditional upon due performance by the Landlord of its corresponding obligations under the Prime Lease, and Sublessor shall not be liable to Sublessee for any default of the Landlord under the Prime Lease. Sublessee shall not have any claim against Sublessor by reason of the Landlord's failure or refusal to comply with any of the provisions of the Prime Lease unless such failure or refusal is a result of Sublessor's act or failure to act. This Sublease shall remain in full force and effect notwithstanding Landlord's failure or refusal to comply with any such provisions of the Prime Lease and Sublessee shall pay rent and additional rent and all other charges provided for herein without any abatement, deduction or setoff whatsoever. Sublessee covenants and warrants that it fully understands and agrees to be subject to, and bound by, all of the covenants, agreements, terms, provisions and conditions of the Prime Lease, except as modified herein. Furthermore, Sublessee and Sublessor further covenant not to take any action or do or perform any act or fail to perform any act which would result in the failure or breach of any of the covenants, agreements, terms, provisions or conditions of the Prime Lease on the part of the Lessee thereunder.

(ii) Whenever the consent of Landlord shall be required by, or Landlord shall fail to perform its obligations under, the Prime Lease, Sublessor agrees to use commercially reasonable efforts to obtain, at Sublessee's sole cost and expense, such consent and/or performance on behalf of Sublessee.

(iii) To its actual knowledge, Sublessor represents and warrants to Sublessee that the Prime Lease is in full force and effect, and Sublessor has neither given nor received a notice of default pursuant to the Prime Lease.

(iv) Sublessor agrees not to terminate the Prime Lease voluntarily, or modify the Prime Lease in a manner that adversely affects

Sublessee's rights under this Sublease. Sublessee and Sublessor shall each refrain from any act or omission that would result in the failure or breach of any of the covenants, provisions or conditions of the Prime Lease on the part of the Lessee under the Prime Lease.

- (d) Indemnity. Sublessee shall indemnify and hold Sublessor harmless from -----
any and all liability, cost, expense, action or claim of nature (including defaults under Prime Lease) arising out of or related to Sublessee's use and occupancy of the Sublet Area.
- (e) Landlord's Approval. Landlord's written consent to this Sublease in -----
accordance with the terms of the Prime Lease is a condition subsequent to the validity of this Sublease.

5. Hazardous Materials.

- (a) The term "Hazardous Material" as used in this Sublease shall mean any product, substance, chemical, material or waste whose presence, nature, quantity and/or intensity of existence, use, manufacture, disposal, transportation, spill, release or effect, either by itself or in combination with other materials expected to be on the premises, is either: (i) potentially injurious to the public health, safety or welfare, the environment, or the Property; (ii) regulated or monitored by any governmental authority; or (iii) a basis for potential liability of Sublessor to any governmental agency or third party under any applicable statute or common law theory. Hazardous Materials shall include, but not be limited to, hydrocarbons, petroleum, gasoline, crude oil or any products or by-products thereof. "Reportable Use" shall mean (i) the installation or use of any above or below-ground storage tank(s), (ii) the generation, possession, storage, use, transportation, or disposal of a Hazardous Material that requires a permit from, or with respect to which a report, notice, registration or business plan is required to be filled with, any governmental authority, and (iii) the presence in, on, over, under or about the Sublet Area of Hazardous Materials with respect to which any applicable laws require that a notice be given to persons entering or occupying the Sublet Area or neighboring properties.
- (b) Sublessee shall not engage in any activity in or about the Sublet Area which constitutes a Reportable Use of Hazardous Materials without the express prior written consent of Sublessor. Notwithstanding the foregoing, Sublessee may, without Sublessor's prior consent, but upon notice to Sublessor and in compliance with all applicable requirements, use any ordinary and customary materials reasonably required to be used by Sublessee in the normal course of the permitted use, so long as such use is not a Reportable Use and does not expose the Sublet Area, the Property or neighboring properties to any meaningful risk of contamination or damage or expose Sublessor to any liability therefor. Prior to bringing Hazardous Materials upon the Sublet Area or the Property, Sublessee shall submit a list of proposed Hazardous Materials to the attention of Sublessor's Safety Officer. Sublessor shall have a period of fifteen (15) days in which to review and either approve or disapprove of such Hazardous Materials. Sublessor may (but without any obligation to do so) condition its consent to any Reportable Use of any Hazardous Materials by Sublessee upon Sublessee's giving Sublessor such additional assurances as Sublessor, in its reasonable discretion, deems necessary to protect itself, the public, the Sublet Area, the Property and the environment against damage, contamination or injury and/or liability therefor, including but not limited to the installation (and, at Lessor's option, removal on or before Sublease expiration or earlier termination) of reasonably necessary protective modifications to the Sublet Area (such as concrete encasements) and/or the deposit of an additional Security Deposit.
- (c) If Sublessee knows, or has reasonable cause to believe, that Hazardous Materials have come to be located in, on, under or about the Sublet Area or the Property, other than as previously consented to by Sublessor, Sublessee shall immediately give Sublessor written notice thereof, together with a copy of any statement, report, notice, registration, application, permit, business plan, license, claim, action, or proceeding given to, or received from, any governmental authority or private party concerning the presence, spill, release, discharge of, or exposure to, such Hazardous Materials, including, but not limited to, all such documents as may be involved

through the plumbing or sanitary sewer system).

- (d) Sublessee shall indemnify, protect, defend and hold Sublessor, its agents, employees, lenders and ground lessor, if any, the Property and the Sublet Area, harmless from and against any and all damages, liabilities, judgments, costs, claims, liens, expenses, penalties, loss of permits and attorneys' and consultants' fees arising out of or involving any Hazardous Materials brought onto the Sublet Area by or for Sublessee or by anyone under Sublessee's control. Sublessee's obligations under this Article shall include, but not be limited to, the effects of any contamination or injury to person, property or the environment created or suffered by Sublessee, and the cost of investigation (including consultants' and attorneys' fees and testing), removal, remediation, restoration and/or abatement thereof, or of any contamination therein involved, and shall survive the expiration or earlier termination of this Sublease. No termination, cancellation or release agreement entered into by Sublessor and Sublessee shall release Sublessee from its obligations under this Sublease with respect to Hazardous Materials, unless specifically so agreed by Sublessor in writing at the time of such agreement.
- (e) Sublessee shall be solely responsible for instructing its employees with respect to laws relating to Hazardous Materials compliance.
- (f) The requirements of this paragraph are in addition to and not in lieu of those set forth in the Prime Lease.

6. Notices to Landlord. The Sublessee will notify the Landlord forthwith in -----
the event of any default that occurs under the provisions of this Sublease which comes to the attention of the Sublessee, such notice to be given to the Landlord by United States Mail, registered or certified, postage prepaid, at the address provided for Landlord in the preamble to the Prime Lease or as such other address as Tenant shall be advised to use by Landlord.

7. Notices. Any notice provided for herein shall be deemed to be duly given if -----
made in writing and delivered in person to an office of such party or mailed by first class registered or certified mail, postage prepaid, addressed as follows:

If to Sublessor: Newport Corporation
 C/O Vice President Finance and Treasurer
 1791 Deere Avenue
 Irvine, CA 92606

If to Sublessee: APA Optics
 C/O President
 5480 Nathan Lane N
 Plymouth, MN 55447

or to such other address with respect to either party hereto as such party shall notify the other party hereto in writing. Any notice so given, if mailed as aforesaid, shall be deemed received the second (2nd) day after it is deposited in the United States Mail.

8. Limitation of Liability. Neither Sublessor or Landlord shall be liable to -----
Sublessee, or those claiming through or under Sublessee, for injury, death or property damage occurring in, on or about the Sublet Area to Sublessee or an employee, customer or invitee of the Sublessee and Sublessee shall indemnify Sublessor and Landlord and hold them harmless from any claim or damage arising out of any injury, death or property damage occurring in, on or about the Sublet Area to Sublessee or an employee, customer or invitee of the Sublessee.

9. Insurance.

(a) Sublessee shall, at its expense, maintain general commercial liability insurance during the term of this Sublease as required by the Prime Lease (See Exhibit A, Article II) in one or more companies acceptable to Sublessor and Landlord, naming Sublessor, Landlord and Sublessee as insureds, in form and substance reasonably

acceptable to Sublessor and Landlord (such insurance to insure performance by Sublessee or its obligations under paragraph 10 hereof), such insurance to be in those amounts as set forth under said Article of the Prime Lease. Such insurance shall not relieve Sublessee of its obligations under paragraph 8. Such insurance shall specifically insure the performance by Sublessee of the indemnity obligations contained in paragraph 8. If Sublessee fails to maintain

the insurance required to be obtained by Sublessee under this paragraph and as provided in the Prime Lease, Sublessor may, without any obligation to do so, obtain the same at Sublessee's expense.

- (b) No policy of insurance obtained by the Sublessee under the provisions of this paragraph 9 may be canceled or terminated except upon not less than twenty (20) days written notice to Sublessor and Landlord, and each policy shall contain a provision to that effect that the rights of the Sublessor and Landlord thereunder will not be affected by any defense which the insurer may have against the Sublessee or any other party. True and correct copies of each policy of insurance, and renewals thereof, obtained by the Sublessee under the provisions of this paragraph 9, forthwith after issuance thereof, shall be delivered to the Sublessor and to Landlord.
- (c) The parties, on behalf of their respective insurance companies insuring such losses, waive any right of subrogation that one may have against the other.

10. Right of Entry. The Sublessor and Landlord, their authorized agents or -----
attorneys, may at any reasonable time, enter the Sublet Area to inspect, make repairs, improvements and/or changes in the Sublet Area or other premises in the Property of which the Sublet Area is a part as the Sublessor and/or Landlord may deem proper; and there shall be no diminution of rent or liability on the part of the Sublessor or Landlord by reason of inconvenience, annoyance, or injury to business.

11. Default; Remedies.

- (a) If the Sublessee defaults in the observance or performance of any of the Sublessee's covenants, agreements or obligations hereunder wherein the default can be cured by the expenditure of money, either the Sublessor or Landlord may, but without obligations and without limiting any other remedies which they may have by reason of such default, cure the default, charge the cost thereof to the Sublessee and the Sublessee shall pay the same forthwith upon demand, together with interest thereon at the highest permissible rate of interest allowed under the usury statutes of the State of Minnesota or in case no such maximum rate of interest is provided, at the rate of 12% per annum.
- (b) If the Sublessee shall default as defined in Article 26 of the Prime Lease, in the payment of any installment of rent or in the observance or performance of any of the Sublessee's covenants, agreements or obligations hereunder, or if any proceeding is commenced by or against the Sublessee for the purpose of subjecting the assets of the Sublessee to any law relating to bankruptcy or insolvency or for an appointment of a receiver of Sublessee or of any of Sublessee's assets, or if Sublessee makes a general assignment of Sublessee's assets for the benefit of creditors, then, in any such event, the Sublessor may, without process, re-enter immediately into the Sublet Area and remove all persons and property therefrom, and at its option, nullify and cancel this Sublease with respect to all future rights or the Sublessee and have, regain, repossess and enjoy the Sublet Area, anything herein to the contrary notwithstanding. Sublessee hereby expressly waives the service of any notice in writing of intention to re-enter as aforesaid, and also all right of restoration to possession of the Sublet Area after re-entry or after judgment for possession thereof. In the case of any such termination, the Sublessee will indemnify the Sublessor against all loss of rents and other damages, which it may incur by reason of such termination during the residue of the term of this Sublease, and also against all attorney's fees and expenses incurred in enforcing any of the terms of this Sublease.
- (c) Neither Sublessee's interest in this Sublease, nor any interest herein of Sublessee nor any estate hereby created in Sublessee shall pass to any trustee or receiver or assignee for the benefit of creditors or otherwise by operation of law. In the event Sublessee shall become bankrupt or insolvent, or make a transfer in fraud of creditors, or make an assignment for the benefit of creditors, or take or have taken against Sublessee, or any proceeding of any kind under the provision of the Federal Bankruptcy Code or under any other federal or state

insolvency, bankruptcy, reorganization or similar act or if a receiver or trustee is appointed for a substantial portion of Sublessee's assets, this Sublease shall immediately terminate and be of no further force or effect whatsoever, without the necessity for any further action by Sublessor, except that Sublessee shall not be relieved of obligations which have accrued prior to the date of such termination. Upon such termination, the provisions herein relating to the expiration or earlier termination of this Sublease shall control and

Sublessee shall immediately surrender the Sublet Area in the condition required by the provisions of this Sublease. Additionally, Sublessor shall be entitled to all relief, including recovery of damages from Sublessee, which may from time to time be permitted, or recoverable, under the Federal Bankruptcy Code or any other applicable laws.

12. Notwithstanding anything in this Sublease to the contrary, nothing herein shall relieve any of the Sublessor's responsibilities to Landlord and said responsibilities derived from the heretofore described Prime Lease.
13. Assignment and Subleasing. The Sublessee shall not have the right to assign

this Sublease or sublet all or any part of the Sublet Area without the prior written consent of the Sublessor and of the Landlord which consent shall not be unreasonably withheld.
14. Condition of Premises. Sublessee acknowledges and agrees that, as

consideration for the reduced rental rate being provided to Sublessee hereunder, Sublessee accepts the Sublet Area in its "as-is" condition, without Sublessor providing or making any alterations, modifications or refurbishment. Sublessee has made, or shall make, such independent investigation as it deems necessary or appropriate concerning the Sublet Area and the use thereof for Sublessee's intended purposes. Sublessor has not made, and does not make any representations, warranties or agreements as to any matters concerning the Sublet Area or the physical condition thereof, including, but not limited to, square footage, compliance with existing law, utilities, present or future zoning, the purposes for which the Sublet Area are to be used, environmental condition, covenants, conditions and restrictions, the heating, ventilating and air conditioning systems, plumbing, electrical and other mechanical systems used in the operation of the Sublet Area, roofs, walls and floors of the improvements, and all other matters which, in Sublessee's judgment, may bear upon the value and suitability of the Sublet Area for Sublessee's purposes. Neither party is relying upon any statement or representation made by the other not embodied in this Sublease. Except as expressly otherwise set forth in this Sublease, Sublessor hereby specifically disclaims any warranty, guaranty or representation, oral or written, past, present or future, of, as to or concerning (i) the nature and condition of the Sublet Area, including environmental conditions or the presence or absence of any Hazardous Materials, (ii) the suitability thereof for any and all activities and uses which Sublessee may elect to conduct thereon; and (iii) the compliance of the Sublet Area or its operation with any laws, ordinances or regulations of any government or other body (including without limitation, the Americans with Disabilities Act ("ADA")).
15. Security Deposit. Sublessee agrees to deposit with Sublessor, on the date

hereof, a Security Deposit in the amount of \$18,025.00 which shall be held by Sublessor, without interest, as security for the performance of Sublessee's covenants and obligations under this Sublease. Upon the occurrence if any event of default by Sublessee, Sublessor may from time to time without prejudice to any other remedy provided herein or provided by law, apply such Security Deposit to any arrears of rent or other payments due Sublessor under this Sublease, and any other damage, injury, expense or liability caused by such event of default without waiving such event of default and Sublessee shall pay to Sublessor on demand the amount to implied in order to restore the Security Deposit to its original amount of \$18,025.00. Although the Security Deposit shall be deemed the property of the Sublessor, any remaining balance of such Security Deposit shall be returned by Sublessor to Sublessee at such time after termination of this Sublease, that all of Sublessee's obligations under this Sublease have been fulfilled.
16. Additional Agreements by Sublessor. The Sublessor acknowledges and agrees

to the following:
- (a) It has the right to sublease the Sublet Area to Sublessee upon the terms herein stated;
 - (b) Subject to the terms of this Sublease and the Prime Lease, Sublessee, upon paying the rent and all other charges herein provided for and observing and keeping the covenants, agreements, and condition of this Sublease on its part to be kept, shall at all times during the term and the extension term, if exercised, peaceably and quietly
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- hold, occupy and enjoy the Premises, without any disturbance from Sublessor or from the Owner or from any person claiming through them.
- (c) It has observed and kept and, subject to the terms of this Sublease, will continue to observe and keep all covenants, agreements and

conditions of the Prime Lease and has paid the rent and all other charges therein provided, and shall not modify or surrender the Prime Lease without the prior written consent of Sublessee (which shall not be unreasonably withheld, conditioned or delayed) so long as this Sublease is in effect.

- (d) It shall provide to Sublessee copies of any and all notices Sublessor receives from the Owner, or any third party, regarding the Premises or the Lease as soon as reasonably practicable following receipt thereof.
- (e) Sublessee shall have the option to terminate this Sublease Agreement in the event Sublessor's total cash equivalency falls below one million dollars (\$1,000,000).

17. Use of Sublessor's Personal Property. During the Sublease Term, Sublessee shall have the right to use the furniture, cubicles and phone system located in the Sublet Area (the "Personal Property") at no charge. Exhibit B contains a list of the Personal Property and outlines the areas of the Sublet Area in which the Personal Property is located. Upon the expiration or earlier termination of this Sublease, Sublessee shall leave the Personal Property in the Sublet Area in the same condition as on the date of this Sublease, normal wear and tear excepted. Sublessee acknowledges that the Personal Property is being made available for Sublessee's use on an "as-is" basis, without any warranty whatsoever. Sublessee agrees to protect, defend, indemnify and hold Sublessor harmless from and against any and all liabilities, claims, expenses, losses and damages, including, without limitation, reasonable attorneys' fees, costs and disbursements, resulting from use of the Personal Property.

18. Miscellaneous Provisions.

a. Waiver. No purported waiver by Sublessor of any default by Sublessee

of any term, condition or covenant contained herein shall be deemed to be a waiver of such term, condition or covenant unless the waiver is in writing and signed by Sublessor. No such waiver shall in any event be deemed a waiver of any subsequent default under the same or any other term, condition or covenant contained herein. Sublessor's acceptance of rent or other charges following a default hereunder by Sublessee shall not be deemed a waiver of such default or of any earlier default by Sublessee of any term, condition or covenant of this Sublease, other than the failure of Sublessee to pay the particular rental so accepted, regardless of Sublessor's knowledge of such default at the time of such acceptance. The consent or approval by Sublessor to or of any act by Sublessee requiring Sublessor's consent or approval shall not be deemed to waive the requirement of Sublessor's consent or approval to or of any subsequent or similar acts by Sublessee.

(b) Accord and Satisfaction. No payment by Sublessee or receipt by

Sublessor of a lesser amount than rent and other charges herein stipulated shall be deemed to be other than on account of the earliest stipulated rent or other charge, nor shall any endorsement or statement on any check or any letter accompanying a check or payment of rent or other charges be deemed an accord or satisfaction. Sublessor may accept such check or payment without charge or pursue any other remedy in this Sublease.

(c) Entire Agreement. This Sublease sets forth the entire understanding

between Sublessor and Sublessee concerning the Sublet Area and incorporates all prior negotiations and understandings. The parties hereto agree that there are no covenants, promises, agreements, conditions or understandings, either oral or written, whatsoever between the parties hereto with respect to any subject covered by this Sublease other than those set forth herein. No alteration, amendment, change or addition to this Sublease shall be binding upon Sublessor or Sublessee unless in writing and signed by the party to be charged.

(d) No Partnership. Nothing contained in this Sublease shall be deemed or

construed by the parties hereto or by any third person to create the relationship of principal and agent or of partnership or of joint venture, and neither the method of computation of rent nor any other provision contained in this Sublease nor any act of the

parties hereto shall be deemed to create any relationship between Sublessor and Sublessee other than the relationship of Sublessor and Sublessee.

(e) Captions and Section Numbers. The captions, article numbers, and

indices appearing in this Sublease are inserted only as a matter of convenience. They do not define, limit, construe, or describe the scope or intent of the provisions of this Sublease.

- (f) Partial Invalidity. If any term, covenant or condition of this -----
Sublease or the application thereof to any person or circumstances shall be invalid or unenforceable, the remainder of this Sublease, or the application of such term, covenant or condition to persons or circumstances other than those as to which it is held invalid shall both be unaffected thereby, and each term, covenant or condition of this Sublease shall be valid and be enforced to the fullest extent permitted by law.
- (g) Authority. Sublessee does hereby represent and warrant that Sublessee -----
is duly organized, validly existing and in good standing under the laws of the State in which it was organized and has all required power and authority to own, sublease, hold and operate properties and conduct business in the State of Minnesota, and concurrently with the execution and delivery of this Sublease, Sublessee shall submit to Sublessor a resolution of Sublessee's directors (or shareholders) (certified by Sublessee's secretary) confirming Sublessee's authority to enter into this Sublease.
- (h) Governing Law. This Sublease is deemed to have been made in the State -----
of Minnesota, and its interpretation, its construction and the remedies for its enforcement or breach are to be applied pursuant to, and in accordance with the laws of the State of Minnesota for contracts made and to be performed therein.
- (i) Capitalized Terms. All terms spelled with initial capital letters in -----
this Sublease that are not expressly defined in this Sublease shall have the respective meaning given such terms in the Prime Lease.
- (j) Counterparts. This Sublease may be executed in facsimile and in any -----
number of counterparts, each of which shall be deemed to be an original and all of which together shall be deemed to be one and the same instrument.
- (k) Attorneys' Fees. If any dispute, action, lawsuit or proceeding -----
relating to this Sublease, or any default thereunder, whether or not any action, lawsuit or proceeding is commenced, the non-prevailing party shall reimburse the prevailing party for its attorneys' fees and all fees, costs and expenses incurred in connection with such dispute, action, lawsuit or proceeding, including, without limitation, any post-judgment fees, costs or expenses incurred on any appeal, in collection of any judgment or in appearing in any bankruptcy proceeding.

IN WITNESS WHEREOF, each of the parties hereto has caused their presence to be duly executed as of the day and year first above written.

SUBLESSOR:
Newport Corporation

SUBLESSEE:
APA Optics, Inc.

By: -----
William R. Abbott,
Vice President of Finance and Treasurer

By: -----
Anil Jain,
President

CERTIFICATION

I, Anil K. Jain, certify that:

1. I have reviewed this quarterly report on Form 10-Q of APA Optics, Inc.;
2. Based on my knowledge, this quarterly 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 quarterly report, fairly represent 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 officers 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)) 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) 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
 - c) 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 that has materially affected, or is reasonably likely to affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers 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:
 - 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 controls over financial reporting.

August 8, 2003

Signature: /s/ Anil K. Jain

Print Name: Anil K. Jain

Print Title: Chief Executive Officer

CERTIFICATION

I, David R. Peters, certify that:

1. I have reviewed this quarterly report on Form 10-Q of APA Optics, Inc.;
2. Based on my knowledge, this quarterly 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 quarterly report, fairly represent 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 officers 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)) 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) 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
 - c) 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 that has materially affected, or is reasonably likely to affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers 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:
 - 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 controls over financial reporting.

August 8, 2003

Signature: /s/ David R. Peters

Print Name: David R. Peters

Print Title: Chief Financial Officer

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of APA Optics, Inc. (the "Company") on Form 10-Q for the period ending June 30, 2003, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Anil K. Jain, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Sec. 1350, as adopted pursuant to Sec. 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Sections 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly represents, in all material respects, the financial condition and results of operations of the Company.

Signature: /s/ Anil K. Jain

Print Name: Anil K. Jain

Print Title: Chief Executive Officer

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of APA Optics, Inc. (the "Company") on Form 10-Q for the period ending June 30, 2003, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, David R. Peters, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Sec. 1350, as adopted pursuant to Sec. 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Sections 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly represents, in all material respects, the financial condition and results of operations of the Company.

Signature: /s/ David R. Peters

Print Name: David R. Peters

Print Title: Chief Financial Officer
