UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

☒ Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended March 31, 2006.

☐ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _______________________ to _______________________.

Commission File Number 0-16106

APA ENTERPRISES, INC.

(Exact Name of Registrant as Specified in its Charter)

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

2950 N.E. 84th Lane
Blaine, Minnesota 55449
(763) 784-4995
(Address, including ZIP code and telephone number, including area code, of registrant's principal executive office)

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

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

Common Stock, par value $.01 per share
(Title of class)

Series B Preferred Share Purchase Rights
(Title of class)

Indicate by check mark if the registrant is a well-seasoned issuer, as defined in Rule 405 of the Securities Act.

☐ YES ☒ NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or section 15(d) of the Exchange Act.

☐ YES ☒ NO

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

☒ YES ☐ NO

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

☒ YES ☐ NO

Indicate by check mark whether the registrant is a large accelerated filer, and accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☒

Indicate whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

☐ YES ☒ NO

The aggregate market value of the voting and non-voting equity held by non-affiliates of the registrant, as of the last business day of the registrant's most recently completed second fiscal quarter computed by reference to the price at which the common equity was last sold was approximately $15,196,584.

The number of shares of common stock outstanding as of June 17, 2006 was 11,872,331.

Documents Incorporated by Reference:

Portions of our proxy statement for the annual shareholders meeting to be held in August 2006 are incorporated by reference into Part III.

APA ENTERPRISES, INC.
ANNUAL REPORT ON FORM 10-K
TABLE OF CONTENTS

PART I

ITEM 1. BUSINESS.

General Development of Business.

APA Enterprises, Inc. ("APA" or the "Company"), formerly APA Optics, Inc., is a Minnesota corporation which was founded in 1979. Our corporate headquarters is located at 2950 84th Lane N.E., Blaine, MN and our corporate website is www.apaenterprises.com. The information available on our website is not part of this Report.

Since the founding of the Company, we have focused on leading edge research in gallium nitride (GaN), sophisticated optoelectronics, and optical systems, with the primary goal of developing advanced products for subsequent fabrication and marketing. Based on this research we have developed multiple products including fiber optic components for metro and access communications networks, a range of GaN based devices, and precision optical products. We believe that gallium nitride based devices have significant potential markets and we have developed specific expertise and/or patent positions relevant to them. During fiscal year 2004 we ceased the design and manufacturing of precision optical components due to intense competition from Asian manufacturers primarily based on lower labor rates and sold this product line in April 2004 (see Note C to the Consolidated Financial Statements included in Item 8 of this Report). The Company acquired the assets of two companies in calendar 2004 and has deployed them in a wholly owned subsidiary of the Company known as APA Cables and Networks, Inc. ("APACN"). APACN is a manufacturer and seller of telecommunications equipment.

In fiscal year 2005 we formed a wholly-owned subsidiary in India, APA Optronics (India) Private Limited ("APA India"), to take advantage of lower manufacturing costs in India. While the prime focus of the subsidiary will be support of manufacturing activities across the Company's products, it will also support other business activities, including software development. The Company has already started the supporting activities in most of these areas. The Company plans to significantly increase its manufacturing activities once the construction of a larger facility in India is completed and manufacturing operations are located in the new facility some time during the calendar year 2006.

In fiscal year 2006 we sold certain equipment and intellectual property related to our research and development work surrounding gallium nitride based heterojunction field effect transistors. The sale to an unrelated third party for consideration including $1.9 million in cash enables us to focus our R&D efforts on power amplifiers built using GaN technology by using commercially available parts, rather than building our own transistors. This is expected to decrease our operating costs and shorten our time to market for power amplifiers.

In fiscal year 2006, the Company also terminated its manufacturing operations, mostly related to fiber optic communication components, in Aberdeen, South Dakota. The associated assets were designated as not being utilized in manufacturing. Most of the assets, if not utilized within the company, will potentially be sold in future.

The Company reports its operations activities in two segments, Optronics (comprising the activities in Blaine, Minnesota, Aberdeen, South Dakota and India) and APACN (comprising the activities in Plymouth, Minnesota).

APACN focuses on custom-engineered products for telecommunications customers, primarily related to cabling management requirements of the Fiber-to-the-Home ("FTTH") marketplace and in designing and terminating custom cable assemblies for commercial and industrial original equipment manufacturers ("OEM's"). In June 2003, APACN purchased the assets of Americable, Inc. The Americable acquisition allowed APACN to add its own brand of fiber distribution equipment to its full-line of standard and custom copper and fiber optic cable assemblies for broadband service providers and OEM's. The Americable acquisition diversified our product offerings, expanded our opportunities for cross-selling our products to former Computer System Products (CSP) and Americable customers, and enabled us to offer a more complete technology solution to all of our customers. To date, APACN has been able to successfully establish itself as a value-added supplier to its target market of independent telephone companies and cable television operators as well as OEM's who value a high level of engineering services as part of their procurement process. APACN has expanded its product offerings and broadened its customer base since its inception two years ago.

APACN also invested in expanding its sales and engineering expenditures by 32% during fiscal 2006 to increase its potential revenues during fiscal year 2007 and beyond. APACN is already realizing the impact of these efforts in terms of increased sales, particularly during the last two quarters of the fiscal year 2006. The increase in revenues is due to additional customers and product acceptance, mainly in the Fiber-to-the-Premise market, as well as an increase in revenue generated from a new supply agreement to an existing customer serving the test equipment market.

Optronics continues to focus upon Gallium Nitride (GaN) related activities.

Additional information regarding operations in the segments is set forth in Note Q in the Notes to the Consolidated Financial Statements under Item 8 herein.

Description of Business -Optronics Segment

Optronics develops manufactures and markets advanced products for UV (ultraviolet) detection, nitride epitaxial layers and wide band-gap transistors. These operations began with the inception of the Company in 1979 and are located principally in our facility in Blaine, Minnesota. Certain products are purchased from contract manufacturers.

Products

Our current products are described below.

- Ultraviolet (UV) Detector-Based Products We currently manufacture value-added products built around UV detectors fabricated by Optronics and procured externally. These products are:

  - SunUV® Personal UV Monitor The SunUV® Personal UV Monitor (formerly, SunUVWatch®) is a personal ultraviolet (UV) radiation monitor that also incorporates a time/day/date function. It detects UV radiation that is hazardous to human health. It keeps track of the total UV exposure of the user and estimates a maximum exposure time according to government guidelines based on skin type and widely-accepted research on UV exposure limits. The product has been introduced and is being sold through retail channels, catalogs and Internet sites in the USA and Europe.

    In fiscal year 2006, we developed and introduced an attractive new PUVM plastic/metal model that offers two key advantages for the product line. This model, manufactured in-house by our off-shore supplier, potentially eliminates most of the manufacturing issue of some of the earlier models. The new model also can be color-matched to the *SunUVStation*™ described below, which allows us to market the two products together in a pairing that retailers and other channels find attractive.

The new SunUVStation consumer product complements the Personal UV Monitor, and together they give Optronics a product line in the sun protection area. The SunUVStation offers a larger display that indicates the UV Index on a colorful 7" diameter analog face for backyard, pool, patio, campground, or other locations where groups of people are exposed to the sun. This product, complementing the small format personalized UV monitor, will be manufactured at the new APA Optronics India facility and marketed in FY2007 through selected channels.

Industrial Products: Profiler M UV Meter Optronics' *Profiler M* radiometer was created for the printing and coating industries that use UV curing. The instrument measures the intensity and distribution of four UV bands inside curing chambers. Data from the instrument can be transferred to a computer for analysis using proprietary *CureControl* software supplied as part of the purchase. Periodic upgrades of the software will be offered, providing the potential for increased utility for the user and an ongoing revenue stream for Optronics. Marketing and sales activities for the Profiler M are now focused on expanding our group of domestic and international distributors. Currently, there are four companies distributing the product - 2 general UV industries suppliers, a UV equipment manufacturer, and a UV coatings and adhesives manufacturer and we are seeking additional representatives in all these areas. Supporting marketing activities include exhibiting at trade shows for the industry and participation in technical conferences and journals that can showcase the advantages of the *Profiler M*.

Research and development efforts at Optronics are described below.

- In the 4th quarter of fiscal year 2006 we completed the sale of our epitaxial foundry to an unrelated, third party for total consideration of $1.9 million in cash and a license back of the technology within a specified field of use. The transaction included sale of APA's multi-wafer metal organic chemical vapor deposition system, the technical know-how associated with the growth of state-of-the-art epitaxial layers, two heterojunction field effect transistor patents (United States patent 5,192,987 and United States patent 5,296,395), an additional pending patent (now allowed, United States patent application claiming priority of United States provisional application No. 60/428,856), and associated intellectual property. Terms of the transaction allow APA to market and sell products for applications greater than 1 GHz and provide revenue sharing based on future licensing agreements regarding these patents. The transaction allowed APA to terminate the lease of an off-site facility utilized by the epi foundry and resulted in termination of three employees associated with the development and growth of epi-layers.

- The sale described in the immediately preceding paragraph should decrease operating costs while enabling early entry into power amplifier markets utilizing GaN power transistors procured from outside sources. Such transistors have demonstrated impressive performance while maintaining excellent reliability. Our goal is to manufacture amplifiers that utilize these transistors - simplifying amplifier architecture, improving amplifier efficiency and increasing bandwidth and power. Such amplifiers will initially target test and measurement and later cellular base station applications.

- Opportunities to team with companies offering complementary capabilities to our own are being evaluated based on relevance to our long term strategic interests.

Marketing and Distribution

We do not maintain a large internal sales force. We have one sales person dedicated to the SunUV(C) Personal UV Monitor and we also maintain product information on our website. Additionally we use manufacturer's representative and distributors domestically.

Competition

The optoelectronics and compound semiconductor electronic device markets are evolving rapidly and, therefore, the competitive landscape changes continually. The opportunities presented by these markets have fostered a highly competitive environment. This competition has resulted in price reductions and lower profit margins for the companies serving this market. Many of the companies engaged in these businesses are well financed and have significantly greater research, development, production, and marketing resources than we do. Some of these companies have long operating histories, well-established distribution channels, broad product offerings and extensive customer bases. Our ability to compete with these companies across our product lines will depend largely on the performance of our devices, our ability to innovate and develop competitive solutions for our customers, our intellectual property, our ability to convince customers to adopt our technology early in their design cycle, and our ability to control costs.

We are not aware of any companies currently marketing a personal UV monitor with a combination of features, style and packaging equivalent to ours, although there are other manufacturers of this type of product in the United States, Japan and Korea. Our SunUVStation product is unique to the best of our knowledge.

Electronic Instrumentation and Technology, Inc. ("EIT"), Apprise Technologies, UV Process Supply and International Light offer UV curing control instruments that perform similar functions to the Profiler M, although we believe that our product offers a very competitive combination of features and price.

There are no currently available GaN/AlGaN power amplifiers; however, we anticipate that there will be several US, Japanese and European firms announcing products in the next calendar year.

Description of Business - APACN

APACN offers a broad range of telecommunications equipment and products developed from over 20 years of product expertise acquired in each of the CSP and Americable acquisitions. Its broad range of product offerings include the design and manufacture of standard and custom connectivity products such as fiber distribution systems, optical components, Outside Plant (OSP) cabinets, and fiber and copper cable assemblies that serve the communication service provider including FTTH, large enterprise, and OEM markets. APACN maintains a range of engineering and technical knowledge in-house that works closely with customers to develop, customize and enhance products from design through production. Most products are produced at APACN's plant in Plymouth, Minnesota with support from a corporate network of global manufacturing partners. APACN produces these products on both a quick-turn and scheduled delivery basis.

Products

- Fiber Distribution Central Office Frame Systems APACN Fiber Distribution Systems ("FDS") are high density, easy access fiber distribution panels and cable management systems that are designed to reduce installation time, guarantee bend radius protection and improve traceability. In the 144-port count configuration, APACN is the industry leader for density, saving the customer expensive real estate in the central office. The product line fully supports a wide range of panel configurations, densities, connectors, and adapters that can be utilized on a stand-alone basis or integrated into the panel system. The unique interchangeable building block design delivers feature rich solutions which are able to meet the needs of a broad range of network deployments.

- Fiber Distribution Outside Plant Cabinets APACN's Fiber Scalability Center ("FSC") is a modular and scalable fiber distribution platform designed for "grow-as-you-go cost containment" as fiber goes beyond the control of a central office and closer to the user. This allows rollout of FTTH services by communication service providers without a large initial expense. Each outside plant cabinet stores feeder and distribution splices, splitters, connectors and slack cable neatly and compactly, utilizing field-tested designs to maximize bend radius protection, connector access, ease of cable routing and physical protection, thereby minimizing the risk of fiber damage. The FSC product has been designed to scale with the application environment as demand requires and to reduce service turn-up time for the end-user.

- Optical Components APACN packages optical components for signal coupling, splitting, termination, multiplexing, demultiplexing and attenuation to seamlessly integrate with the APACN FDS. This value-added packaging allows the customer to source from a single supplier and reduce space requirements. The products are built and tested to meet the strictest industry standards ensuring customers trouble-free performance in extreme outside plant environments.

- Cable Assemblies APACN manufactures high quality fiber and copper assemblies with an industry-standard or customer-specified configuration. Industry-standard assemblies built include but are not limited to: single mode fiber, multimode fiber, multi-fiber, CATV node assembly, DS1 Telco, DS 3 (734/735) coax, Category 5e and 6, SCSI, Token Ring, and V.35. In addition, APACN's engineering services team works alongside the engineering design departments of our OEM customers to design and manufacturer custom solutions for both in-the-box as well as network connectivity assemblies specific to that customer's product line.

Marketing and Distribution

APACN markets its products in the United States through a direct sales team with limited support from a network of manufacturer representative organizations. In addition, during fiscal 2006, the company significantly expanded its use of a two-tier distribution channel allowing the product line to penetrate a broader field of broadband service providers. APACN works closely with its target customers to adapt the company's product platform to the client's unique requirements. APACN offers a high level of customer service and principally brings new products to markets based upon the specific requests of its customers.

Competition

Competitors for the APACN FDS and FSC include but are not limited to ADC Telecommunications, Inc., Corning Cabling Systems, Inc., OFS (Furukawa Electric North America, Inc.), Telect Inc., Fiber Optic Network Solutions (FONS) Corporation (acquired by ADC Telecommunications during fiscal 2006), Alcatel, Inc., and Tyco Electronics, Inc. Nearly all of these firms are substantially larger than APACN and as a result may be able to procure pricing for necessary components and labor at much lower prices. Competition for the custom fiber and copper termination services for cable assemblies is intense. Competitors range from small, family-run businesses to very large contract manufacturing facilities.

Sources of Materials and Outsourced Labor

Numerous purchased materials, components, and labor, are used in the manufacturing of the Company's products. Most of these are readily available from multiple suppliers. However, some critical components and outsourced labor are purchased from a single or a limited number of suppliers. The loss of access to some components and outsourced labor would have a material adverse effect on our ability to deliver products on a timely basis and on our financial performance.

Patents and Intellectual Property

As of March 31, 2006, we had 14 patents issued in the United States and two pending patent applications inside and outside the United States. During the last fiscal year the following 2 patents and a patent in process were sold:

US Patent 5,192,987 "High electron mobility transistor with GaN/AlGaN heterojunction";

US Patent 5,2196,395 " Method of making a high electron mobility transistor";

US Patent application from provisional No. 60/428,856 (since allowed).

Terms of the sale of these patents allow APA to market and sell products for applications greater than 1 GHz

All of our patents relate to the business of our Optronics segment. We believe our success heavily depends upon technology we develop internally and we anticipate additional patent application filings this year. We have made significant progress toward improving the active, strategic management of our intellectual property portfolio. The markets for our products are characterized by rapid change and continual innovation that could render our technology and patents obsolete before their statutory protection expires. Several of the companies we compete with have greater research and development resources than we do and could develop technologies and products that are similar or even superior to ours without infringing on our intellectual property. It is possible that sale or license of part of our patent portfolio could be helpful to our business plans.

Environmental Compliance

Because we handle a number of chemicals in our operations, we must comply with federal, state and local laws and regulations regarding the handling and disposal of such chemicals. To date the cost of such compliance has not been material.

Major Customers

No single customer accounted for more than 10% of the Company's sales in fiscal 2006, 2005, or 2004.

Backlog

Backlog reflects purchase order commitments for our products received from customers that have yet to be fulfilled. Backlog orders are generally shipped within three months. Optronics had no backlog as of March 31, 2006, a backlog of $7,200 as of March 31, 2005 and a backlog of $6,490 as of March 31, 2004. APACN had backlogs of $1,383,206 as of March 31, 2006, $429,180 as of March 31, 2005, and $856,700 as of March 31, 2004.

Research and Development

During the fiscal years ended March 31, 2006, 2005, and 2004, Optronics spent approximately $1,409,000, $1,104,000, and $949,000, respectively, on research and development, mainly for the development of compound semiconductor electronic devices. This segment had no research activities sponsored by customers in fiscal years 2006, 2005 or 2004. We operate in highly competitive and rapidly evolving markets and plan to commit significant resources for research and development for the foreseeable future. We could locate research and development facilities in locations other than our current facilities in Minnesota based on several factors, including accessibility to qualified personnel and facility costs. APACN has made no significant expenditures for research and development from its inception through March 31, 2006.

Employees

As of March 31, 2006, Optronics had 36 full-time employees in the combined locations of Blaine, MN, Aberdeen, SD, and India. As of March 31, 2006, APACN had 92 full-time employees, mainly in Plymouth, MN. Our future performance is dependent on our ability to attract, train, and retain highly qualified personnel. We have no employment agreements with our employees. The loss of one or more key employees could negatively impact the Company.

ITEM 1A. RISK FACTORS.

Factors That May Affect Future Results

The statements contained in this Report on Form 10-K 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. Forward-looking statements include, but are not limited to, statements contained in "Item 1. Business" and "Item 7. 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 Report as Form 10-K 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.

Our Results of Operations

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 March 31, 2006, we had an accumulated deficit of $36.5 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.

Acquisitions or investments could have an adverse affect on our business.

We acquired the assets of Americable in June 2003 and integrated them with the assets of APACN. We acquired assets in India in March 2005 as part of a strategy to take advantage of lower manufacturing costs in India. 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.

Our Products and Introduction of New Products

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 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 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.

We may make additional strategic changes in our product portfolio, but our strategic changes and restructuring programs may not yield the benefits that we expect.

In connection with the downturn in the communications industry we have divested or closed product lines and businesses that either were not profitable or did not match our new strategic focus. As necessary, we may make further divestitures or closures of product lines and businesses. We may also make strategic acquisitions.

The impact of potential changes to our product portfolio and the effect of such changes on our business, operating results and financial condition, are unknown at this time. If we acquire other businesses in our areas of strategic focus, we may have difficulty assimilating these businesses and their products, services, technologies and personnel into our operations. These difficulties could disrupt our ongoing business, distract our management and workforce, increase our expenses and adversely affect our operating results and financial condition. In addition to these integration risks, if we acquire new businesses, we may not realize all of the anticipated benefits of these acquisitions, and we may not be able to retain key management, technical and sales personnel after an acquisition. Divestitures or elimination of existing businesses or product lines could also have disruptive effects and may cause us to incur material expenses.

Manufacturing and Operations

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

We purchase components and labor that are incorporated into our products from outside vendors. In the case of the SunUV® Personal UV Monitor, we supply components to an outside assembler who delivers the completed product. 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. In addition, we have increased our reliance on the use of contract manufacturers to make our products. If these contract manufacturers do not fulfill their obligations or if we do not properly manage these relationships, our existing customer relationships may suffer.

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 precise 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 precise 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.

We are dependent upon skilled employees; if we lose the services of our key personnel our ability to execute our operating plan, and our operating results, may suffer.

Our future performance depends in part upon the continued service and contributions of key management, engineering, sales and marketing personnel, many of whom would be difficult to replace quickly. If we lose any of these key personnel, our business, operating results and financial condition could be materially adversely affected or delay the development or marketing of existing or future products. Competition for these personnel is intense and we may not be able to retain or attract such personnel. Our success will depend in part upon our ability to attract and retain additional personnel with the highly specialized expertise necessary to generate revenue and to engineer, design and support our products and services.

Markets and Market Conditions

Demand for our products is subject to significant fluctuation. Adverse market conditions in the communications equipment industry and any slowdown in the United States economy may harm our financial condition.

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. 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 products.

Our industry is highly competitive and subject to pricing pressure.

Competition in the communications equipment market is intense. We have experienced and anticipate experiencing increasing pricing pressures from current and future competitors as well as general pricing pressure from our customers as part of their cost containment efforts. Many of our competitors have more extensive engineering, manufacturing, marketing, financial and personnel resources than we do. As a result, these competitors may be able to respond more quickly to new or emerging technologies and changes.

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 manufacturing and 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.

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.

Conditions in global markets could affect our operations.

We have acquired facilities in India which will support design and production of our products. We also source products and labor from off shore suppliers. We expect that our foreign operations and reliance on off shore sourcing will increase in the future. As such we are subject to the risks of conducting business internationally. Those risks include but are not limited to:

- local economic and market conditions;
- political and economic instability;
- fluctuations in foreign currency exchange rates;
- tariffs and other barriers and restrictions;
- geopolitical and environmental risks; and
- changes in diplomatic or trade relationships and natural disasters.

We cannot predict whether our business operations and reliance in these markets will be affected adversely by these conditions.

Our Customers

Our sales could be negatively impacted if one or more of our key customers substantially reduce orders for our products.

If we lose a significant customer, our sales and gross margins would be negatively impacted. In addition, the loss of sales may require us to record impairment, restructuring charges or exit a particular business or product line.

Consolidation among our customers could result in our losing a customer or experiencing a slowdown as integration takes place.

It is likely that there will be increased consolidation among our customers in order for them to increase market share and achieve greater economies of scale. Consolidation is likely to impact our business as our customers focus on integrating their operations and choosing their equipment vendors. After a consolidation occurs, there can be no assurance that we will continue to supply the surviving entity.

Customer payment defaults could have an adverse effect on our financial condition and results of operations.

As a result of competitive conditions in the telecommunications market, some of our customers may experience financial difficulties. It is possible that customers from whom we expect to derive substantial revenue will default or that the level of defaults will increase. Any material payment defaults by our customers would have an adverse effect on our results of operations and financial condition.

Performance Requirements and Performance of our Products

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

Some of the Company's products are designed to be deployed in large and complex networks and must be compatible with other components of the system, both current and future. Our customers may discover errors or defects in our products only after they have been fully deployed. In addition, our products may not operate as expected over long periods of time. In the case of the SunUV® Personal UV Monitor, a consumer product, customers could encounter a latent defect not detected in the quality inspection. 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.

Product defects could cause us to lose customers and revenue or to incur unexpected expenses.

If our products do not meet our customers' performance requirements, our customer relationships may suffer. Also, our products may contain defects. Any failure or poor performance of our products could result in:

- delayed market acceptance of our products;
- delays in product shipments;
- unexpected expenses and diversion of resources to replace defective products or identify the source of errors and correct them;
- damage to our reputation and our customer relationships;

- delayed recognition of sales or reduced sales; and

- product liability claims or other claims for damages that may be caused by any product defects or performance failures.

Intellectual Property

If we are unable to adequately protect our intellectual property, third parties may be able to use our technology, which could adversely affect our ability to compete in the market.

Our success will depend in part on our ability to obtain patents and maintain adequate protection of the intellectual property related to our technologies and products. The patent positions of technology companies, including our patent position, are generally uncertain and involve complex legal and factual questions. We will be able to protect our intellectual property rights from unauthorized use by third parties only to the extent that our technologies are covered by valid and enforceable patents or are effectively maintained as trade secrets. The laws of some foreign countries do not protect intellectual property rights to the same extent as the laws of the U.S., and many companies have encountered significant problems in protecting and defending such rights in foreign jurisdictions. We will apply for patents covering our technologies and products as and when we deem appropriate. However, these applications may be challenged or may fail to result in issued patents. Our existing patents and any future patents we obtain may not be sufficiently broad to prevent others from practicing our technologies or from developing competing products. Furthermore, others may independently develop similar or alternative technologies or design around our patents. In addition, our patents may be challenged, invalidated or fail to provide us with any competitive advantages.

We rely on trade secret protection for our confidential and proprietary information. We have taken security measures to protect our proprietary information and trade secrets, but these measures may not provide adequate protection. While we seek to protect our proprietary information by entering into confidentiality agreements with employees, collaborators and consultants, we cannot assure you that our proprietary information will not be disclosed, or that we can meaningfully protect our trade secrets. In addition, our competitors may independently develop substantially equivalent proprietary information or may otherwise gain access to our trade secrets.

Our business will suffer if we are unable to protect our patents or our proprietary rights.

Our success depends to a significant degree upon our ability to develop proprietary products. However, patents may not be granted on any of our pending patent applications in the United States or in other countries. In addition, the scope of any of our issued patents may not be sufficiently broad to offer meaningful protection. Furthermore, our issued patents or patents licensed to us could potentially be successfully challenged, invalidated or circumvented so that our patent rights would not create an effective competitive barrier.

Intellectual property litigation could harm our business.

It is possible that we may have to defend our intellectual property rights in the future. In the event of an intellectual property dispute, we may be forced to litigate or otherwise defend our intellectual property assets. Disputes could involve litigation or proceedings declared by the United States Patent and Trademark Office or the International Trade Commission. Intellectual property litigation can be extremely expensive, and this expense, as well as the consequences should we not prevail, could seriously harm our business.

If a third party claimed an intellectual property right to technology we use, we might be forced to discontinue an important product or product line, alter our products and processes, pay license fees or cease certain activities. We may not be able to obtain a license to such intellectual property on favorable terms, if at all.

Litigation or third party claims of intellectual property infringement could require us to spend substantial time and money and adversely affect our ability to develop and commercialize products.

Our commercial success depends in part on our ability to avoid infringing patents and proprietary rights of third parties, and not breaching any licenses that we have entered into with regard to our technologies. Other parties have filed, and in the future are likely to file, patent applications covering genes and gene fragments, techniques and methodologies relating to model systems, and products and technologies that we have developed or intend to develop. If patents covering technologies required by our operations are issued to others, we may have to rely on licenses from third parties, which may not be available on commercially reasonable terms, or at all.

Third parties may accuse us of employing their proprietary technology without authorization. In addition, third parties may obtain patents that relate to our technologies and claim that use of such technologies infringes these patents. Regardless of their merit, such claims could require us to incur substantial costs, including the diversion of management and technical personnel, in defending ourselves against any such claims or enforcing our patents. In the event that a successful claim of infringement is brought against us, we may be required to pay damages and obtain one or more licenses from third parties. We may not be able to obtain these licenses at a reasonable cost, or at all. Defense of any lawsuit or failure to obtain any of these licenses could adversely affect our ability to develop and commercialize products.

Executive Officers

The following is a list of our executive officers, their ages, positions and offices as of March 31, 2006.

Name	***Age***	***Position***
Dr. Anil K. Jain	60	Chief Executive Officer/President/Chief Financial Officer of APA Enterprises, Inc.
Cheri Beranek Podzimek	43	President, APACN

Dr. Anil K. Jain has been a Director, Chief Executive Officer and President since March 1979. He also currently serves as Chief Financial Officer. From 1973 until October 15, 1983, when Dr. Jain commenced full time employment with the Company, he was employed at the Systems and Research Center at Honeywell Inc. as a Senior Research Fellow, coordinating optics-related development.

Cheri Beranek Podzimek joined APACN in July 2003 as President. Ms. Podzimek was previously President of Americable, which was acquired by APACN in June 2003. She served as President of Americable from 2002 to 2003. From 2001 to 2002 Ms. Podzimek was Chief Operating Officer of Americable. Previously, Ms. Podzimek held a variety of lead marketing positions with emerging high-growth technology companies. She served as Vice President of Marketing from 1996-2001 at Transition Networks, a manufacturer of network connectivity products, Director of Marketing from 1992 to 1996 at Tricord Systems, an early stage multi-processor based super server manufacturer, and Director of Marketing from 1988 to 1992 at Digi International, a designer and manufacturer of connectivity products. Earlier in her career Ms. Podzimek held marketing positions for non-profit organizations, including the City of Fargo, the Metropolitan Planning Commission of Fargo/Moorhead and North Dakota State University.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

None

ITEM 2. PROPERTIES.

We have corporate offices, manufacturing facilities, and laboratories located in an industrial building at 2950 N.E. 84th Lane, Blaine, Minnesota. We currently lease 23,500 square feet of space under a lease from Jain-Olsen Properties, a partnership consisting of Anil K. Jain and Kenneth A. Olsen, the former being officer and director of the Company. See Note O of Notes to the Consolidated Financial Statements included under Item 8 of this Report. We own land directly west of the Blaine facility that may be used for future expansion.

We own a 24,000 square foot production facility in Aberdeen, South Dakota, which was used mainly for assembly of products for APACN customers and to a lesser extent for assembly of our DWDM components and UV detectors. During the fiscal year 2006 the Company terminated all the manufacturing activities at this facility and put the facility for potential lease or sale. The land upon which this facility is located (approximately 12 acres) was granted to us as part of a financing package from the city of Aberdeen. See Note I of Notes to the Consolidated Financial Statements included under Item 8 in this Report for further information regarding the financing of this facility. This land was sub-divided into two parcels of approximately 10 and 2 acres, and the latter was sold to Aberdeen Development Corporation. The Company contemplates further sub-dividing the balance 10 acre land in to two parts of approximately 5 acres each with the intention of selling or leasing the building along with 5 acre land and retaining the other 5 acre parcel for future use.

APA signed a lease agreement in June of 2004 with Veeco Compound Semiconductor, Inc. to locate APA's multi-wafer MOCVD unit, purchased in fiscal 2004, in Veeco's facilities in White Bear Lake, Minnesota, which is near APA's Blaine facility. The lease term commenced on December 1, 2004 and was terminated March 10, 2006 coinciding with the sale of the epi foundry operation to an unrelated third party.

APA India currently leases, on a month to month basis, a 500 square meter facility in a special export zone near New Delhi, India. The Company is planning to relocate in to its own 1,000 square meter facility, under construction at present in the same general location, some time in calendar year 2006.

APACN subleases a 37,000 square foot facility in Plymouth, Minnesota consisting of office, manufacturing and warehouse space. This lease runs through June, 2006. Subsequent to year end, the company has renewed the lease of this facility through November 2013 on 30,000 square feet.

ITEM 3. LEGAL PROCEEDINGS.

On May 23, 2005 APA Enterprises, Inc. ("APA") was served with a complaint filed in U.S. District Court, District of Virginia by Electronic Instrumentation and Technology, Inc. ("EIT"). EIT alleged that APA obtained certain confidential information from EIT and used such information for unauthorized purposes. EIT requested money damages of unspecified amount and equitable relief. This matter was tried to a jury in December 2005. APA defeated EIT's claims of fraud and misappropriation of trade secrets. APA was ordered to pay EIT $35,000 for breach of contract. EIT filed certain post-trial motions, all of which were denied by the court. EIT did not appeal the verdict and this matter is concluded.

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

No matter was submitted to a vote of security holders during the fourth quarter of the fiscal year covered by this Report.

PART II

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

Our common stock is traded on The NASDAQ National Market under the symbol "APAT." The following table sets forth the quarterly high and low sales prices for our common stock for each quarter of the past two fiscal years as reported by NASDAQ.

Fiscal 2006	High	Low
Quarter ended June 30, 2005	$ 1.62	$ 1.20
Quarter ended September 30, 2005	1.48	1.18
Quarter ended December 31, 2005	1.35	1.10
Quarter ended March 31, 2006	2.01	1.17

Fiscal 2005	High	Low
Quarter ended June 30, 2004	$ 3.75	$ 2.22
Quarter ended September 30, 2004	2.28	1.37
Quarter ended December 31, 2004	2.48	1.37
Quarter ended March 31, 2005	2.21	1.36

There were approximately 329 holders of record of our common stock as of March 31, 2006.

We have never paid cash dividends on our common stock. The loan agreement relating to certain bonds issued by the South Dakota Economic Development Finance Authority restricts our ability to pay dividends.

ITEM 6. SELECTED FINANCIAL DATA.

	2006	2005	2004	2003	2002
Statements of Operations Data:					
Revenues	$ 15,717,837	$ 13,886,486	$ 11,909,465	$ 436,157	$ 595,955
Net loss	(3,348,848)	(3,420,038)	(6,535,147)	(5,009,434)	(4,738,199)
Net loss per share, basic and diluted	(.28)	(.29)	(.55)	(.42)	(.40)
Weighted average number of shares, basic and diluted	11,872,331	11,872,331	11,872,331	11,873,914	11,896,976
Balance Sheet Data:					
Total assets	$ 19,593,571	$ 22,074,014	$ 26,083,516	$ 31,884,526	$ 36,396,410
Long-term obligations, including current portion	1,360,961	1,578,836	1,811,759	2,173,682	2,461,363
Shareholders' equity	15,579,442	18,922,161	22,363,061	28,918,943	33,504,917

The above selected financial data should be read in conjunction with the financial statements and related notes included under Item 8 of this Report and "Management's Discussion and Analysis of Financial Condition and Results of Operations" appearing in Item 7 of this Report.

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

General

Optronics is, at present, engaged in designing, manufacturing, and marketing of various optoelectronic products, ultraviolet ("UV") detectors and related products. For the last several years our goal has been to manufacture and market products/components based on our technology developments. Previously, we focused on DWDM components for fiber optic communications and GaN based UV detectors (both components and integrated detector/electronic/display packages) because we believe that these two product areas have significant potential markets and because we have expertise and/or patent positions related to them. Optronics terminated the fiber optic communication activities at the end of fiscal year 2006.

APACN, which is a wholly owned subsidiary of APA Enterprises, is engaged in the design, manufacture, distribution, and marketing of a variety of fiber optics and copper components to the data communication and telecommunication industries. APACN's primary manufactured products include standard and custom fiber optic cable assemblies, copper cable assemblies, Outside Plant (OSP) cabinets, value-added fiber optics frames, panels and modules. APACN acquired certain assets of Americable on June 27, 2003. Several items discussed under the "Results of Operations" show significant changes from the comparable periods in the preceding fiscal year as a result of the acquisitions of Americable.

Application of Critical Accounting Policies

In preparing our consolidated financial statements, we make estimates, assumptions and judgments that can have a significant impact on our revenues, loss from operations and net loss, as well as on the value of certain assets and liabilities on our consolidated balance sheet. We believe that there are several accounting policies that are critical to an understanding of our historical and future performance, as these policies affect the reported amounts of revenues, expenses and significant estimates and judgments applied by management. While there are a number of accounting policies, methods and estimates affecting our consolidated financial statements, areas that are particularly significant include:

- Accounting for income taxes; and

- Valuation and evaluating impairment of long-lived assets and goodwill.

Accounting for Income Taxes

As part of the process of preparing our consolidated financial statements, we are required to estimate our income tax liability in each of the jurisdictions in which we do business. This process involves estimating our actual current tax expense together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities. We must then assess the likelihood that these deferred tax assets will be recovered from future taxable income and, to the extent we believe that recovery is not more likely than not or unknown, we must establish a valuation allowance.

Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our deferred tax assets. At March 31, 2006, we have recorded a full valuation allowance of $13,390,433 against our deferred tax assets, due to uncertainties related to our ability to utilize our deferred tax assets, consisting principally of certain net operating losses carried forward. The valuation allowance is based on our estimates of taxable income by jurisdiction and the period over which our deferred tax assets will be recoverable. The Company had U.S. federal and state net operating loss (NOL) carry forwards of approximately $33,782,000 which expire in fiscal years 2007 to 2026. To date the Company has not completed a section 382 analysis. If certain ownership changes occurred under section 382, there may be further limitations on the usage of the net operating loss carry forwards.

During the fourth quarter of fiscal year 2006, the Company recorded a deferred income tax liability of $272,000 for the book and income tax basis difference in goodwill on acquisitions.

Realization of the NOL carry forwards and other deferred tax temporary differences are contingent on future taxable earnings. The deferred tax asset was reviewed for expected utilization using a “more likely than not” approach as required by SFAS No. 109, “Accounting for Income Taxes,” by assessing the available positive and negative evidence surrounding its recoverability.

We will continue to assess and evaluate strategies that will enable the deferred tax asset, or portion thereof, to be utilized, and will reduce the valuation allowance appropriately at such time when it is determined that the “more likely than not” approach is satisfied.

Valuation and evaluating impairment of long-lived assets and goodwill

Goodwill represents the excess of the purchase price over the fair value of net assets acquired. Goodwill is not amortized, but reviewed for impairment annually or whenever conditions exist that indicate an impairment could exist. The Company performed the annual impairment test in fiscal years 2006, 2005 and 2004 and concluded that no impairment had occurred.

The Company evaluates the recoverability of its long-lived assets in accordance with SFAS 144, “Accounting for the Impairment or Disposal of Long-Lived Assets.” SFAS 144 requires recognition of impairment of long-lived assets in the event that events or circumstances indicate an impairment may have occurred and when the net book value of such assets exceeds the future undiscounted cash flows attributed to such assets. We assess the impairment of long-lived assets whenever events or changes in circumstances indicate that the carrying value may not be recoverable. No impairment of long-lived assets has occurred through the year ended March 31, 2006.

New Accounting Pronouncement

In December 2004, the Financial Accounting Standards Board (FASB) issued FASB Statement No. 123 (revised 2004)(SFAS 123R), *Share-Based Payment.* This statement requires the compensation cost relating to share-based payment transactions to be recognized in a company's financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. Statement 123(R) covers a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans. The Company will be required to apply Statement 123(R) effective April 1, 2006. For fiscal year 2007, management estimates the expense to be approximately $103,000.

Contractual Obligations

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

	Total	Less than 1 Year	1-3 years	4-5 years	After 5 years
Long-term debt (1)	$ 1,361	$ 1,343	$ 18	$ 0	$ 0
Operating leases	568	193	261	89	25
Total Contractual Cash Obligations	$ 1,929	$ 1,536	$ 279	$ 89	$ 25

(1) Includes fixed interest ranging from 0.62 to 10.00%.

Results of Operations

2006 Compared to 2005

REVENUES

Consolidated revenues for the fiscal year ended 2006 increased 13% to $15,718,000 from sales of $13,886,000 in 2005. Consolidated cost of sales decreased from 81% in 2005 to 78% in 2006 resulting in improved gross margin of $3,517,000 in 2006 as compared to $2,688,000 in 2005, an increase of 31%. Consolidated operating losses, however increased to $4,655,000 in 2006 compared to $3,795,000 in 2005. Consolidated net losses, however, decreased somewhat to $3,349,000 in 2006 or $.28 per diluted share compared to $3,420,000 or $.29 in 2005. The losses in fiscal 2006 were impacted by significantly increased legal expenses and non-operating activities related to the sale of Metal Organic Chemical Vapor Deposition (MOCVD) operations and a non-cash deferred tax liability related to goodwill on acquisitions. Increased legal expenses related to the defense of a lawsuit brought by EIT, a Virginia corporation, and a non-cash tax expense accrual related to goodwill were offset by a gain on the sale of Metal Organic Chemical Vapor Deposition (MOCVD) operations.

APACN's revenues for the year ended 2006 were $15,641,000 versus $13,801,000 in the year ended 2005, an increase of 13%. The increase is primarily attributable to an increased acceptance of the Company's products within the FTTH market resulting from increased sales and marketing activities during the fiscal year 2006. Sales to broadband service providers and commercial data networks, which include APACN custom fiber distribution systems, associated cable assemblies and optical components, were $10,488,000 or 67% of revenue. Sales to OEM's, consisting primarily of fiber optic and copper cable assemblies produced to customer design specifications, were $5,152,000, or 33% of revenue. This compares to 69% for broadband and commercial data networks and 31% for OEM's in the prior year. APACN's revenue growth is dependent upon capital expenditures in the communications equipment industry, our ability to develop and introduce new products, and our ability to acquire and retain business in a competitive industry. We expect sales at APACN in fiscal 2007 to continue to increase as a result of our investment in market development activities and the acceptance of the product line within our target customers.

Gross revenues at Optronics for the year ended 2006 were $400,000, compared to $489,000 in 2005, a decrease of 24%. Gross revenues reflect approximately $323,000 of sales to APACN for fiber optics products and subcontracted labor versus $404,000 last year. These sales are eliminated as intercompany sales in the consolidated financial statements. Sales of UV monitors were $39,000 versus $29,000 in the prior year period, and sales of foundry services were $60,000 in 2006 versus $41,000 in 2005. Optronics' revenue growth is dependent upon our ability to successfully establish manufacturing reliability for our GaN products and successful selling into our targeted market segments.

COST OF SALES AND GROSS PROFIT

APACN's gross profit for the year ended in 2006 was $4,195,000 as compared to $3,821,000 in 2005. Gross profit percent for APACN for the year ended March 31, 2006 was 27% versus 28% in the prior year. The decrease in margin percentage reflects continued downward price pressure. The company expects to experience continued downward price pressure throughout fiscal 2007 and is continuing on its ongoing program to reduce the cost of its products through a combination of product re-design, process improvement and global sourcing of components and outside manufacturing. We expect gross margin percentage for APACN in fiscal 2007 to be about the same as in fiscal 2006.

Optronic's net cost of sales for the year ended 2006 were $755,000 as compared to $1,218,000 in 2005. Personnel related expenses decreased approximately $250,000 due to staff reductions in our GaN product line and the termination of our Aberdeen manufacturing facility.

RESEARCH AND DEVELOPMENT EXPENSES

Research and development ("R&D") expenses consist solely of the research and development expense at Optronics. There have been no research and development expenses at APACN. R&D expenses increased by approximately $305,000, to $1,409,000 for the year ended March 31, 2006 as compared to $1,104,000 for the year ended March 31, 2005. This represents an increase of 28% from 2005. The majority of the increase reflects additional rental and depreciation costs associated with operating a semiconductor machine for the entire year fiscal year of 2006 as compared to only the last two quarters in fiscal 2005. We expect these R&D expenses to reduce significantly during fiscal 2007 due mainly to the sale of the operations of the semiconductor machine.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Consolidated selling, general and administration ("S, G & A") expenses increased approximately $1,384,000, or 26%, to $6,763,000 in 2006 from $5,379,000 in 2005.

S, G & A expenses at APACN were $4,248,000 for the year ending March 31, 2006 as compared to $3,487,000 in 2005, an increase of $761,000 or 22% mainly due to increased sales and marketing activities. As a percentage of revenue, we expect S, G & A expenses to be comparable in fiscal year 2007 to fiscal year 2006.

S, G & A expenses at Optronics increased $626,000 to $2,519,000 for the year ending March 31, 2006, from $1,893,000 in the prior period. The increase is mainly due to $443,000 increased legal costs primarily associated with the defense of a law suit from Electronic Instrumentation and Technology, Inc. (EIT), a Virginia corporation. We expect S, G, & A in fiscal 2007 to decrease significantly as compared to S, G & A in fiscal 2006.

GAIN ON DISPOSAL OF ASSETS (net)

Gains on disposal of assets at APACN were $4,000 in fiscal year ending March 31, 2006. There were no gains in the prior fiscal year.

Gains on disposal of assets at Optronics were $1,195,000 in fiscal year ended March 31, 2006 as compared to $209,000 in fiscal year ended March 31, 2005. A gain of approximately $1,163,000 was recognized on the sale of the MOCVD equipment and licensing of two patents during March 2006. In the prior fiscal year, the company realized a gain of approximately $196,000 on the sale of the optics product line in April 2004

OTHER INCOME AND EXPENSE

Other income at APACN increased approximately $114,000 to $122,000 in fiscal 2006 as compared to $8,000 in fiscal 2005. The difference is due mainly to significant contingent goodwill earn out of approximately $119,000, during fiscal year 2006, from Crescent Electric during the 3rd and final year of agreement acquired as a direct result of CSP acquisition. Other expense at APACN increased $83,000 to $386,000 for the year ending March 31, 2006 versus $303,000 in the prior year period. Interest expense increased $83,000 due to a higher debt balance outstanding and increasing interest rates over the year.

Other income at Optronics increased approximately $251,000 to $808,000 in fiscal 2006 from $557,000 in 2005. Interest income increased approximately $183,000 due mainly to higher interest income earned on cash equivalents. Other expenses increased approximately $69,000 to $160,000 from $91,000 in 2005, due mainly to the expenses related to the EIT judgment and write-down of fiber optic assets during the fiscal year 2006.

NET LOSS

Consolidated net loss decreased $71,000 to $3,349,000, or $.28 cents per share in fiscal 2006, as compared to a net loss of $3,420,000, or $.29 cents per share, in fiscal 2005.

Net loss for APACN for the year ending 2006 was $588,000 versus a profit of $36,000 in fiscal 2005. The increased losses during the fiscal 2006 were mainly due to the expansion of its sales and marketing activities and an accrual for taxes on goodwill.

Net loss for Optronics for the year ending 2006 was $2,760,000, a decrease of $696,000, or 20%, from $3,456,000 in 2005. The decreased losses are primarily the result of sale of its MOCVD operations and licensing of two patents.

2005 Compared to 2004

REVENUES

Consolidated revenues for the fiscal year ended 2005 increased 17% to $13,886,000 from sales of $11,909,000 in 2004. Consolidated cost of sales decreased to $11,198,000 in 2005 from $11,914,000 in 2004. Consolidated operating losses decreased to $3,795,000 in 2005 compared to $6,558,000 in 2004. Consolidated net losses decreased to $3,420,000 in 2005 or $.29 per diluted share compared to $6,535,000 or $.55 in 2004.

APACN's revenues for the year ended 2005 were $13,801,000 versus $11,691,000 in the year ended 2004, an increase of 18%. The increase is primarily attributable to higher revenues in the first quarter of fiscal 2005 generated by the acquisition of Americable, Inc., which occurred at the end of the first quarter of fiscal 2004. The Americable assets contributed no corresponding revenues for the first quarter of fiscal 2004. Sales to broadband service providers and commercial data networks, which include APACN custom fiber distribution systems, associated cable assemblies and optical components, were $9,483,000 or 69% of revenue. Sales to OEM's, consisting primarily of fiber optic and copper cable assemblies produced to customer design specifications, were $4,317,000, or 31% of revenue. This compares to 60% for broadband and commercial data networks and 40% for OEM's in the prior year. The change in mix is partially a result of an increased acceptance of the Company's products within the FTTH market, offset by lower demand from some OEM customers. APACN's revenue growth is dependent upon capital expenditures in the communications equipment industry, our ability to develop and introduce new products, and our ability to acquire and retain business in a competitive industry.

Gross revenues at Optronics for the year ended 2005 were $490,000, compared to $409,000 in 2004, an increase of 20%. Gross revenues reflect approximately $404,000 of sales to APACN for fiber optics products and subcontracted labor versus $191,000 last year. These sales are eliminated as intercompany sales in the consolidated financial statements. The Company had no sales of its optics products in 2005 versus $92,000 in the prior year due to the sale of that product line in April 2004. Sales of UV monitors were $28,000 versus $23,000 in the prior year period, and sales of foundry services were $41,000 in 2005. Optronics' revenue growth is dependent upon our ability to successfully establish manufacturing reliability for our GaN products and successful selling into our targeted market segments.

COST OF SALES AND GROSS PROFIT

APACN's gross profit for the year ended in 2005 was $3,821,000 as compared to $2,660,000 in 2004. The increase is due mainly to higher margins generated in the first quarter of fiscal 2005 generated by the acquisition of Americable assets. Gross profit percent for APACN for the year ended March 31, 2005 was 28% versus 23% in the prior year. The increase in margin percentage reflects reduced production costs, resulting from consolidating multiple facilities, and a focus on selling higher margin products.

Optronic's net cost of sales for the year ended 2005 were $1,218,000 as compared to $2,883,000 in 2004. Personnel related costs decreased approximately $780,000 due to staff reductions in response to demand and the sale of the optics product line in April 2004. In addition, inventory writeoffs decreased approximately $125,000 and other production expenses decreased approximately $140,000 due to cost reductions implemented in fiscal 2004 and 2005 in the optics and GaN product lines.

RESEARCH AND DEVELOPMENT EXPENSES

Research and development ("R&D") expenses consist solely of the research and development expense at Optronics. There have been no research and development expenses at APACN. R&D expenses increased by approximately $155,000, to $1,104,000 for the year ended March 31, 2005 as compared to $949,000 for the year ended March 31, 2004. This represents an increase of 16% from 2004. The majority of the increase reflects additional rental and depreciation costs associated with operating a semiconductor machine, beginning in the third quarter of fiscal 2005, as well as personnel costs associated with this start up and HFET development.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Consolidated selling, general and administration ("S, G & A") expenses decreased approximately $226,000, or 4%, to $5,379,000 in 2005 from $5,605,000 in 2004.

S, G & A expenses at APACN were $3,487,000 for the year ending March 31, 2005 as compared to $3,615,000 in 2004. The majority of the difference is attributable to expenses generated by the assets acquired from Americable which occurred at the end of the first quarter of fiscal 2004. Consolidation of facilities beginning in fiscal 2004 also contributed to lower costs in fiscal 2005.

S, G & A expenses at Optronics decreased $97,000 to $1,893,000 for the year ending March 31, 2005, from $1,990,000 in the prior period. The decrease is attributable to a reduction in personnel expense of $260,000 in 2005, which was offset in part by higher outside services in 2005 related to India development expenses, along with higher facility expenses in 2005 (which consists of facility expenses included in cost of sales in 2004 but reclassified as S, G, & A in 2005) as this portion of the facility is no longer used for manufacturing operations.

GAIN ON DISPOSAL OF ASSETS (net)

Gains on disposal of assets were only recognized at Optronics. These gains were $209,000 in fiscal year ended March 31, 2005. There were no gains recognized in the prior fiscal year. The company realized a gain of approximately $196,000 on the sale of the optics product line in April 2004.

OTHER INCOME AND EXPENSE

Other income at APACN decreased approximately $15,000 to $8,000 in fiscal 2005 as compared to $23,000 in fiscal 2004. The difference is due mainly to higher income for management fees earned in fiscal 2004 related to the CSP acquisition. Other expense at APACN decreased $9,000 to $303,000 for the year ending March 31, 2005 versus $312,000 in the prior year period. Interest expense increased $64,000 due to a higher debt balance outstanding over the year. That was offset by a reduction of $77,000 in asset disposal charges absorbed in the prior year.

Other income at Optronics increased approximately $127,000 to $557,000 in fiscal 2005 from $430,000 in 2004. Interest income increased approximately $100,000 due mainly to higher interest income earned on cash equivalents. In addition $39,000 in facility related rental was also generated due to the sale of the fiber optics product line in April 2004. Other expenses decreased approximately $24,000 to $91,000 from $115,000 in 2004, due mainly to the absence of expenses related to assets disposed of in the prior year.

NET LOSS

Consolidated net loss decreased $3,115,000 to $3,420,000, or $.29 cents per share, as compared to a net loss of $6,535,000, or $.55 cents per share, in fiscal 2004.

Net income for APACN for the year ending 2005 was $36,000 versus a loss of $1,245,000 in fiscal 2004. The income is due mainly to increased revenue, reduced duplicate and one time expenses, lower personnel costs and more efficient operations achieved in the consolidation of the CSP and Americable assets.

Net loss for Optronics for the year ending 2005 was $3,456,000, a decrease of $1,834,000, or 35%, from $5,290,000 in 2004. The decreased losses are primarily the result of lower personnel and production expenses from cost reduction efforts implemented in fiscal 2004 and 2005, combined with the gain on sale of the optics business and the related savings of expense related to that product line.

Liquidity and Capital Resources

As of March 31, 2006, our principal source of liquidity was our cash, cash equivalents and short-term investments, which totaled $8,948,000 compared to $10,813,000 at March 31, 2005.

We used $3,276,000 to fund operating activities during fiscal 2006 compared to $2,247,000 in fiscal 2005, and $5,596,000 in fiscal 2004. In all three years the largest use of cash in operating activities was the funding of the net losses. The net loss for fiscal 2006 decreased to $3,349,000 from $3,420,000 in fiscal 2005. The primary factor contributing to the decreased loss from fiscal 2005 to 2006 was the sale of the MOCVD equipment and licensing of two patents which was mostly negated by increased S, G&A costs. The primary factors contributing to the decreased loss from fiscal 2004 to 2005 were the profitable operations at APACN and reduced expenses at Optronics.

In fiscal 2006 we netted approximately $1,629,000 in positive cash flows from investing activities after accounting for the purchase of property and equipment of $428,000 and $2,057,000 proceeds from the sale of assets, including proceed of $1,900,000 of MOCVD equipment and licensing of two patents. In fiscal 2005 we used $249,000 in investing activities, including $49,000 used to purchase assets through APA Optronics (India) Private Limited (See Note B of Notes to the Consolidated Financial Statements included under Item 8 of this Report). We also invested $429,000 to purchase property and equipment, mainly for production equipment at Optronics. In fiscal 2004 we used $2,753,000 in investing activities including $1,960,000 used to purchase the assets of Americable. We also invested $786,000 to purchase property and equipment, mainly for the purchase of the MOCVD system

In fiscal 2006, we used $219,000 in financing activities, primarily to pay down long-term debt relating to our facility in Aberdeen, South Dakota. In fiscal 2005, we used $235,000 in financing activities, primarily to pay down long-term debt relating to our facility in Aberdeen, South Dakota. In fiscal 2004, we used $342,000 in financing activities primarily to pay down long-term debt relating to our facility in Aberdeen, South Dakota.

Construction of our manufacturing facility in Aberdeen utilized certain economic incentive programs offered by the State of South Dakota and the City of Aberdeen. At March 31, 2006, the total principal outstanding under bonds issued by the State of South Dakota was $1,320,000. Interest on the bonds ranges from 5.8% to 6.75%, and the bonds are due in various installments between 2005 and 2016. These bonds require compliance with certain financial covenants. We were out of compliance with these covenants during all of fiscal 2004, 2005 and 2006. For further information regarding these bonds, see Note I of Notes to the Consolidated Financial Statements included under Item 8 of this Report. On April 14, 2004 the Company sold its optics manufacturing operations, as discussed in Note C to the Consolidated Financial Statements included under Item 8 of this Report, to PNE, Inc. dba IRD. The terms of the sale required the Company to prepay $89,000 of a loan with the Aberdeen Development Corporation (“ADC”) in South Dakota and to accelerate the loan payment schedule to maturity in fiscal 2011 from 2016. In June 2005, the Company sold a portion of the land in Aberdeen acquired from ADC back to ADC in consideration of cancellation of the remaining $120,000 due on the loan. Accordingly, the loan from ADC is fully satisfied. See Note D to the Consolidated Financial Statements included under Item 8 of this Report.

Our capital requirements are dependent upon several factors, including market acceptance of our products, the timing and extent of new product introductions and delivery, and the costs of marketing and supporting our products on a worldwide basis. See “Item 1. Business.” Although we believe that our current cash, cash equivalents, and short-term investments will be sufficient to fund our operations for more than the next 12 months, we cannot assure you that we will not seek additional funds through public or private equity or debt financing or from other sources within this time frame, or that additional funding, if needed, will be available on terms acceptable to us, or at all. We may also consider the acquisition of, or evaluate investments in, products and businesses complementary to our business. Any acquisition or investment may require additional capital.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Our exposure to market risk for changes in interest rates relates primarily to our cash equivalents. 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. See "Cash and Equivalents" under Note A of the Consolidated Financial Statements.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

Quarterly Results of Operations. The following tables present our unaudited quarterly operating results for the eight quarters ended March 31, 2006:

Statement of Operations Data	Quarter Ended June 30, 2004[1]	Quarter Ended September 30, 2004	Quarter Ended December 31, 2004	Quarter Ended March 31, 2005
Net revenue	$ 3,687,718	$ 3,668,068	$ 3,305,299	$ 3,225,401
Gross profit	600,875	782,264	601,140	704,031
Net loss	(702,836)	(883,047)	(928,510)	(905,645)
Net loss per share, basic and diluted	$ (0.06)	$ (0.07)	$ (0.08)	$ (0.08)

Statement of Operations Data	Quarter Ended June 30, 2005	Quarter Ended September 30, 2005	Quarter Ended December 31, 2005	Quarter Ended March 31, 2006[2]
Net revenue	$ 3,512,563	$ 4,069,367	$ 4,379,192	$ 3,756,715
Gross profit	725,110	904,070	1,024,333	863,591
Net loss	(891,006)	(1,063,628)	(1,275,786)	(118,428)
Net loss per share, basic and diluted	$ (0.08)	$ (0.09)	$ (0.11)	$ (0.01)

(1) In January, 2004 the Company announced the discontinuance of optics manufacturing at its Blaine, Minnesota facility. The closure was the result of aggressive off-shore pricing and continued lower demand for this product line. The Company sold its optics manufacturing operations on April 14, 2004 for $220,000.

(2) During the fourth quarter of fiscal year 2006, the Company recorded a deferred income tax liability of $272,000 related to goodwill from acquisitions.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
APA Enterprises, Inc.

We have audited the accompanying consolidated balance sheets of APA Enterprises, Inc. and subsidiaries as of March 31, 2006 and 2005, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended March 31, 2006. These consolidated financial statements are the responsibility of the Com-pany's management. Our responsibility is to express an opinion on these consolidated financial state-ments based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assur-ance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal controls over financial reporting. Our audit included consideration of internal controls over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion of the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above pre-sent fairly, in all material respects, the consolidated financial position of APA Enterprises, Inc. and subsidiaries as of March 31, 2006 and 2005 and the consolidated results of their operations and their consolidated cash flows for each of the three years in the period ended March 31, 2006, in con-formity with accounting principles generally accepted in the United States of America.

/s/ Grant Thornton LLP

Minneapolis, Minnesota
May 12, 2006

APA Enterprises, Inc.

CONSOLIDATED BALANCE SHEETS

March 31,

ASSETS	2006	2005
CURRENT ASSETS		
Cash and cash equivalents	$ 8,947,777	$ 10,813,492
Accounts receivable, net of allowance for uncollectible accounts of $77,831 and $57,107 at March 31, 2006 and 2005	1,892,483	1,446,248
Inventories	1,836,843	1,270,653
Prepaid expenses	173,040	264,372
Bond reserve funds	126,385	131,548
Total current assets	12,976,528	13,926,313
PROPERTY, PLANT AND EQUIPMENT, net	2,623,412	3,946,998
OTHER ASSETS		
Bond reserve funds	343,241	337,091
Goodwill	3,422,511	3,422,511
Other	227,879	441,101
	3,993,631	4,200,703
	$ 19,593,571	$ 22,074,014

The accompanying notes are an integral part of these financial statements.

APA Enterprises, Inc.

CONSOLIDATED BALANCE SHEETS - Continued

March 31,

LIABILITIES AND SHAREHOLDERS' EQUITY	2006	2005
CURRENT LIABILITIES		
Current maturities of long-term debt	$ 1,342,481	$ 1,471,036
Accounts payable	1,353,828	814,005
Accrued compensation	815,046	568,950
Accrued expenses	211,840	190,062
Total current liabilities	3,723,195	3,044,053
LONG-TERM DEBT, net of current maturities	18,480	107,800
DEFERRED INCOME TAXES	272,454	-
Total liabilities	4,014,129	3,151,853
COMMITMENTS AND CONTINGENCIES	-	-
SHAREHOLDERS' EQUITY		
Undesignated shares, 4,999,500 authorized shares; no shares issued and outstanding	-	-
Preferred stock, $.01 par value; 500 authorized shares; no shares issued and outstanding	-	-
Common stock, $.01 par value; 50,000,000 authorized shares; 11,872,331 shares issued and outstanding at March 31, 2006 and 2005	118,723	118,723
Additional paid-in capital	51,966,213	51,960,084
Accumulated deficit	(36,505,494)	(33,156,646)
Total shareholders equity	15,579,442	18,922,161
	$ 19,593,571	$ 22,074,014

The accompanying notes are an integral part of these financial statements.

APA Enterprises, Inc.

CONSOLIDATED STATEMENTS OF OPERATIONS

Years ended March 31,

	2006	2005	2004
Revenues	$ 15,717,837	$ 13,886,486	$ 11,909,465
Cost of sales	12,200,733	11,198,176	11,914,050
Gross profit (loss)	3,517,104	2,688,310	(4,585)
Operating expenses			
Research and development	1,408,778	1,103,972	948,737
Selling, general and administrative	6,763,068	5,379,483	5,605,177
Gain on sale of assets (net)	(1,198,295)	(208,837)	-
	6,973,551	6,274,618	6,553,914
Loss from operations	(3,456,447)	(3,586,308)	(6,558,499)
Other income	547,878	275,661	225,719
Other expense	(164,708)	(105,253)	(200,314)
	383,170	170,408	25,405
Loss before income taxes	(3,073,277)	(3,415,900)	(6,533,094)
Income taxes	275,571	4,138	2,053
Net loss	$ (3,348,848)	$ (3,420,038)	$ (6,535,147)
Net loss per share			
Basic and diluted	$ (0.28)	$ (0.29)	$ (0.55)
Weighted average shares outstanding			
Basic and diluted	11,872,331	11,872,331	11,872,331

The accompanying notes are an integral part of these financial statements.

APA Enterprises, Inc.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

Years ended March 31,

	Undesignated shares	Preferred stock		Common stock		Additional paid-in capital	Accumulated deficit	Total shareholders' equity
		Shares	Amount	Shares	Amount			
Balance at March 31, 2003	-	-	$ -	11,872,331	$ 118,723	$ 52,001,681	$ (23,201,461)	$ 28,918,943
Options issued as compensation	-	-	-	-	-	(20,735)	-	(20,735)
Net loss	-	-	-	-	-	-	(6,535,147)	(6,535,147)
Balance at March 31, 2004	-	-	-	11,872,331	118,723	51,980,946	(29,736,608)	22,363,061
Options issued as compensation	-	-	-	-	-	(20,862)	-	(20,862)
Net loss	-	-	-	-	-	-	(3,420,038)	(3,420,038)
Balance at March 31, 2005	-	-	-	11,872,331	$ 118,723	$ 51,960,084	$ (33,156,646)	$ 18,922,161
Change in options issued as compensation	-	-	-	-	-	6,129	-	6,129
Net loss	-	-	-	-	-	-	(3,348,848)	(3,348,848)
Balance at March 31, 2006	-	-	$ -	11,872,331	$ 118,723	$ 51,966,213	$ (36,505,494)	$ 15,579,442

The accompanying notes are an integral part of these financial statements.

APA Enterprises, Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended March 31,

	2006	2005	2004
Cash flows from operating activities:			
Net loss	$ (3,348,848)	$ (3,420,038)	$ (6,535,147)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities, net of acquisitions:			
Depreciation and amortization	1,061,199	1,003,573	971,194
Deferred tax liability	272,454	-	-
Gain on sale of assets	(1,198,295)	(208,837)	-
Compensation expense	6,129	(20,862)	(20,735)
Changes in operating assets and liabilities, net of acquisitions:			
Accounts receivable, net	(446,235)	341,293	(678,686)
Inventories	(566,190)	303,535	(179,293)
Prepaid expenses and other assets	136,111	(134,910)	(44,909)
Accounts payable and accrued expenses	807,697	(110,679)	891,795
Net cash used in operating activities	(3,275,978)	(2,246,925)	(5,595,781)
Cash flows from investing activities:			
Purchases of property and equipment	(427,631)	(429,457)	(785,870)
Proceeds from sale of assets	1,936,756	229,000	-
Cash paid for business acquisitions	-	(48,772)	(1,960,000)
Other	-	-	(7,376)
Net cash provided by (used in) investing activities	1,509,125	(249,229)	(2,753,246)
Cash flows from financing activities:			
Payment of long-term debt	(97,875)	(232,923)	(361,923)
Bond reserve funds	(987)	(2,341)	20,174
Net cash used in financing activities	(98,862)	(235,264)	(341,749)
Decrease in cash and cash equivalents	(1,865,715)	(2,731,418)	(8,690,776)
Cash and cash equivalents at beginning of year	10,813,492	13,544,910	22,235,686
Cash and cash equivalents at end of year	$ 8,947,777	$ 10,813,492	$ 13,544,910
Supplemental cash flow information:			
Cash paid during the year for:			
Interest	$ 90,816	$ 99,337	$ 109,251
Income taxes	3,117	4,138	2,053
Noncash investing and financing transactions:			
Debt relieved in exchange for land	$ 120,000	$ -	$ -
Capital expenditure included in accounts payable	$ -	$ -	$ 225,000

The accompanying notes are an integral part of these financial statements.

APA Enterprises, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2006, 2005 and 2004

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Business

APA Enterprises, Inc., formerly APA Optics, Inc., (the Company) is a manufacturer of custom cable assemblies and supplier of premise cabling components and networking products to customers throughout the United States with a concentration in Minnesota. The Company also manufactures and markets a range of gallium nitride-based devices.

Principles of Consolidation

The consolidated financial statements include the accounts of APA Enterprises, Inc. and its wholly-owned subsidiaries. All significant inter-company accounts and transactions have been eliminated in consolidation.

Foreign Currency Translation

The Company uses the United States dollar as its functional currency for its subsidiary in India. India's financial statements were translated into U.S. Dollars at the year end exchange rate, while income and expenses are translated at the average exchange rates during the year. There was no significant foreign exchange translation gain or losses during fiscal years ended March 31, 2006 and 2005. There were no foreign currency operations during fiscal year ended March 31, 2004.

Revenue Recognition

Revenue is recognized when persuasive evidence of an arrangement exists, the product has been delivered, the fee is fixed, acceptance by the customer is reasonably certain and collection is probable.

Cash and Cash Equivalents

The Company considers all highly liquid investments with original maturities of three months or less to be cash equivalents. Investments classified as cash equivalents at March 31, 2006 and 2005 consist entirely of short-term money market accounts. Cash equivalents are stated at cost, which approximates fair value.

Cash of approximately $104,000 and $145,000 was on deposit in foreign financial institutions at March 31, 2006 and 2005. The Company maintains cash balances at several financial institutions, and at times, such balances exceed insured limits. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Accounts Receivable

Credit is extended based on the evaluation of a customer's financial condition and, generally, collateral is not required. Accounts outstanding longer than the contractual payment terms are considered past due. The Company determines its allowance by considering a number of factors, including the length of time trade receivables are past due, the Company's previous loss history, the customer's current ability to pay its obligation to the Company, and the condition of the general economy and the industry as whole. The Company writes off accounts receivable when they become uncollectible; payments subsequently received on such receivables are credited to the allowance for doubtful accounts.

Inventories

Inventories consist of finished goods, raw materials and work in process and are stated at the lower of average cost (which approximates the first-in, first-out method) or market. Cost is determined using material costs, labor charges, and allocated factory overhead charges.

Property, Plant and Equipment

Property, plant and equipment are stated at cost, less accumulated depreciation and amortiza-tion. Depreciation and amortization are provided on the straight-line method for book and tax purposes over the follow-ing estimated useful lives of the assets:

	Years
Building	20
Equipment	3 - 7
Leasehold improvements	7 - 10 or life of lease

Goodwill

Goodwill represents the excess of the purchase price over net assets acquired. Goodwill is not amortized. Goodwill is tested for impairment annually or whenever conditions exist that indicate an impairment could exist. The Company performed the annual impairment test in fiscal years 2006 and 2005 and concluded that no impairment had occurred.

Stock-Based Compensation

The Company has various incentive and non-qualified stock option plans which are used as an incentive for directors, officers, and other employees, as described more fully in Note N. The Company uses the intrinsic value method to value stock options issued to employees. Under this method, compensation expense is recognized for the amount by which the market price of the common stock on the date of grant exceeds the exercise price. The Company's stock based compensation income also reflects the benefit of the cancellation of previously unvested expensed options. The Company rec-ognized compensation expense of $6,129 for the year ended March 31, 2006 and compensation income of $20,862 and $20,735 for the years ended March 31, 2005 and 2004. For those stock options granted where the exercise price was equal to the market value of the underlying common stock on the date of grant, no stock-based employee compensation cost is reflected in the net loss. Had the fair value method been applied, our compensation expense would have been different. The following table illustrates the effect on net loss and net loss per share if the Company had applied the fair value method, to stock-based employee compensation for the following fiscal years:

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

	March 31, 2006	March 31, 2005	March 31, 2004
Net loss to common shareholders - as reported	$ (3,348,848)	$ (3,420,038)	$ (6,535,147)
Less: Total stock-based employee compensation expense determined under fair value method for all awards, net of related tax effects	108,472	129,914	158,936
Net loss - pro forma	$ (3,457,320)	$ (3,549,952)	$ (6,694,083)
Basic and diluted net loss per common share - as reported	$ (.28)	$ (.29)	$ (.55)
Basic and diluted net loss per common share - pro forma	$ (.29)	$ (.30)	$ (.56)

The weighted average fair value of options granted in 2006, 2005 and 2004 was $1.39, $1.79, and $2.62. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions used for grants in 2006, 2005 and 2004; zero dividend yield, risk-free interest rate of 3.9%, 3.4% and 3.3%; volatility of 75%, 75% and 75%, and a weighted-average expected term of the options of five years. No adjustment was made to the Black Scholes calculation to reflect that the options are not freely traded.

Fair Value of Financial Instruments

Due to their short-term nature, the carrying value of current financial assets and liabilities approximates their fair values. The fair value of long-term obligations, if recalculated based on current interest rates, would not significantly differ from the recorded amounts.

Net Loss Per Share

Basic net loss per share is computed by dividing net loss by the weighted average number of common shares outstanding. Diluted net loss per share is computed by dividing net loss by the weighted average number of common shares outstanding and common share equivalents related to stock options and warrants, when dilutive.

Common stock options and warrants to purchase 633,780, 683,361 and 975,937 shares of com-mon stock with a weighted average exercise price of $2.96, $4.99 and $6.35 were out-standing during the years ended March 31, 2006, 2005 and 2004, but were excluded from the calculation of net loss per share because they were antidilutive. Had we not incurred net losses during the fiscal years ended March 31, 2006, 2005 and 2004, we would not have assumed any conversion of stock options in fiscal 2006 and 2005, and we would have assumed conversion of stock options into 18,031 common shares in fiscal 2004.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assump-tions that affect the reported amounts of assets and liabilities, related revenues and expenses and disclo-sure about contingent assets and liabilities at the date of the financial statements. Actual results may differ from those estimates used by management.

Impairment of Long-Lived Assets

The Company evaluates the recoverability of its long-lived assets and requires recognition of impairment of long-lived assets if events or circumstances indicate an impairment may have occurred and when the net book value of such assets exceeds the future undiscounted cash flows attributed to such assets. The Company assesses the impairment of long-lived assets whenever events or changes in circumstances indicate that the carrying value may not be recoverable. No impairment of long-lived assets has occurred through the year ended March 31, 2006.

Income Taxes

The Company records income taxes in accordance with the liability method of accounting. Deferred taxes are recognized for the estimated taxes ultimately payable or recoverable based on enacted tax law. The Company establishes a valuation allowance to reduce the deferred tax asset to an amount that is more likely than not to be realizable. Changes in tax rates are reflected in the tax provision as they occur.

Reclassifications

Certain reclassifications have been made to the 2005 financial statements to conform with the presentation used in 2006. These reclassifications had no effect on net loss or shareholders' equity as previously reported.

Newly Adopted Accounting Standards

In December 2004, the Financial Accounting Standards Board (FASB) issued FASB Statement No. 123 (revised 2004) (SFAS 123R), *Share-Based Payment.* This statement requires the compensation cost relating to share-based payment transactions to be recognized in a company's financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. Statement 123(R) covers a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans. The Company will be required to apply Statement 123(R) effective April 1, 2006. For fiscal year 2007, management estimates the expense to be approximately $103,000.

NOTE B - ACQUISITIONS

Americable, Inc.

On June 27, 2003, the Company acquired certain assets of Americable, Inc. The acquisition was accounted for as a purchase and, accordingly, results of operations relating to the purchased assets have been included in the statement of operations from the date of acquisition. There are no contingent payments related to the acquisition.

NOTE B - ACQUISITIONS - Continued

In accordance with SFAS 141, the Company reclassified certain balances from the original Americable purchase price allocation as part of an asset valuation adjustment. The adjustment was made after determining the fair value of the assets purchased. The result of the change was a decrease in inventory and property, an increase in accounts receivable, and an increase in goodwill recorded. This did not change the purchase price of the transaction. The purchase price and assets acquired with purchase price adjustments are as follows:

	Original Purchase Price Allocation	Purchase Price Adjustment	Net Purchase Price Allocation
Accounts receivable	$ 594,000	$ 46,279	$ 640,279
Inventory	638,000	(13,944)	624,056
Property, plant and equipment	450,000	(49,186)	400,814
Assets purchased	1,682,000	(16,851)	1,665,149
Goodwill	278,000	16,851	294,851
Purchase price	$ 1,960,000	$ -	$ 1,960,000

Goodwill is expected to be fully deductible for tax purposes.

NOTE C - SALE OF OPTICS MANUFACTURING OPERATIONS

In January, 2004 the Company announced the discontinuance of optics manufacturing at its Blaine, Minnesota facility. The closure was the result of aggressive off-shore pricing and continued lower demand for this product line. This resulted in a charge of $171,000 taken in the 4th quarter ended March 31, 2004. The Company sold its optics manufacturing operations on April 14, 2004 for $220,000. The terms of the sale required the Company to restructure a loan with the City of Aberdeen, South Dakota, which included an upfront loan payment of $89,305 and payment of the remaining $140,000 loan amount in seven annual installments of $20,000 each beginning June 30, 2004. The Company recorded a gain of approximately $208,000 on the sale in the first quarter of fiscal 2005.

NOTE D - SALE OF LAND

In June 2005 the Company sold approximately 2 acres of its land in Aberdeen, South Dakota to the Aberdeen Development Corporation (ADC) in exchange for the retirement of its remaining $120,000 debt on its loan with ADC. The land was granted to APA in conjunction with building a facility in Aberdeen and is part of a single parcel of approximately 12 acres on which the Company has constructed and operates its manufacturing facility. The Company recognized a gain of approximately $109,000 on the sale of the land in the first quarter of fiscal 2006.

NOTE E - CLOSING OF THE ABERDEEN FACILITY

The Company ceased all of its operations during the later part of fiscal year 2006 as a part of its consolidation of manufacturing operations. The Company owned facility, located approximately on a 10-acre parcel, is designated for lease or sale after sub-division of the land in approximately two 5-acre parcels. The Company does not have a formal plan for leasing or selling the facility and thus the building remains classified as property, plant and equipment as of March 31, 2006. The company plans to retain the 5-acre vacant land for potential future use. The facility, built using proceeds from a South Dakota assisted bond, currently has a long-term debt balance of approximately $1.0 Million, after adjusting the proceeds from the reserve funds. Note I provides more detailed financial information about the long-term debt and reserve funds.

NOTE F - SALE OF METAL ORGANIC CHEMICAL VAPOR DEPOSITION (MOCVD) OPERATIONS

In March, 2006 the Company sold certain equipment and related intellectual property related to its MOCVD operations to an unrelated party for a total consideration of $1.9 million in cash and a license back of the technology within a specified field of use. The asset purchase agreement includes an additional consulting agreement for up to $100,000 over the course of one year. The company recorded a gain of approximately $1.2 million on the sale in the fourth quarter of fiscal 2006. The company does not track discrete financial information, therefore this has not been presented as a discontinued operation.

NOTE G - INVENTORIES

Inventories consist of the following at March 31:

	2006	2005
Raw materials	$ 429,954	$ 266,051
Work-in-process	48,474	9,661
Finished goods	1,358,415	994,941
	$ 1,836,843	$ 1,270,653

NOTE H - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consist of the following at March 31:

	2006	2005
Land	$ 116,195	$ 127,760
Buildings	1,809,881	1,682,205
Manufacturing equipment	4,802,514	5,895,170
Office equipment	863,131	699,839
Vehicles	10,648	-
Leasehold improvements	1,135,728	1,132,651
	8,738,097	9,537,625
Less accumulated depreciation and amortization	6,114,685	5,590,627
	$ 2,623,412	$ 3,946,998

NOTE I - LONG-TERM DEBT

The following is a summary of the outstanding debt at March 31:

	2006	2005
South Dakota Governor's Office of Economic Development and the Aberdeen Development Corporation Bond, 5.8% to 6.75%, due in various installments through 2016	$ 1,320,000	$ 1,405,000
Low interest economic development loans, 0%, due in various installments through fiscal 2011	-	120,000
Other	40,961	53,836
	1,360,961	1,578,836
Less current maturities	1,342,481	1,471,036
	$ 18,480	$ 107,800

At March 31, 2006 and 2005, the Company had on deposit with trustees $469,626 and $468,639 in reserve funds for bond maturities, of which $126,385 and $131,548 are for current bond maturities. These funds are included in bond reserve funds in the accompanying balance sheets.

The loan agreement requires the Company to maintain compliance with certain cove-nants. The Company was out of compliance with certain of these covenants in fiscal 2006. All debt, except for other long term debt, has been classified as current due to the Company's covenant violation.
All of the above debt is secured by land, buildings, and certain equipment of the Company.

Scheduled maturities of the Company's long-term debt are as follows:

Years ending March 31,	
2007	$ 1,342,481
2008	14,773
2009	3,707
	$ 1,360,961

NOTE J - EMPLOYEE BENEFIT PLAN

The Company maintains a contributory 401(k) profit sharing benefit plan covering all employ-ees. The Company matches 50% of the first 6% of the employee's salary that was contributed by the employee to the plan. The Company's contributions under this plan were $114,000, $97,000, and $72,000 for the years ended March 31, 2006, 2005 and 2004.

NOTE K - INCOME TAXES

Deferred taxes recognize the impact of temporary differences between the amounts of the assets and liabilities recorded for financial statement purposes and such amount measured in accordance with tax laws. Realization of net operating loss carry forward and other deferred tax temporary differences are contingent upon future taxable earnings. The Company's deferred tax asset was reviewed for expected utilization using a "more likely than not" approach as required by SFAS 109 by assessing the available positive and negative factors surrounding its recoverability. Accordingly, the Company has recorded a full valuation allowance at March 31, 2006 and 2005.

Significant components of deferred income tax assets and liabilities are as follows at March 31:

	2006	2005
Current deferred income tax assets:		
Inventories	$ 160,129	$ 116,156
Accrued expenses	194,841	163,338
	354,970	279,494
Long-term deferred income tax asset:		
Intangibles	12,766	33,130
Net operating loss carryforward	13,173,801	12,296,918
	13,186,567	12,330,048
Total deferred income tax assets	13,541,537	12,609,542
Long-term deferred income tax liabilities:		
Property and equipment depreciation	151,104	288,639
Goodwill	272,454	153,696
	423,558	442,335
Total net deferred income taxes	13,117,979	12,167,207
Valuation allowance	(13,390,433)	(12,167,207)
Total	$ (272,454)	$ -

As of March 31, 2006, the Company has net operating loss carry forwards for federal and state income tax purposes of approximately $33,782,000 which expire in fiscal years 2007 to 2026. To date the Company has not completed a Section 382 analysis. If certain ownership changes occurred under Section 382, there may be further limitations on the usage of the net operating loss carry forwards.

The following is a reconciliation of the federal statutory income tax rate to the consolidated effective tax rate for March 31:

	Percent of Pre-tax Income		
	2006	2005	2004
Federal statutory rate	(34%)	(34%)	(34%)
State income taxes	(5%)	(5%)	(5%)
Permanent differences	7%	1%	0%
Other	1%	0%	0%
Change in valuation allowance	40%	38%	39%
Tax Rate	9%	0%	0%

NOTE K - INCOME TAXES - Continued

Components of the (benefit) provision for income taxes are as follows for the years ended March 31:

	2006	2005	2004
Current:			
Federal	$ 272,454	$ -	$ -
State	3,117	4,138	2,053
Deferred:			
Federal	1,064,207	869,866	2,106,637
State	159,019	127,921	309,799
Valuation allowance	(1,223,226)	(997,787)	(2,416,436)
Income tax expense	$ 275,571	$ 4,138	$ 2,053

During the fourth quarter of fiscal year 2006, the Company recorded a $272,000 deferred income tax liability for the book and income tax basis difference in goodwill. Income tax expense consists primarily of state taxes in 2005 and 2004.

On June 1, 2006, the Treasury issued final regulations concerning the deduction for income attributable to domestic production activities under Section 199. Section 199 was enacted as part of the American Jobs Creation Act of 2004. The company examined the effect of these regulations and concluded the impact to be immaterial until all net operating losses have been fully utilized.

NOTE L - SHAREHOLDERS' EQUITY

The Board of Directors may, by resolution, establish from the undesignated shares different classes or series of shares and may fix the relative rights and preferences of shares in any class or series. The Company is authorized to issue 500 shares of preferred stock and 50,000,000 shares of common stock at $.01 par value. The Company has not issued any shares of preferred stock.

NOTE M - SHAREHOLDER RIGHTS PLAN

Pursuant to the Shareholder Rights Plan each share of com-mon stock has attached to it a right, and each share of common stock issued in the future will have a right attached until the rights expire or are redeemed. Upon the occurrence of certain change in control events, each right entitles the holder to purchase one one-hundredth of a share of Series B Junior Preferred Participating Share, at an exercise price of $80 per share, subject to adjustment. The rights expire on November 10, 2010 and may be redeemed by the Company at a price of $.001 per right prior to the time they become exercisable.

NOTE N - STOCK OPTIONS AND WARRANTS

Stock Options

The Company has various incentive and non-qualified stock option plans which are used as an incentive for directors, officers, and other employees. Options are generally granted at fair market values determined on the date of grant and vesting normally occurs over a six-year period. The plans had 673,530 shares of common stock available for issue at March 31, 2006.

Option transactions under these plans during the three years ended March 31, 2006 are summa-rized as follows:

	Number of shares	Weighted average exercise price
Outstanding at March 31, 2003	408,375	$4.27
Granted	140,000	2.62
Canceled	(163,260)	5.65
Outstanding at March 31, 2004	385,115	3.74
Granted	72,000	1.79
Canceled	(220,485)	3.60
Outstanding at March 31, 2005	236,630	3.28
Granted	65,000	1.39
Cancelled	(25,160)	3.75
Outstanding at March 31, 2006	276,470	2.80

The number of shares exercisable at March 31, 2006, 2005 and 2004 was 113,510, 72,255, and 176,815, respectively, at a weighted average exercise price of $3.83, $4.47, and $4.21 per share, respectively.

The following table summarizes information concerning currently outstanding and exercisable stock options at March 31, 2006:

	Options outstanding			Options exercisable	
Range of exercise prices	Number outstanding	Weighted average remaining contractual life	Weighted average exercise price	Number outstanding	Weighted average exercise price
$1.30-$2.91	236,470	3.93 years	$ 1.99	78,510	$ 2.23
5.53-8.90	40,000	0.94 years	7.55	35,000	6.49
	276,470	3.50 years	2.80	113,510	3.83

NOTE N - STOCK OPTIONS AND WARRANTS - Continued

Stock Warrants

The following is a table of the warrants to purchase shares of the Company's common stock:

	Warrants outstanding	Exercise price per share	Expiration date
Balance at March 31, 2003	590,822	$ 3.00 - 17.84	2005 - 2008
Issued	-	-	-
Expired	-	-	-
Balance at March 31, 2004	590,822	3.00 -17.84	2005 - 2008
Issued	-	-	-
Expired	(144,091)	14.72	2005
Balance at March 31, 2005	446,731	3.00 - 17.84	2006 - 2008
Issued	-	-	-
Expired	(89,421)	$ 6.00-17.84	2006
Balance at March 31, 2006	357,310	3.00-7.00	2007-2008

All warrants are exercisable upon date of grant.

NOTE O - COMMITMENTS

The Company leases office and manufacturing facilities from a partnership whose two partners are major shareholders, officers and directors of the Company. The Company has determined FIN 46 (R), *Consolidation of Variable Interest Entities* (VIE's), does not require the consolidation of the partnership with APA's financial statements. The lease agreement, classified as an operating lease, expires November 30, 2009 and provides for periodic increases of the rental rate based on increases in the consumer price index. Rental expense was $585,000, $478,000 and $485,000 for the years ended March 31, 2006, 2005 and 2004, of which $160,000, $155,000 and $149,000 was paid to the partnership, respectively.

The following is a schedule of approximate minimum payments required under the capital and operating leases:

Year ending March 31	Operating leases
2007	$ 193,354
2008	133,402
2009	128,022
2010	86,190
2011	2,526
Thereafter	25,260
Total minimum lease payments	$ 568,754

NOTE P - CONCENTRATIONS

Suppliers

The Company purchases raw materials, component parts and outsourced labor from many suppliers. Although many of these items are single-sourced, the Company has experienced no significant difficulties to date in obtaining adequate quantities. These circumstances could change, however, and the Company cannot guarantee that sufficient quantities or quality of raw materials, component parts and outsourced labor will be as readily available in the future or, if available, that we will be able to obtain them at favorable prices.

NOTE Q - SEGMENTS OF BUSINESS

The Company has identified two reportable segments based on its internal organizational structure, management of operations, and performance evaluation. These segments are Optronics and Cables and Networks (APACN). Optronic's revenue is generated in the design, manufacture and marketing of ultraviolet (UV) detection and measurement devices. APACN's revenue is derived primarily from standard and custom fiber optic cable assemblies, copper cable assemblies, value added fiber optics frames, panels and modules. Expenses are allocated between the companies based on detailed information contained in invoices. In addition, corporate overhead costs for management's time and other expenses are allocated to each segment. Segment detail is summarized as follows (unaudited, in thousands):

	Optronics	Cables & Networks	Eliminations	Consolidated
Year ended March 31, 2006				
External sales	$ 400	$ 15,641	$ (323)	$ 15,718
Gross profit (loss)	(674)	4,195	(4)	3,517
Operating loss	(3,407)	(49)	-	(3,456)
Depreciation and amortization	798	263	-	1,061
Capital expenditures	289	138	-	427
Assets	19,333	7,879	(7,618)	19,594
Year ended March 31, 2005				
External sales	$ 489	$ 13,801	$ (404)	$ 13,886
Gross profit (loss)	(1,133)	3,821	-	2,688
Operating profit (loss)	(3,920)	334	-	(3,586)
Depreciation and amortization	774	230	-	1,004
Capital expenditures	397	79	-	476
Assets	22,253	7,188	(7,367)	22,074
Year ended March 31, 2004				
External sales	$ 409	$ 11,691	$ (191)	$ 11,909
Gross profit (loss)	(2,665)	2,660	-	(5)
Operating loss	(5,604)	(955)	-	(6,559)
Depreciation and amortization	797	174	-	971
Capital expenditures	695	91	-	786
Assets	26,187	7,310	(7,413)	26,084

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None.

ITEM 9A. CONTROLS AND PROCEDURES.

The Company's chief executive officer and chief financial officer (the same person) has evaluated the Company's disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e) as of the end of the period covered by this report, and based on such evaluation has concluded that they are effective.

During the fiscal quarter ended March 31, 2006, there was no change in the Company's internal controls over financial reporting that materially affected, or is reasonably likely to materially affect, the Company's controls over financial reporting.

ITEM 9B. OTHER INFORMATION

There were no events during the quarter ended March 31, 2006 required to be disclosed on Form 8-K which were not so disclosed.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.

Information regarding executive officers is included in Part I of this Report and is incorporated in this Item 10 by reference.

Information regarding directors and the information required by Items 11, and 13, below, is incorporated in this Report by reference to the proxy statement for our annual meeting of shareholders to be held in August 2006.

ITEM 11. EXECUTIVE COMPENSATION.

Information required by Item 11 is incorporated in this Report by reference to the proxy statement for our annual meeting of shareholders to be held in August 2006.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS.

Certain information required by Item 12 is incorporated in this Report by reference to the proxy statement for annual meeting of shareholders to be held in August 2006.

The following table provides information about the Company's equity compensation plans (including individual compensation arrangements) as of March 31, 2006.

	(a)	(b)	(c)
Plan category	Number of securities to be issued upon exercise of options, warrants or rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders	276,470	$2.80	673,530
Equity compensation plans not approved by security holders	357,310	$3.08	Not applicable*
Total	633,780	$2.96	673,530

* These securities are comprised solely of warrants that were not issued pursuant to any formal plan with an authorized number of securities available for issuance.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

Information required by Item 13 is incorporated in this Report by reference to the proxy statement for our annual meeting of shareholders to be held in August 2006.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Information required by Item 14 is incorporated in this Report by reference to the proxy statement for our annual meeting of shareholders to be held in August 2006.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.

(a) (1) The following financial statements are filed herewith under Item 8.

(2) Financial Statement Schedules: See Schedule II on page following signatures.

(b) Exhibits. See Exhibit Index.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

APA Enterprises, Inc.

Date: June 28, 2006

By /s/ Anil K. Jain
Anil K. Jain
President and Chief Executive Officer

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

Signature	**Title**	**Date**
/s/ Anil K. Jain Anil K. Jain	President, Chief Executive Officer, Chief Financial Officer and Director (principal executive officer and principal financial officer)	June 28 , 2006
/s/ Chris M. Goettl Chris M. Goettl	Controller	June 28 , 2006
/s/ John G. Reddan John G. Reddan	Director	June 28 , 2006
/s/ Ronald G. Roth Ronald G. Roth	Director	June 28, 2006
/s/ Stephen L. Zuckerman MD Stephen L. Zuckerman	Director	June 28, 2006

SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS

Description	Balance at Beginning of Period	Additions: Charged to: Cost and Expenses	Additions: Charged to: Other Accounts	Deductions	Balance at End of Period
Allowance for doubtful accounts					
March 31, 2006	$ 57,107	$ 18,000	$ 6,121 (1)	$ 3,397 (2)	$ 77,831
March 31, 2005	49,038	33,000	10,692 (1)	35,623 (2)	57,107
March 31, 2004	20,644	31,500	2,562 (1)	5,668 (2)	49,038

(1) Represents recovery of bad debt and other adjustments
(2) Represents writeoffs of bad debt

REPORT OF INDEPENDENT REGISTERED CERTIFIED

PUBLIC ACCOUNTING FIRM ON SCHEDULE

To the Board of Directors and Shareholders

APA Enterprises, Inc.

We have audited in accordance with the standards of the Public Company Accounting Oversight Board (United States) the consolidated financial statements of APA Enterprises, Inc. and subsidiaries referred to in our report dated May 12, 2006, which is included in the annual report to security holders. Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying Schedule II is presented for purposes of complying with the rules of the Securities and Exchange Commission and is not a required part of the basic financial statements. This schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, fairly states in all material respects the financial data required to be set forth therein, in relation to the basic financial statements taken as a whole.

/s/ GRANT THORNTON LLP

Minneapolis, Minnesota

May 12, 2006

EXHIBIT INDEX

Number	Description	Page Number or Incorporated by Reference to
2.1	Asset Purchase Agreement between APACN and CSP, Inc.	Exhibit 2.1 to Form 8-K filed March 31, 2003
2.1	Asset Purchase Agreement between APACN and Americable, Inc.	Exhibit 2.1 to Form 8-K filed July 2, 2003
2.2	Agreement Not to Compete with Peter Lee as part of CSP asset purchase	Exhibit 2.2 to Form 8-K filed March 31, 2003
2.3	Asset Purchase Agreement between APA Enterprises, Inc. and Software Moguls India Private Limited and S M Infoexpert Private Limited	Exhibit 2.3 to Registrant's Report on Form 10-K for the fiscal year ended March 31, 2005
3.1	Restated Articles of Incorporation, as amended to date	Exhibit 3.1 to Registrant's Report on Form 10-Q for the quarter ended September 30, 2000
3.1 (a)	Restated Articles of Incorporation, as amended to date thru August 25, 2004	Exhibit 3.1 to Registrant's Report on Form 10-Q for the quarter ended September 30, 2004
3.2	Bylaws, as amended and restated to date	Exhibit 3.2 to Registrant's Report on Form 10-KSB for the fiscal year ended March 31, 1999
4.1(a)	State of South Dakota Board of Economic Development $300,000 Promissory Note, REDI Loan: 95-13-A	Exhibit 4.1(a) to the Report on 10-QSB for the quarter ended June 30, 1996 (the "June 1996 10-QSB")
4.1(b)	State of South Dakota Board of Economic Development Security Agreement REDI Loan No: 95-13-A dated May 28, 1996	Exhibit 4.1(b) to the June 1996 10-QSB
4.2(a)	$700,000 Loan Agreement dated June 24, 1996 by and between Aberdeen Development Corporation and APA Enterprises, Inc.	Exhibit 4.2(a) to the June 1996 10-QSB
4.2(b)	$300,000 Loan Agreement dated June 24, 1996 between Aberdeen Development Corporation and APA Enterprises, Inc.	Exhibit 4.2(b) to the June 1996 10-QSB
4.2(c)	$250,000 Loan Agreement dated June 24, 1996 by and between Aberdeen Development Corporation and APA Enterprises, Inc.	Exhibit 4.2(c) to the June 1996 10-QSB

Number	Description	Page Number or Incorporated by Reference to
4.2(d)	$300,000 Loan Agreement dated June 24, 1996 by and between Aberdeen Development Corporation and APA Enterprises, Inc.	Exhibit 4.2(d) to the June 1996 10-QSB
4.2(e)	Amended Loan Agreement with Aberdeen Development Corporation and APA Enterprises, Inc.	Exhibit 4.2(e) to Registrants Report on Form 10-K for fiscal year ended March 31, 2004
4.2(f)	Purchase Agreement for land with Aberdeen Development Corporation and APA Enterprises, Inc.	Exhibit 4.2(f) to Registrant's Report on Form 10-K for the fiscal year ended March 31, 2005
4.3(a)	Loan Agreement between South Dakota Economic Development Finance and APA Enterprises, Inc.	Exhibit 4.3(a) to the June 1996 10-QSB
4.3(b)	Mortgage and Security Agreement - One Hundred Day Redemption from APA Enterprises, Inc. to South Dakota Economic Development Finance Authority dated as of June 24, 1996	Exhibit 4.3(b) to the June 1996 10-QSB
4.4(a)	Subscription and Investment Representation Agreement of NE Venture, Inc.	Exhibit 4.4(a) to the June 1996 10-QSB
4.4(b)	Form of Common Stock Purchase Warrant for NE Venture, Inc.	Exhibit 4.4(b) to the June 1996 10-QSB
4.5(a)	Certificate of Designation for 2% Series A Convertible Preferred Stock	Exhibit 4.5(a) filed as a part of Registration Statement on Form S-3 (Commission File No. 333-33968)
4.5(b)	Form of common stock warrant issued in connection with 2% Series A Convertible Preferred Stock	Exhibit 4.5(b) filed as a part of Registration Statement on Form S-3 (Commission File No. 333-33968)
4.6	Common Stock Purchase Warrant issued to Ladenburg Thalmann & Co. Inc. to purchase 84,083 shares	Exhibit 4.6 to Registrant's Report on Form 10-K for fiscal year ended March 31, 2000 ("2000 10-K")
4.7	Share Rights Agreement dated October 23, 2000 by and between the Registrant and Wells Fargo Bank Minnesota NA as Rights Agent	Exhibit 1 to the Registration Statement on Form 8-A filed November 8, 2000
4.8	Common Stock Warrant Purchase Agreement with Peter Lee as part of CSP asset purchase	Exhibit 4.8 to Form 8-K filed March 31, 2003
10.1(a)	Sublease Agreement between the Registrant and Jain-Olsen Properties and Sublease Agreement and Option Agreement between the Registrant and Jain-Olsen Properties	Exhibit 10.1 to the Registration Statement on Form S-18 filed with the Chicago Regional Office of the Securities and Exchange Commission on June 26, 1986

Number	Description	Page Number or Incorporated by Reference to
10.1(b)	Amendment and Extension of Sublease Agreement dated August 31, 1999	Exhibit 10.1(b) to 2000 10-K
10.1(c)	Lease Agreement between Registrant and Jain-Olsen Properties	Exhibit 10.1(c) to Registrant's Form 10Q-SB for quarter ended September 30, 2004
*10.2(a)	Stock Option Plan for Nonemployee Directors	Exhibit 10.3a to Registrant's Report on Form 10-KSB for the fiscal year ended March 31, 1994 (the "1994 10-KSB")
*10.2(b)	Form of option agreement issued under the Nonemployee Directors Plan	Exhibit 10.3b to 1994 10-KSB
*10.3	1997 Stock Compensation Plan	Exhibit 10.3 to Registrant's Report on Form 10-KSB for the fiscal year ended March 31, 1997
*10.4	Insurance agreement by and between the Registrant and Anil K. Jain	Exhibit 10.5 to Registrant's Report on Form 10-K for the fiscal year ended March 31, 1990
*10.5	Form of Agreement regarding Repurchase of Stock upon Change in Control Event with Anil K. Jain and Kenneth A. Olsen	Exhibit 10.1 to Registrant's Report on Form 10-QSB for the quarter ended September 30, 1997 ("September 1997 10-QSB")
*10.6	Form of Agreement regarding Employment/Compensation upon Change in Control with Messrs. Jain and Olsen	Exhibit 10.2 to the September 1997 10-QSB
*10.7	Form of Agreement regarding Indemnification of Directors and Officers with Messrs. Jain, Olsen, Ringstad, Roth, Von Wald and Zuckerman	Exhibit 10.7 to Registrant's Report on From 10-K for the fiscal year ended March 31, 2002.
10.8	Sublease agreement between Newport and APACN	Exhibit 10.8 to Registrant's Report of Form 10-QSB for the quarter ended June 30, 2003
10.9	Sublease agreement between Veeco Compound Semiconductor and APA Enterprises, Inc.	Exhibit 10.9 to Registrant's Report of Form 10-K for the fiscal year ended March 31, 2004
10.9(b)	Amendment to sublease between Veeco Compound Semiconductor and APA Enterprises, Inc.	Exhibit 10.9 (b) to Registrant's Report on Form 10-QSB for the quarter ended September 30, 2004
*10.10	Ken Olsen Separation Agreement	Exhibit 10.10 to Registrant's Report on Form 10-K for the fiscal year ended March 31, 2004
*10.11	Stock option agreement with Cheri Podzimek, President of APACN	Exhibit 10.11 to Registrant's Report on Form 10-K for the fiscal year ended March 31, 2005

Number	Description	Page Number or Incorporated by Reference to
10.12	Agreements on sale of MOCVD Assets	Exhibit 10.12 to Registrant's Report on for 8-K filed March 10, 2006
10.13	Patent and Technology and Revenue Sharing License Agreement	Exhibit 10.13 to Registrant's Report on for 8-K filed March 10, 2006
10.14	Lease agreement between Bass Lake Realty, LLC and APACN	**
14	Code of Ethics	Exhibit 14 to Registrant's Report on Form 10-K for the fiscal year ended March 31, 2004
21	List of Subsidiaries	**
23.1	Consent of Grant Thornton LLP	**
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	**
32.1	Certification of Chief Executive Officer and Principal Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	**

*Indicates management contract or compensation plan or arrangements required to be filed as an exhibit to this form.

** Filed with this Report.

LEASE

BY AND BETWEEN

BASS LAKE REALTY LLC,
as Landlord

AND

APA CABLES & NETWORKS. INC.,
as Tenant

DATED: MAY 31, 2006

PROPERTY : BASS LAKE BUSINESS CENTRE I, 5480 NATHAN LANE, PLYMOUTH, MN

LEASE

THIS LEASE is made this 31st day of May, 2006 between Bass Lake Realty LLC, a Delaware limited liability company ("Landlord"), and the Tenant named below.

ARTICLE I
BASIC TERMS

TENANT:	APA Cables & Networks, Inc., a Minnesota corporation
TENANT'S NOTICE ADDRESS:	5480 Nathan Lane, Suite 120 Plymouth, Minnesota 55442 Attn: Chris B Podzimek
LANDLORD'S NOTICE ADDRESS:	c/o Great Point Investors LLC Two Center Plaza, Suite 410 Boston, MA 02108 Attn: Joseph A. Versaggi with a copy to: United Properties LLC 3500 American Boulevard West Suite 200 Bloomington, MN 55431 Attn: Lisa Dongoske Rent payments to be sent to: United Properties MI 65 PO Box 1150 Minneapolis, MN 55480-1150
PROPERTY:	Bass Lake Business Centre, 5480 Nathan Lane, Plymouth, MN (the "Building"), together with the parking areas, landscaping, walkways and other improvements related to the Building, as described on Exhibit A.
PREMISES:	Approximately Twenty-Nine Thousand Seven Hundred Thirty-Eight (29,738) rentable square feet (9,284 square feet of which is office space, 4,499 square feet of which is warehouse space, and15,955 space) located at the Building, as shown on square feet of which is production/tech Exhibit B.
PROPERTY RENTABLE AREA:	Approximately Sixty-Three rentable square feet.
TENANT'S PRO RATA SHARE:	47.2%

LEASE TERM:	Approximately eighty-nine (89) months beginning on the Lease Commencement Date and ending on November 30, 2013.
LEASE COMMENCEMENT DATE:	July 1, 2006.
RENT COMMENCEMENT DATE:	November 1, 2006.
BASE RENT:	(a) From the Rent Commencement Date through and including the last day of the first Lease Year, $203,110.54 per year; $16,925.88 per month; (b) For the second Lease Year, $210,247.66 per year; $17,520.64 per month; (c) For the third Lease Year, $217,384.78 per year; $18,115.40 per month; (d) For the fourth Lease Year, $225,116.66 per year; $18,759.72 per month; (e) For the fifth Lease Year, $232,551.16 per year; $19,379.26 per month; (f) For the sixth Lease Year, $239,985.66 per year; $19,998.81 per month; (g) For the seventh Lease Year, $247,122.78 per year; $20,593.56 per month; and (h) For the last five months of the Term, five monthly payments, each in the amount of $21,237.89.
LEASE YEAR:	Each successive twelve (12) month period comprising the Term, except that the first (1st) Lease Year of the Term may be greater than twelve (12) months and shall commence on the Lease Commencement Date and end on the last day of the month in which the first (1st) anniversary of the Lease Commencement Date occurs (unless the Lease Commencement Date occurs on the first day of a month, in which case the first Lease Year shall end on the day before the first (1st) anniversary of the Lease Commencement Date). Subsequent Lease Years shall commence on the day after the last day of the first (1st) Lease Year or an anniversary thereof, and shall end on each anniversary of the last day of the first (1st) Lease Year.
SECURITY DEPOSIT:	An unconditional, irrevocable letter of credit in the amount of One Hundred Thousand ($100,000) Dollars in the form attached hereto as Exhibit E, subject to reduction as set forth in Section 14.14.

PERMITTED USES:	Subject to applicable zoning, for general office, warehouse and production/technical use, and for no other purpose whatsoever.
BROKERS:	United Properties LLC 3500 American Boulevard West Suite 200 Bloomington, MN 55431 Attn: Mark Sims, Jon Yanta, and Bruce Hoberman
PARKING SPACES:	Eighty-Nine (89) unreserved spaces.

ARTICLE II
LEASE TERM

2.1 LEASE OF PREMISES FOR LEASE TERM.

Landlord hereby leases the Premises to Tenant and Tenant leases the Premises from Landlord for the Lease Term, unless sooner terminated pursuant to the terms hereof. Additionally, from June 1, 2006 until the date that is two (2) weeks after substantial completion of Landlord's Work (as hereinafter defined), Landlord grants to Tenant a license to use approximately 5,000 square feet of warehouse space in a location determined by Landlord at the property known as Eagle Lake Business Centre II, 10200 73rd Avenue, Maple Grove, MN, or Parkers Lake Point III, 14305 21st Avenue. Plymouth, MN. Tenant's use and occupancy of such warehouse space shall be subject to all of the terms and conditions of this Lease, provided, however, Tenant shall not be required to pay any rent for such use and occupancy, and Landlord may immediately terminate such license in the event of any default by Tenant hereunder.

2.2 DELAY IN COMMENCEMENT.

If Landlord is unable to deliver the Premises on the Lease Commencement Date, such date will be postponed to the date possession of the Premises is delivered to Tenant (and all other dates herein shall likewise be recalculated). At Landlord's request, Landlord and Tenant will execute a Memorandum of Acceptance of Lease, in Landlord's customary form, setting forth the Lease Commencement Date, Rent Commencement Date and Expiration Date of this Lease.

2.3 EARLY TERMINATION OPTION.

Provided no default exists or would exist but for the passage of time or the giving of notice, or both, Tenant shall have the right to send to Landlord, on or before March 1, 2011, written notice (the "Termination Notice") that Tenant has elected to terminate the Term effective on November 30, 2011 (the "Early Termination Date"). If Tenant elects to terminate the Term pursuant to the immediately preceding sentence, the effectiveness of such termination will be conditioned upon Tenant's paying to Landlord, contemporaneously with Tenant's delivery of the Termination Notice to Landlord, an early termination fee (the "Early Termination Fee") equal to the sum of (a) $77,517.04, (b) four (4) months of Additional Rent due to Landlord pursuant to the terms hereof at the rate payable during such fifth (5th) Lease Year, and (c) all unamortized transaction costs, including but not limited to the four months free Base Rent provided hereunder, brokerage commissions, costs of tenant improvements made by Landlord, and legal fees; provided, however, if a replacement tenant occupies, pursuant to the terms of a lease, the entire Premises, by February 1, 2012, Landlord will refund to Tenant $38,758.52, plus two (2) months of Additional Rent due to Landlord pursuant to the terms hereof at the rate payable during the fifth (5th) Lease Year. The Early Termination Fee is consideration for Tenant's option to terminate and will not be applied to rent or any other obligation of Tenant. If Tenant exercises this early termination option, on or before the Early Termination Date, Tenant shall vacate and surrender the Premises to Landlord pursuant to the terms of the Lease, and, as of such Early Terminate Date, Tenant shall no longer be responsible for Tenant's obligations under the terms of the Lease, except for those provisions of the Lease that survive termination of the Lease, and any obligations arising prior to the Early Termination Date.

ARTICLE III
RENT

3.1 BASE RENT.

Commencing on the Rent Commencement Date, on the first day of each calendar month during the Lease Term, Tenant will pay to Landlord the Base Rent in equal monthly installments, in lawful money of the United States, in advance and without offset, deduction prior notice or demand. The Base Rent is payable at Landlord's Rent Payment Address or at such other place or to such other person as Landlord may designate in writing from time to time. Payments of Base Rent for any partial calendar month will be prorated. Base Rent for the first month of the Term shall be paid on the date hereof.

3.2 ADDITIONAL RENT.

All sums payable by Tenant under this Lease other than Base Rent are "Additional Rent"; the term "Rent" includes both Base Rent and Additional Rent. Landlord will estimate in advance and charge to Tenant the following costs ("Total Operating Costs"), which Tenant will pay with the Base Rent on a monthly basis throughout the Occupancy Period: (i) all Real Property Taxes for which Tenant is liable under Article 4, (ii) all utility costs (to the extent utilities are not separately metered) for which Tenant is liable under Article 5, (iii) all insurance premiums for which Tenant is liable under Article 6 and (iv) all Operating Expenses for which Tenant is liable under Article 7 of this Lease. Landlord may adjust its estimates of Total Operating Costs at any time based upon Landlord's experience and reasonable anticipation of costs. Such adjustments will be effective as of the next Rent payment date after notice to Tenant. "Occupancy Period" means the period from the time Tenant first enters the Premises, throughout the Lease Term and thereafter as long as Tenant remains in the Premises.

After the end of each fiscal year during the Term, Landlord will deliver to Tenant a statement setting forth, in reasonable detail, the Total Operating Costs paid or incurred by Landlord during the preceding fiscal year and Tenant's Pro Rata Share of such expenses. Within 30 days after Tenant's receipt of such statement, there will be an adjustment between Landlord and Tenant, with payment to or credit given by Landlord (as the case may be).

3.3 INTEREST AND LATE CHARGES.

Any Rent or other amount due to Landlord, if not paid when due, will bear interest from the date due until paid at the rate of 10% per year, but not to exceed the highest rate legally permitted. In addition, if any installment of Rent or any other sums due from Tenant is not received by Landlord within 5 days following the due date, Tenant will pay to Landlord a late charge equal to 5% of such overdue amount. The parties hereby agree that such late charge represents a fair and reasonable estimate of the costs Landlord will incur by reason of late payment by Tenant. Notwithstanding the foregoing, no interest shall accrue and the late charge shall not be due for the first late payment in any rolling twelve (12) month period.

ARTICLE IV
PROPERTY TAXES

4.1 REAL PROPERTY TAXES.

Tenant will pay Tenant's Pro Rata Share of Real Property Taxes allocable to the Occupancy Period. If Landlord receives a refund of any Real Property Taxes with respect to which Tenant has paid Tenant's Pro Rata Share, Landlord will refund to Tenant Tenant's Pro Rata Share of such refund after deducting therefrom all related costs and expenses. "Real Property Taxes" means taxes, assessments (special, betterment, or otherwise), levies, fees, rent taxes, excises, impositions, charges, water and sewer rents and charges, and all other government levies and charges, general and special, ordinary and extraordinary, foreseen and unforeseen, which are imposed or levied upon or assessed against the Property or any Rent. Real Property Taxes include Landlord's costs and expenses of review and contesting any Real Property Tax. If at any time during the Lease Term the present system of ad valorem taxation of real property is changed so that in lieu of the whole or any part of the ad valorem tax on real property, or in lieu of increases therein, Landlord is assessed a capital levy or other tax on the gross rents received with respect to the Property or a federal, state, county, municipal, or other local income, franchise, excise or similar tax, assessment, levy, or charge (distinct from any now in effect) measured by or based, in whole or in part, upon gross rents or any similar substitute tax or levy, then all of such taxes, assessments, levies or charges, to the extent so measured or based, will be deemed to be a Real Property Tax.

4.2 PERSONAL PROPERTY TAXES.

Tenant will pay directly all taxes charged against trade fixtures, furnishings, equipment, inventory or any other personal property belonging to Tenant. Tenant will use its best efforts to have personal property taxed separately from the Property. If any of Tenant's personal property is taxed with the Property, Tenant will pay Landlord the taxes for such personal property within 15 days after Tenant receives a written statement from Landlord for such personal property taxes.

ARTICLE V
UTILITIES

5.1 UTILITIES.

Tenant will promptly pay, directly to the appropriate supplier, the cost of all natural gas, heat, cooling, energy, light, power, sewer service, telephone, water, refuse disposal and other utilities and services supplied to the Premises, together with any related installation or connection charges or deposits (collectively, "Utility Costs") incurred during the Occupancy Period. If any services or utilities are jointly metered with other premises, Landlord will make a reasonable determination of Tenant's proportionate share of such Utility Costs and Tenant will pay such share to Landlord. Landlord reserves the right to participate in wholesale energy purchase programs and to provide energy to the Premises through such programs so long as the cost to Tenant is competitive.

ARTICLE SIX
INSURANCE

6.1. TENANT'S INSURANCE.

Tenant, at its expense, will maintain the following insurance coverages during the Occupancy Period:

(a) Liability Insurance. Commercial general liability insurance insuring Tenant against liability for bodily injury, property damage (including loss of use of property) and personal injury at the Premises, including contractual liability. Such insurance will name Landlord, its property manager, any mortgagee, Great Point Investors LLC, and such other parties as Landlord may designate, as additional insureds. The initial amount of such insurance will be Five Million Dollars ($5,000,000) per occurrence and will be subject to periodic increases reasonably specified by Landlord based upon inflation, increased liability awards, recommendations of Landlord's professional insurance advisers, and other relevant factors. The liability insurance obtained by Tenant under this Section 6.1 will (i) be primary and (ii) insure Tenant's obligations to Landlord under Section 6.4. The amount and coverage of such insurance will not limit Tenant's liability nor relieve Tenant of any other obligation under this Lease.

(b) Worker's Compensation Insurance. Worker's Compensation Insurance in the statutory amount (and Employers' Liability Insurance) covering all employees of Tenant employed or performing services at the Premises, in order to provide the statutory benefits required by the laws of the state in which the Premises are located.

(c) Automobile Liability Insurance. Automobile Liability Insurance, including but not limited to, passenger liability, on all owned, non-owned, and hired vehicles used in connection with the Premises, with a combined single limit per occurrence of not less than One Million Dollars ($1,000,000) for injuries or death of one or more persons or loss or damage to property.

(d) Personal Property Insurance. Personal Property Insurance covering leasehold improvements paid for by Tenant and Tenant's personal property and fixtures from time to time in, on, or at the Premises, in an amount not less than 100% of the full replacement cost, without deduction for depreciation, providing protection against events protected under "All Risk Coverage," as well as against sprinkler damage, vandalism, and malicious mischief. Any proceeds from the Personal Property Insurance will be used for the repair or replacement of the property damaged or destroyed, unless the Lease Term is terminated under an applicable provision herein. If the Premises are not repaired or restored in accordance with this Lease, Landlord will receive any proceeds from the personal property insurance allocable to Tenant's leasehold improvements.

6.2 LANDLORD'S INSURANCE.

During the Lease Term, Landlord will maintain in effect all risk insurance covering loss of or damage to the Property in the amount of its replacement value with such endorsements and deductibles as Landlord determines from time to time. Landlord will have the right to obtain flood, earthquake, and such other insurance as Landlord determines from time to time or is required by any mortgagee of the Property. Landlord will not insure Tenant's fixtures or equipment or building improvements installed or paid by Tenant. Landlord may obtain commercial general liability insurance in an amount and with coverage determined by Landlord insuring Landlord against liability with respect to the Premises and the Property. The policy obtained by Landlord will not provide primary insurance, will not be contributory and will be excess over any liability insurance maintained by Tenant. Landlord will also maintain a rental income insurance policy, with loss payable to Landlord. Tenant will pay Tenant's Pro Rata Share of premiums for the insurance policies maintained by Landlord. Any increase in the cost of Landlord's insurance due to Tenant's use or activities at the Premises will be paid by Tenant to Landlord as Additional Rent.

6.3 GENERAL INSURANCE PROVISIONS.

(a) Any insurance which Tenant is required to maintain under this Lease will include a provision which requires the insurance carrier to give Landlord not less than 30 days' written notice prior to any cancellation or modification of such coverage.

(b) Prior to the earlier of Tenant's entry into the Premises or the Lease Commencement Date, Tenant will deliver to Landlord an insurance company certificate that Tenant maintains the insurance required by Section 6.1 and not less than 20 days prior to the expiration or termination of any such insurance, Tenant will deliver to Landlord renewal certificates therefor. Tenant will provide Landlord with copies of the policies promptly upon request from time to time.

(c) All insurance policies required under this Lease will be with companies having a "General Policy Rating" of A -; X or better, as set forth in the most current issue of the Best Key Rating Guide.

(d) Without limiting the provisions of Section 6.4, Landlord and Tenant, on behalf of themselves and their insurers, each hereby waives any and all rights of recovery against the other, the agents, advisors, employees, members, officers, directors, partners, trustees, beneficiaries and shareholders of the other and the agents, advisors, employees, members, officers, directors, partners, trustees, beneficiaries and shareholders of each of the foregoing (collectively, "Representatives"), for loss of or damage to its property or the property of others under its control, to the extent that such loss or damage is covered by any insurance policy in force (whether or not described in this Lease) at the time of such loss or damage, or required to be carried under this Article 6. All property insurance carried by either party will contain a waiver of subrogation against the other party to the extent such right was waived by the insured party prior to the occurrence of loss or injury.

6.4 INDEMNITY.

To the fullest extent permitted by law, Tenant hereby waives all claims against Landlord and its Representatives (collectively, the "Indemnitees") for damage to any property or injury to or death of any person in, upon or about the Premises or the Property arising at any time and from any cause. Tenant shall hold Indemnitees harmless from and defend Indemnitees from and against all claims, liabilities, judgments, demands, causes of action, losses, damages, costs and expenses, including reasonable attorney's fees, for damage to any property or injury to or death of any person arising from (i) the use or occupancy of the Premises by Tenant or persons claiming under Tenant, except such as is caused by the sole negligence or willful misconduct of Landlord, its agents, employees or contractors, (ii) the negligence or willful misconduct of Tenant in, upon or about the Properly, or (iii) any breach or default by Tenant under this Lease.

ARTICLE VII
OPERATING EXPENSES

7.1 OPERATING EXPENSES.

Tenant will pay Tenant's Pro Rata Share of all Operating Expenses allocable to the Occupancy Period. "Operating Expenses" means all costs and expenses incurred by Landlord with respect to the ownership, maintenance and operation of the Property including, but not limited to: maintenance, repair and replacement of the heating, ventilation, air conditioning, plumbing, electrical, mechanical, utility and safety systems, paving and parking areas, roads and driveways; maintenance of exterior areas such as gardening and landscaping, snow removal and signage; maintenance and repair of roof membrane, flashings, gutters, downspouts, roof drains, skylights and waterproofing; painting; lighting; cleaning; refuse removal; security; utility services attributable to the Common Areas (as defined below); Building personnel costs; personal property taxes; rentals or lease payments paid by Landlord for rented or leased personal property used in the operation or maintenance of the Property; fees for required licenses and permits; a property management fee,; and contributions to reserves for any or all of the foregoing. Operating Expenses do not include: (a) expenditures for capital improvements except (i) those which Landlord anticipates will have the effect of reducing current and/or future Operating Expenses or the rate of increase in Operating Expenses, and (ii) those required by Legal Requirements or insurance requirements; (b) debt service under mortgages; (c) costs of restoration to the extent of net insurance proceeds received by Landlord; (d) leasing commissions and tenant improvement costs; and (e) litigation expenses relating to disputes with tenants.

ARTICLE VIII
USE OF PREMISES

8.1 MANNER OF USE.

Tenant will use the Premises only for the Permitted Uses. Tenant will not cause or permit the Premises to be used in any way which (i) constitutes a violation of any Legal Requirements (as defined below) or the rules and regulations (the "Rules and Regulations") established by Landlord, a copy of which is attached as Exhibit C, as they may be amended in writing by Landlord, (ii) annoys or interferes with the rights of tenants of the Properly, or (iii) constitutes a nuisance or waste or will invalidate any insurance carried by Landlord. Tenant will obtain and pay for all necessary permits, including a certificate of occupancy, and will promptly take all actions necessary to comply with all applicable Federal, State or local statutes, ordinances, notes, regulations, orders, recorded declarations, covenants and requirements (collectively, "Legal Requirements") regulating the use by Tenant of the Premises, including, without limitation, the Occupational Safety and Health Act and the Americans With Disabilities Act.

8.2 ENVIRONMENTAL REQUIREMENTS.

(a) Definition of "Hazardous Material". "Hazardous Material" means any flammable items, explosives, radioactive materials, oil, hazardous or toxic substances, material or waste or related materials, including any substances defined as or included in the definition of "hazardous substances", "hazardous wastes", "hazardous materials" or "toxic substances" now or hereafter regulated under any Legal Requirements, including without limitation petroleum-based products, paints, solvents, lead, cyanide, DDT, printing inks, acids, pesticides, ammonia compounds and other chemical products, asbestos, PCBs and similar compounds, and including any different products and materials which are found to have adverse effects on the environment or the health and safety of persons; provided, however, "Hazardous Material" does not include any de minimis quantities of office or other cleaning supplies commonly used in accordance with Legal Requirements.

(b) Tenant's Obligations. Tenant will not cause or permit any Hazardous Material to be generated, produced, brought upon, used, stored, treated or disposed of in or about the Property by Tenant, its agents, employees, contractors, sublessees or invitees without (i) the prior written consent of Landlord, and (ii) complying with all applicable Legal Requirements pertaining to the transportation, storage, use or disposal of such Hazardous Material (collectively, "Environmental Laws"), including, but not limited to, obtaining proper permits. Landlord is entitled to take into account such other factors or facts Landlord deems reasonably relevant in granting or withholding consent to Tenant's proposed activity with respect to Hazardous Material. Landlord will not, however, be required to consent to the installation or use of any storage tanks on the Property.

If Tenant's transportation, storage, use or disposal of Hazardous Materials results in the contamination of the soil or surface or ground water, release of a Hazardous Material or loss or damage to person(s) or property or the violation of any Environmental Law, then Tenant agrees to: (x) notify Landlord immediately of any contamination, claim of contamination, release, loss or damage, (y) after consultation with Landlord, clean up the contamination in full compliance with all Environmental Laws and (z) indemnify, defend and hold Landlord harmless from and against any claims, suits, causes of action, costs and fees, including, without limitation, attorney's fees and costs, arising from or connected with any such contamination, claim of contamination, release, loss or damage. Tenant will fully cooperate with Landlord and provide such documents, affidavits and information as may be requested by Landlord (A) to comply with any Environmental Law, (B) to comply with the request of any lender, purchaser or tenant, and/or (C) as otherwise deemed reasonably necessary by Landlord in its discretion. Tenant will notify Landlord promptly in the event of any spill or other release of any Hazardous Material at, in, on, under or about the Premises which is required to be reported to a governmental authority under any Environmental Law, will promptly forward to Landlord copies of any notices received by Tenant relating to alleged violations of any Environmental Law, will promptly pay when due any fine or assessment against Landlord, Tenant or the Property and remove or bond any lien filed against the Property relating to any violation of Tenant's obligations with respect to Hazardous Material.

(c) Landlord's Rights. Landlord will have the right, but not the obligation, without in any way limiting Landlord's other rights and remedies under this Lease, to enter upon the Premises, or to take such other actions as it deems necessary or advisable, to investigate, clean up, remove or remediate any Hazardous Material or contamination by Hazardous Material present on, in, at, under or emanating from the Premises or the Property in violation of Tenant's obligations under this Lease or under any laws regulating Hazardous Material or that Tenant is liable under this Lease to clean up, remove or remediate. Landlord will have the right, at its election, in its own name or as Tenant's agent, to negotiate, defend, approve and appeal, at Tenant's expense, any action taken or order issued by any governmental agency or authority against Tenant, Landlord or the Premises or the Property relating to any Hazardous Material or under any related law or the occurrence of any event or existence of any condition that would cause a breach of any of the covenants set forth in this Section 8.2.

If Landlord determines in good faith that a release or other environmental condition may have occurred during the Occupancy Period, at Tenant's cost, Landlord may require an environmental audit of the Premises by a qualified environmental consultant. Tenant will, at it sole cost and expense, take all actions recommended in such audit to remediate any environmental conditions for which it is responsible under this Lease.

8.3 LANDLORD'S ACCESS.

Landlord or its agents may enter the Premises, upon 24 hours notice to Tenant (except in the case of an emergency), to show the Premises to potential buyers, investors or tenants or other parties, for routine property inspections and maintenance or for any other purpose Landlord deems reasonably necessary. During the last 9 months of the Lease Term, Landlord may place customary "For Lease" signs on the Premises.

8.4 COMMON AREAS.

(a) Common Areas. "Common Areas" means all areas within the Property which are available for the common use of tenants of the Property and which are not leased or held for the exclusive use of Tenant or other tenants, including, but not limited to, parking areas, driveways, sidewalks, access roads, landscaping, and planted areas. Landlord, from time to time, may change the size, location, nature, and use of any of the Common Areas, convert Common Areas into leaseable areas, construct additional parking facilities in the Common Areas, and increase or decrease Common Area land or facilities so long as Tenant's use of the Premises is not materially affected.

(b) Use of Common Areas. Tenant will have the non-exclusive right (in common with other tenants and all others to whom Landlord has granted or may grant such rights) to use the Common Areas, including the Parking Spaces, for the purposes intended, subject to such reasonable rules and regulations as Landlord may establish or modify from time to time. Tenant agrees to abide by all such rules and regulations and to use its best efforts to cause others who use the Common Areas with Tenant's express or implied permission to abide by the Rules and Regulations. At any time, Landlord may close any Common Areas to perform any acts as, in Landlord's reasonable judgment, are desirable to maintain or improve the Property. Tenant will not interfere with the rights of Landlord, other tenants, or any other person entitled to use the Common Areas.

(c) Parking. Tenant shall be entitled to park in common with other tenants of Landlord, and receive three (3) nonreserved, unassigned parking spaces for every 1,000 square feet of rentable area of the Premises (i.e., eighty-nine (89) spaces as of the date hereof). Tenant agrees not to overburden the parking facilities, agrees to cooperate with Landlord and other tenants in the use of parking facilities, and to abide by all rules and regulations regarding the use of such parking facilities as may now exist, or as may hereinafter be promulgated by Landlord. Said parking spaces shall be used for parking by vehicles no larger than full-size passenger automobiles or pick-up trucks, herein called "Permitted Size Vehicles." Vehicles other than Permitted Size Vehicles shall be parked and loaded or unloaded as directed by Landlord. Landlord reserves the right, in its absolute discretion, to determine whether parking facilities are becoming overcrowded, and in such event, to allocate parking spaces among tenants or to designate areas within which Tenant must park. Landlord further reserves the right to modify, restripe, and otherwise change the location of drives and parking spaces. Tenant and Tenant's employees, visitors and customers assume all responsibility for damage and theft to vehicles. Tenant shall repair or cause to be repaired, at Tenant's sole cost and expense, any and all damage to the buildings on the Property caused by Tenant's, or Tenant's employees', visitors' or customers' use of such parking areas thereon.

ARTICLE IX
CONDITION AND MAINTENANCE OF PREMISES

9.1 EXISTING CONDITIONS.

Tenant hereby accepts the Property and the Premises in their present condition, subject to all Legal Requirements. Tenant acknowledges that neither Landlord nor any agent of Landlord has made any representation as to the condition of the Property or the suitability of the Property for Tenant's intended use, and except as specifically set forth herein, no agreement of Landlord to alter, remodel, decorate, clean or improve the Premises or Property (or to provide Tenant with any credit or allowance for the same), have been made by or on behalf of Landlord or relied upon by Tenant. Tenant represents and warrants that Tenant has made its own inspection of and inquiry regarding the condition of the Property and is not relying on any representations of Landlord or any broker with respect thereto. Notwithstanding the foregoing, Landlord, at Landlord's sole cost and expense, shall perform the improvements to the Premises as described on Exhibit D attached hereto and made a pail hereof using building standard materials and finishes ("Landlord's Work"). Landlord estimates that the cost of Landlord's Work is Two Hundred Five Thousand Five Hundred Fifteen and 00/100 ($205,515.00) Dollars. In the event that Tenant requests changes to Landlord's Work which will increase the cost thereof, Tenant shall pay to Landlord any such additional costs (the "Excess Costs") upon demand by Landlord. Tenant shall provide its own furniture, fixtures, equipment and appliances for the Premises.

9.2 LANDLORD'S OBLIGATIONS.

Subject to the provisions of Article 10 (Casualty and Condemnation) and Tenant's obligation to pay Additional Rent pursuant to Section 3.2, and except for damage caused by any act or omission of Tenant or Tenant's employees, agents, contractors or invitees, Landlord will maintain the Common Areas in good order, condition and repair and will keep the foundation, roof, building systems (including the heating, ventilating and air conditioning system), structural supports and exterior walls of the improvements on the Property in good order, condition and repair. Landlord will not be obligated to maintain or repair windows, doors or plate glass. Tenant will promptly report in writing to Landlord any defective condition known to it which Landlord is required to repair. Landlord will repair, at Tenant's expense, any damage to the Property caused by Tenant's acts or omissions which is Landlord's maintenance responsibility. In the event that Landlord replaces the heating, ventilating and air conditioning system serving the Premises (after its determination that such replacement is necessary), the cost thereof shall accrue interest at a rate reasonably determined by Landlord and shall be amortized over a term often (10) years, with payments of principal and interest with respect to such replacement cost to be made by Tenant to Landlord on a monthly basis from the date of an invoice from Landlord to Tenant through the expiration of the Lease and paid with Tenant's payments of Base Rent hereunder.

9.3 TENANT'S OBLIGATIONS.

Subject to the provisions of Article 10 (Casualty and Condemnation), at its sole cost and expense, Tenant will keep all portions of the Premises (including without limitation, all systems and equipment, i.e., dock levelers, bumpers, doors and floors including slabs and slab repairs, crack filling and joint repairs, other than the heating, ventilating and air conditioning system, which is to be maintained, repaired and replaced by Landlord as set forth above) in good order, condition and repair (including repainting and refinishing, as needed). If any portion of the Premises or any system or equipment in the Premises which Tenant is obligated to repair can not be fully repaired or restored, Tenant will promptly replace such portion of the Premises or system or equipment. If the benefit or useful life of such replacement extends beyond the Lease Term, Tenant will only pay for a prorated portion of the useful life of such replacement. At Tenant's request, Landlord will perform Tenant's maintenance and repair obligations under this Section 9.03 and Tenant will reimburse Landlord for all costs incurred in doing so promptly upon receipt of an invoice from Landlord.

9.4 ALTERATIONS, ADDITIONS, AND IMPROVEMENTS.

(a) Tenant's Work. Tenant may not make any installations, alterations, additions, or improvements or major repairs in or to the Premises without obtaining Landlord's prior written consent. All work will be performed in accordance with plans and specifications approved by Landlord. Tenant will procure all necessary permits and licenses before undertaking any work on the Premises and will perform all work in a good and workmanlike manner employing materials of good quality and in conformity with all applicable Legal Requirements and insurance requirements. Tenant will (i) employ only contractors reasonably approved by Landlord, (ii) require all contractors employed by Tenant to carry worker's compensation insurance in accordance with statutory requirements and commercial general liability insurance covering such contractors on or about the Premises with a combined single limit not less than $1,000,000 and (iii) submit certificates evidencing such coverage to Landlord prior to the commencement of any work. Landlord may inspect Tenant's work at reasonable times. Tenant will prosecute and complete such work with reasonable diligence and will provide Landlord with "as built" plans, copies of all construction contracts and proof of payment for all labor and materials.

(b) No Liens. Tenant will pay when due all claims for labor and material furnished to the Premises and keep the Property at all times free from liens for labor and materials. Tenant will give Landlord at least 20 days' prior written notice of the commencement of any work on the Premises, regardless of whether Landlord's consent to such work is required. Landlord may record and post notices of non-responsibility on the Premises.

9.5 CONDITION UPON TERMINATION.

Upon the expiration or termination of the Lease Term, Tenant will surrender the Premises to Landlord broom clean and in the condition which Tenant is required to maintain the Premises under this Lease. Tenant will not be obligated to repair any damage which Landlord is required to repair under Article 10 (Casualty and Condemnation). Landlord may require Tenant, at its expense, to remove any alterations, additions or improvements (other than Landlord's Work), as well as any and all signage installed by or for Tenant on the Premises or the Building, prior to the expiration of the Lease and to restore the Premises and the Building to their prior condition. With respect to any alterations, additions or improvements which require Landlord's approval, Landlord will specify if Tenant will be required to remove the same at the time of such approval. Additionally, prior to the expiration or earlier termination of the Lease Term or Tenant's right to possession of the Premises, Tenant shall remove its furniture, equipment, trade fixtures, other items of personal property, and any and all wiring and cabling (including but not limited to telephone, fiber optic, computer, communications, and fire alarm wires and cables) from the Premises, as well as any and all risers, plenums and conduits installed and used exclusively by Tenant in the Building. If Tenant does not remove any such alterations, additions, improvements, or items as set forth herein, Tenant shall be conclusively presumed to have conveyed the same to Landlord free and clear of any and all liens and security interests without further payment or credit by Landlord to Tenant; or at Landlord's sole option, such items shall be deemed abandoned, in which event Landlord may cause such items to be removed and disposed of at Tenant's expense, without notice to Tenant and without obligation to compensate Tenant, and Landlord shall, prior to returning the Security Deposit to Tenant pursuant to Section 14.4 hereof, deduct the cost of such removal and disposal from the Security Deposit, with any costs thereof in excess of the Security Deposit to be paid by Tenant to Landlord upon demand.

9.6 EXEMPTION OF LANDLORD FROM LIABILITY.

Landlord will not be liable for any damage or injury to the person, business (or any loss of income therefrom), goods, wares, merchandise or other property of Tenant, Tenant's employees, invitees, customers or any other person or about the Property, whether such damage or injury is caused by or results from: (a) fire, steam, electricity, water, gas or rain; (b) the breakage, leakage, obstruction or other defects of pipes, sprinklers, wires, appliances, plumbing, air conditioning or lighting fixtures or any other cause; (c) conditions arising in or about the Property, or from other sources or places; (d) any curtailment or interruption in utility services or (e) any act or omission of any other tenant of the Property. Tenant will give Landlord prompt notice upon the occurrence of any accident or casualty at the Premises. The provisions of this Section will not exempt Landlord from liability for its gross negligence or willful misconduct; provided, however, Landlord will not be liable for any consequential damages.

ARTICLE X
CASUALTY AND CONDEMNATION

10.1 DAMAGE TO PREMISES.

(a) If the Premises are destroyed or rendered untenantable, either wholly or in part, by fire or other casualty ("Casualty"), Tenant will immediately notify Landlord in writing upon the occurrence of such Casualty. Landlord may elect either to (i) repair the damage caused by such casualty as soon as reasonably possible, in which case this Lease will remain in full force and effect, or (ii) terminate the Lease Term as of the date the Casualty occurred. Landlord will notify Tenant within 30 days after receipt of notice of the Casualty whether Landlord elects to repair the damage or terminate the Lease Term. If Landlord elects to repair the damage, Tenant will pay Landlord Tenant's Pro Rata Share of the deductible amount (which deductible shall not exceed $25,000) under Landlord's insurance allocable to the damage to the Premises and, if the damage was due to an act or omission of Tenant or its employees, agents, contractors or invitees, the difference between the actual cost of repair and any insurance proceeds received by Landlord.

(b) If (i) based on the estimate of Landlord's architect or contractor, it will take Landlord more than 9 months to rebuild the Premises or (ii) the Casualty occurs during the last 6 months of the Lease Term and the damage is estimated by Landlord to require more than 30 days to repair, Tenant may elect to terminate the Lease Term as of the date the Casualty occurred, which must be exercised by written notification to Landlord within 10 days after the occurrence of the Casualty.

(c) If the Property is destroyed or damaged by Casualty and Landlord elects to repair or restore the Property pursuant to the provisions of this Article 10, any Rent payable during the period of such damage, repair and/or restoration will be reduced according to the degree, if any, to which Tenant's use of the Premises is impaired.

(d) The provisions of this Article 10 will govern the rights and obligations of Landlord and Tenant in the event of any damage or destruction of or to the Property. Tenant waives the protection of any statute, code or judicial decision which grants a tenant the right to terminate a lease in the event of the damage or destruction of the leased property.

10.2 CONDEMNATION.

If more than 20% of the floor area of the Premises or more than 25% of the parking on the Property is taken by eminent domain, either Landlord or Tenant may terminate the Lease Term as of the date the condemning authority takes title or possession, by delivering notice to the other within 10 days after receipt of written notice of such taking (or in the absence of such notice, within 10 days after the condemning authority takes title or possession). If neither party terminates the Lease Term, this Lease will remain hi effect as to the portion of the Premises not taken, except that the Base Rent will be reduced in proportion to the reduction in the floor area of the Premises. Any condemnation award or payment will be paid to Landlord. Tenant will have no claim against Landlord for the value of the unexpired lease term or otherwise; provided, however, Tenant may make a separate claim with the condemning authority for its personal property and/or moving costs so long as Landlord's award is not reduced thereby.

ARTICLE XI
ASSIGNMENT AND SUBLETTING

11.1 LANDLORD'S CONSENT REQUIRED.

Tenant will not assign or transfer this Lease or sublease the Premises or any part thereof or interest therein, or mortgage, pledge or hypothecate its leasehold interest, without Landlord's prior written consent, which will not be unreasonably withheld. Unless Tenant is a publicly traded company, a transfer of a controlling interest in Tenant will be deemed an assignment of this Lease. Any attempted transfer without consent will be void and constitute a non-curable Event of Default under this Lease (as defined below). Tenant's request for consent will include the details of the proposed sublease or assignment, including the name, business and financial condition of the prospective transferee, financial details of the proposed transaction (e.g., the term of and the rent and security deposit payable under any proposed assignment or sublease), and any other information Landlord deems relevant. Landlord will have the right to withhold consent, in its reasonable business judgment, or to grant consent, based on the following factors: (i) the business of the proposed assignee or subtenant and the proposed use of the Premises; (ii) the net worth and financial condition of the proposed assignee or subtenant; (iii) Tenant's compliance with all of its obligations under this Lease; and (iv) such other factors as Landlord may reasonably deem relevant. Tenant will promptly furnish to Landlord copies of all transaction documentation.

11.2 OFFER TO TERMINATE.

If Tenant desires to assign this Lease or sublease all or any part of the Premises, Tenant will notify Landlord and Landlord for a period of 30 days will have the right to terminate the Lease Term. If Tenant desires to sublease only a portion of the Premises, and such portion is subdividable (with any costs paid by Tenant), then the right to terminate may be exercised with respect to only that portion of the Premises to be subleased. If Landlord elects not to terminate the Lease Term as provided in this Section 11.2, Tenant shall pay to Landlord 50% of any net profits (i.e., profits after deducting the actual bona fide costs or expenses incurred by Tenant in connection with such assignment or sublease, amortized monthly on a straight-line basis over the term of the applicable sublease or assignment) received by Tenant from any assignment of this Lease or sublet of the Premises.

11.3 NO RELEASE OF TENANT.

Notwithstanding any assignment or subletting, Tenant will at all times remain fully responsible and primarily liable for the payment of Rent and compliance with all of Tenant's obligations under this Lease. Consent to one transfer will not be deemed a consent to any subsequent transfer or a waiver of the obligation to obtain consent on subsequent occasions. If Tenant's assignee or transferee defaults under this Lease, Landlord may proceed directly against Tenant without pursuing remedies against the assignee or transferee.

ARTICLE XII
DEFAULTS AND REMEDIES

12.1 COVENANTS AND CONDITIONS.

Tenant's performance of each of Tenant's obligations under this Lease is a condition as well as a covenant. Tenant's right to continue in possession of the Premises is conditioned upon such performance. Time is of the essence in the performance by Tenant of all covenants and conditions.

12.2 DEFAULTS.

Each of the following constitutes an "Event of Default" under this Lease:

(a) Tenant fails to pay Rent or any other sum payable under this Lease within 5 days after it is due;

(b) Tenant fails to perform any of Tenant's other obligations under this Lease and such failure continues for a period of 30 days after notice from Landlord; provided that if more than 30 days are reasonably required to complete such performance, Tenant will not be in default if Tenant commences such performance within the 30 day period and thereafter diligently pursues its completion;

(c) Tenant abandons the Premises; or

(d) Tenant (or Guarantor) becomes insolvent or bankrupt, has a receiver or trustee appointed for any part of its property, makes an assignment for the benefit of its creditors, or any proceeding is commenced either by Tenant or against it under any bankruptcy or insolvency laws, which proceeding is not dismissed within 60 days; provided, however, if a court of competent jurisdiction determines that any of the acts described in this subsection (d) is not an Event of Default under this Lease, and a trustee is appointed to take possession (or if Tenant remains a debtor in possession) and such trustee or Tenant assigns, subleases, or transfers Tenant's interest hereunder, then Landlord will receive, as Additional Rent, the excess, if any, of the rent (or any other consideration) paid in connection with such assignment, transfer or sublease over the rent payable by Tenant under this Lease.

12.3 REMEDIES.

On the occurrence of an Event of Default, Landlord may, at any time thereafter, with or without notice or demand, and without limiting Landlord in the exercise of any right or remedy which Landlord may have:

(a) Terminate the Lease Term by written notice to Tenant. Tenant will then immediately quit and surrender the Premises to Landlord, but Tenant will remain liable as hereinafter provided. Following termination, without prejudice to other remedies Landlord may have by reason of Tenant's default or of such termination, Landlord may (i) peaceably reenter the Premises upon voluntary surrender by Tenant or remove Tenant therefrom and any other persons occupying the Premises, using such legal proceedings as may be available; (ii) repossess the Premises or relet the Premises or any part thereof for such term (which may be for a term extending beyond the Lease Term), at such rental and upon such other terms and conditions as Landlord in Landlord's sole discretion determines, with the right to make alterations and repairs to the Premises; and (iii) remove all personal property therefrom.

The amount of damages Tenant will pay to Landlord following termination will include all Rent unpaid up to the termination of the Lease Term, the value of any free or reduced rent provided for in this Lease, costs and expenses incurred by Landlord due to such Event of Default and, in addition, Tenant will pay to Landlord as damages, at the election of Landlord (if Landlord shall elect subsection (y) below, it may cease such election at any time), either (x) the amount, discounted to present value (at the then Federal Reserve Bank discount rate) by which, at the time of the termination of the Lease Term or of Tenant's right to possession (or at any time thereafter if Landlord initially elects damages under subsection (y) below), (i) the aggregate of the Rent and other charges projected over the period commencing with such termination and ending on the expiration date of this Lease exceeds (ii) the aggregate projected rental value of the Premises for such period; or (y) amounts equal to the Rent and other charges which would have been payable by Tenant had the Lease Term or Tenant's right to possession not been so terminated, payable upon the due dates therefor specified herein following such termination and until the expiration date of this Lease, provided, however, that if Landlord re-lets the Premises during such period, Landlord will credit Tenant with the net rents received by Landlord from such re-letting, such net rents to be determined by first deducting from the gross rents received from such re-letting the expenses incurred or paid by Landlord in terminating this Lease, and the reasonable expenses of re-letting, including, without limitation, altering and preparing the Premises for new tenants, brokers' commissions and legal fees, it being understood that any such reletting may be for a period equal to or shorter or longer than the remaining Lease Term; and provided, further, that in no event (i) will Tenant be entitled to receive any excess of such net rents over the sums payable by Tenant to Landlord hereunder or (ii) will Tenant be entitled in any suit for the collection of damages pursuant to this subsection (y) to a credit in respect of any net rents from a re-letting except to the extent that such net rents are actually received by Landlord prior to the commencement of such suit.

If the Premises or any part thereof are re-let in combination with other space, then proper apportionment on a square foot area basis will be made of the rent received from such re-letting and of the expenses of re-letting. In calculating the Rent and other charges under subsection (x) above, there will be included, in addition to the Rent, other considerations agreed to be paid or performed by Tenant, on the assumption that all such considerations would have remained constant for the balance of the full Lease Term hereby granted. Landlord may re-let the Premises or any part thereof for such rent and on such terms as it determines (including the right to re-let the Premises for a greater or lesser term than the Lease Term, the right to re-let the Premises as part of a larger area and the right to change the character or use made of the Premises). Landlord will use reasonable efforts to re-let the Premises and otherwise to mitigate Tenant's damages upon redelivery of the Premises to Landlord. Suit or suits for the recovery of damages, or any installments thereof, may be brought by Landlord from time to time at its election, and nothing contained herein will be deemed to require Landlord to postpone suit until the date when the Lease Term would have expired if it had not been terminated hereunder.

(b) Maintain Tenant's right to possession, in which case this Lease will continue in effect whether or not Tenant has abandoned the Premises. In such event, Landlord will be entitled to enforce all of Landlord's rights and remedies under this Lease, including the right to recover the Rent as it becomes due.

(c) Pursue any other remedy now or hereafter available to Landlord under the laws or judicial decisions of the state in which the Property is located.

12.4 DAMAGES.

On any termination, Landlord's damages will include all costs and fees, including reasonable attorneys' fees that Landlord incurs in connection with any bankruptcy court or other court proceeding with respect to the Lease, the obtaining of relief from any stay in bankruptcy restraining any action to evict Tenant, or the pursuing of any action with respect to Landlord's right to possession of the Premises. All such damages suffered (apart from Rent payable hereunder) will constitute pecuniary damages which will be paid to Landlord prior to assumption of the Lease by Tenant or any successor to Tenant in any bankruptcy or other proceedings.

12.5 CUMULATIVE REMEDIES.

Except as otherwise expressly provided herein, any and all rights and remedies which Landlord may have under this Lease and at law and equity are cumulative and will not be deemed inconsistent with each other, and any two or more of all such rights and remedies may be exercised at the same time to the greatest extent permitted by law.

ARTICLE XIII
PROTECTION OF LENDERS

13.1 SUBORDINATION.

This Lease shall be automatically subordinated to any Mortgage encumbering the Property. Landlord shall use commercially reasonable efforts to provide to Tenant an instrument in commercially reasonable form providing that the ground lessor, mortgagor or beneficiary of such Mortgage agrees that in the event of the foreclosure or termination of such Mortgage, this Lease and the rights of Tenant hereunder will continue in full force and effect so long as Tenant continues to comply with all its obligations hereunder. "Mortgage" includes any mortgage, deed of trust or ground lease, together with any amendments, additional advances, restatements, modifications or consolidations of such instrument. If any ground lessor, beneficiary or mortgagee elects to have this Lease prior to the lien of its Mortgage and gives written notice thereof to Tenant, this Lease will be deemed prior to such Mortgage whether this Lease is dated prior or subsequent to the date of said Mortgage or the date of recording thereof.

13.2 ATTORNMENT.

If Landlord's interest in the Property is acquired by any ground lessor, beneficiary, mortgagee, or purchaser at a foreclosure sale, Tenant will attorn to the transferee of or successor to Landlord's interest in the Property and recognize such transferee or successor as successor Landlord under this Lease. Tenant waives the protection of any statute or rule of law which gives Tenant any right to terminate this Lease or surrender possession of the Premises upon the transfer of Landlord's interest.

13.3 ESTOPPEL CERTIFICATES.

Within 10 days after Landlord's request, Tenant will execute, acknowledge and deliver to Landlord a written statement certifying: (i) that none of the terms or provisions of this Lease have been changed (or if they have been changed, stating how they have been changed); (ii) that this Lease has not been canceled or terminated; (iii) the last date of payment of the Base Rent and other charges and the time period covered by such payment; (iv) that Landlord is not in default under this Lease (or if Landlord is claimed to be in default, setting forth such default in reasonable detail); and (v) such other information with respect to Tenant or this Lease as Landlord may reasonably request or which any prospective purchaser or encumbrancer of the Property may require. Landlord may deliver any such statement by Tenant to any prospective purchaser or encumbrancer of the Property, and such purchaser or encumbrancer may rely conclusively upon such statement as true and correct. If Tenant does not deliver such statement to Landlord within such 10 day period, Landlord, and any prospective purchaser or encumbrancer, may conclusively presume and rely upon (and Tenant will be estopped from denying): (i) that the terms and provisions of this Lease have not been changed except as otherwise represented by Landlord; (ii) that this Lease has not been canceled or terminated except as otherwise represented by Landlord; (iii) that not more than one month's Base Rent or other charges have been paid in advance; and (iv) that Landlord is not in default under this Lease.

13.4 TENANT'S FINANCIAL CONDITION.

Within 10 days after request from Landlord from time to time, Tenant will deliver to Landlord Tenant's financial statements (audited, if available) for the most recent two fiscal years. Such financial statements may be delivered to Landlord's mortgagees and lenders and prospective mortgagees, lenders and purchasers. Landlord shall exercise commercially reasonable efforts to keep all non-public financial statements confidential to Landlord and such mortgagees or prospective purchasers and their respective attorneys, accountants and representatives, and Landlord will use them only in connection with the Property and this Lease.

ARTICLE XIV
MISCELLANEOUS PROVISIONS

14.1 COVENANT OF QUIET ENJOYMENT.

Tenant on paying the Rent and performing its obligations hereunder will peacefully and quietly have, hold and enjoy the Premises throughout the Lease Term without any manner of hindrance from Landlord, subject however to all the terms and provisions hereof.

14.2 LANDLORD'S LIABILITY AND INDEMNITY.

The obligations of this Lease run with the land, and this Lease will be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns. No owner of the Property will be liable under this Lease except for breaches of Landlord's obligations occurring while it is owner of the Property. The obligations of Landlord will be binding upon the assets of Landlord which comprise the Property but not upon other assets of Landlord. No individual Representative will be personally liable under this Lease or any other instrument, transaction or undertaking contemplated hereby.

To the fullest extent permitted by law, Landlord will indemnify and hold harmless Tenant from any liabilities, losses, damages, costs, expenses (including reasonable attorneys' fees and expenses), causes of action, suits, claims, demands or judgments arising from any act of negligence of Landlord, except to the extent arising out of Tenant's negligence or willful misconduct or breach of this Lease. This indemnity does not cover claims arising from the presence or release of Hazardous Materials.

14.3 NOTICE TO LANDLORD.

Tenant will give written notice of any failure by Landlord to perform any of its obligations under this Lease to Landlord and to any ground lessor, mortgagee or beneficiary under any Mortgage encumbering the Property whose name and address have been furnished to Tenant. Landlord will not be in default under this Lease unless Landlord (or such ground lessor, mortgagee or beneficiary) fails to cure such non-performance within 30 days after receipt of Tenant's notice or such longer period as may be required to diligently complete such matter. If Landlord (or such ground lessor, mortgagee or beneficiary) can not perform any of its obligations due to events beyond its reasonable control, the time provided for performing such obligations will be extended by a period of time equal to the duration of such events. Events beyond Landlord's reasonable control include, but are not limited to, acts of God, war, civil commotion, labor disputes, strikes, fire, flood or other casualty or weather conditions, shortages of labor or material, and Legal Requirements.

14.4 HOLDING OVER.

If Tenant does not vacate the Premises upon the expiration or earlier termination of this Lease, (i) Tenant will indemnify Landlord against all damages, costs, liabilities and expenses, including attorneys' fees, which Landlord incurs on account of Tenant's failure to vacate and (ii) the Base Rent will increase to 150% of the Base Rent then in effect, payable to Landlord in monthly installments without pro-ration for any partial month, and Tenant's obligation to pay Additional Rent will continue. Any holdover by Tenant does not constitute an extension of the Lease or recognition by Landlord of any right of Tenant to remain in the Premises.

14.5 LANDLORD'S CONSENT.

Tenant will pay Landlord its reasonable fees and expenses incurred in connection with any act by Tenant which requires Landlord's consent or approval under this Lease.

14.6 LANDLORD'S RIGHT TO CURE.

If Tenant defaults in the performance of any obligation under this Lease, Landlord will have the right (but is not required) to perform such obligation and, if necessary, to enter upon the Premises. All costs incurred by Landlord (together with interest at the rate of 15% per year but not to exceed the highest legal rate) will be deemed to be Additional Rent under this Lease and will be payable to Landlord immediately on demand. Landlord may exercise the foregoing rights without waiving any of its other rights or releasing Tenant from any of its obligations under this Lease.

14.7 INTERPRETATION.

The captions of the Articles or Sections of this Lease are not a part of the terms or provisions of this Lease. Whenever required by the context of this Lease, the singular includes the plural and the plural includes the singular. The masculine, feminine and neuter genders each include the other. In any provision relating to the conduct, acts or omissions of Tenant, the term "Tenant" includes Tenant's agents, employees, contractors, invitees, successors or others using the Premises with Tenant's express or implied permission. This Lease does not, and nothing contained herein, will create a partnership or other joint venture between Landlord and Tenant. A determination by a court of competent jurisdiction that any provision of this Lease or any part thereof is illegal or unenforceable will not invalidate the remainder of such provision, which will remain in full force and effect.

14.8 INCORPORATION OF PRIOR AGREEMENTS; MODIFICATIONS.

This Lease is the only agreement between the parties pertaining to the lease of the Premises. All amendments to this Lease must be in writing and signed by all parties. Any other attempted amendment will be void.

14.9 NOTICES.

All notices, requests and other communications required or permitted under this Lease will be in writing and personally delivered or sent by a national overnight delivery service which maintains delivery records. Notices will be delivered to Tenant's Notice Address or to Landlord's Notice Address, as appropriate. All notices will be effective upon delivery (or refusal to accept delivery). Either party may change its notice address upon written notice to the other party.

14.10 WAIVERS.

All waivers will be in writing and signed by the waiving party. Landlord's failure to enforce any provision of this Lease or its acceptance of Rent is not a waiver and will not prevent Landlord from enforcing that provision or any other provision of this Lease in the future. No statement on a payment check from Tenant or in a letter accompanying a payment check will be binding on Landlord. Landlord may, with or without notice to Tenant, negotiate such check without being bound by to the conditions of such statement.

14.11 BINDING EFFECT; CHOICE OF LAW.

This Lease will bind any party who legally acquires any rights or interest in this Lease from Landlord or Tenant, provided that Landlord will have no obligation to Tenant's successor unless the rights or interests of Tenant's successor are acquired in accordance with the terms of this Lease. The laws of the state in which the Property is located govern this Lease. The parties hereto waive trial by jury in any action, proceeding or counterclaim brought by any party(ies) against any other party(ies) on any matter arising out of or in any way connected with this Lease or the relationship of the parties hereunder.

14.12 EXECUTION OF LEASE.

This Lease may be executed in counterparts and, when all counterpart documents are executed, the counterparts will constitute a single binding instrument. Landlord's delivery of this Lease to Tenant is not be deemed to be an offer to lease and will not be binding upon either party until executed and delivered by both parties.

14.13 SURVIVAL.

All representations and warranties of Landlord and Tenant, Tenant's indemnity under Section 6.4, the provisions of Section 8.2 and all obligations of Tenant to pay Additional Rent hereunder, shall survive the termination of this Lease.

14.14 SECURITY DEPOSIT.

Upon the execution of this Lease and as a condition precedent to the effectiveness of this Lease, Tenant shall deposit with Landlord the Security Deposit. Landlord may, at its option, apply all or part of the Security Deposit to any unpaid Rent or other charges due from Tenant, cure any other defaults of Tenant, or compensate Landlord for any loss or damage which Landlord may suffer due to Tenant's default. If Landlord uses any part of the Security Deposit, Tenant will restore the Security Deposit to its full amount within 10 days after Landlord's request. No interest will be paid on the Security Deposit, no trust relationship is created herein between Landlord and Tenant with respect to the Security Deposit, and the Security Deposit may be commingled with other funds of Landlord. Upon expiration or termination of this Lease not resulting from Tenant's default and after Tenant has vacated the Premises in the manner required by this Lease, Landlord will pay to Tenant any balance of the Security Deposit not applied pursuant to this Section. If the Security Deposit is in the form of an unconditional, irrevocable letter of credit, such letter of credit will be issued by a financial institution approved by Landlord and in the form of Exhibit E attached hereto and made a part hereof. Tenant acknowledges that any failure of the issuing bank to renew the letter of credit for an additional period of one (1) year (unless the letter of credit has been reduced to $0 as set forth below, or the Term has expired) shall constitute an Event of Default hereunder, entitling Landlord to immediately draw down on such letter of credit without notice to Tenant.

So long as Tenant is not in default under the terms of the Lease (and no condition exists which, but for the passage of time or the giving of notice would constitute a default hereunder), upon notice to Landlord, and Landlord's written approval thereof, the Letter of Credit may be reduced as follows (a) to $75,000 on the first day of the third (3^{rd}) Lease Year, (b) to $50,000 on the first day of the fourth (4^{th}) Lease Year, (c) to $25,000 on the first day of the fifth (5^{th}) Lease Year, and (d) to $0 on the first day of the sixth (6^{th}) Lease Year. If Tenant is not entitled to any one reduction, as set forth above, Tenant shall not be entitled to any further reductions hereunder. Upon reduction of the amount of the Letter of Credit, Tenant shall deliver to Landlord an amendment to the Letter of Credit setting forth the new amount thereof. If the Letter of Credit has not been released as set forth above, within forty-five (45) days of the Expiration Date, provided no draw is pending or has been made with the issuer of said Letter of Credit by Landlord, and Tenant is not in default (nor are there any conditions which, but for the passage of time or the giving of notice would constitute a default hereunder), Tenant shall be entitled to a full release of the Letter of Credit.

14.15 ACTS OF GOD.

In any case where either party hereto is required to do any act, delays caused by or resulting from Acts of God, war, civil commotion, fire, floor or other casualty, labor difficulties, shortages of labor, materials or equipment, government regulations, unusually severe weather, or other causes beyond such party's reasonable control, shall not be counted in determining the time during which work shall be completed, whether such time be designated by a fixed date, a fixed time or a "reasonable time", and such time shall be deemed to be extended by the period of such delay.

14.16 INTENTIONALLY DELETED.

14.17 INTENTIONALLY DELETED.

14.18 NO OTHER BROKERS.

Landlord and Tenant each represent and warrant to the other that the Brokers are the only agents, brokers, finders or other parties with whom it has dealt who may be entitled to any commission or fee with respect to this Lease or the Premises or the Property. Landlord and Tenant each agree to indemnify and hold the other party harmless from any claim, demand, cost or liability, including, without limitation, attorneys' fees and expenses, asserted by any party other than the Brokers based upon dealings with that party.

14.19 LEGAL COSTS.

In any enforcement proceeding brought by either party with respect to this Lease, the non-prevailing party will pay to the prevailing party in such proceeding all costs, including reasonable attorneys' fees and court costs, incurred by such other party with respect to said proceeding and any appeals therefrom.

14.20 ADDITIONAL PROVISIONS.

The exhibits, if any, attached hereto, are incorporated herein by reference.

SIGNATURES FOLLOW ON NEXT PAGE

Signed on June 6, 2006

LANDLORD:

BASS LAKEJ&EALTY LLC, a Delaware limited liability company

By: /s/ Randolph L. Razazian III

Name: Randolph L. Razazian III

Title: Manager

Signed on May 31, 2006

TENANT:

APA CABLES & NETWORKS, INC., a Minnesota corporation

By: /s/ Cheri B Podzimek

Name: Cheri B Podzimek

Title: President

EXHIBIT A
THE PROPERTY

Lot 1, Block 1, NATHAN 54 CENTER, Hennepin County, Minnesota,

(Abstract property).

EXHIBIT "B"

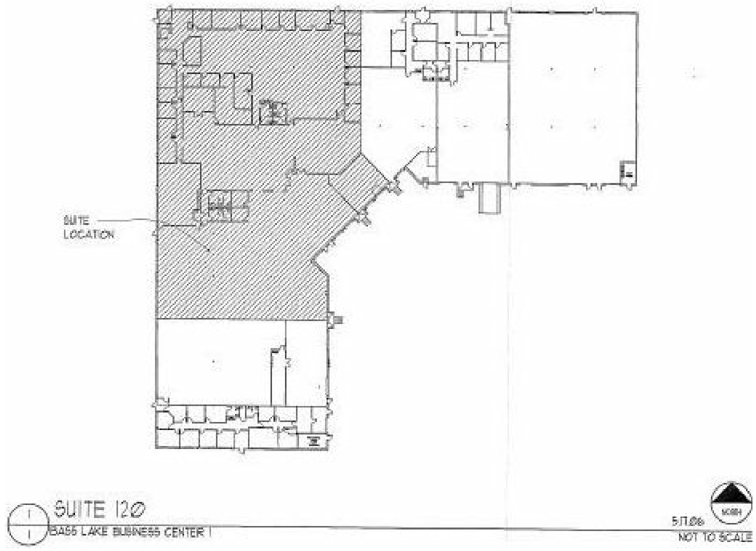
SUITE
LOCATION
SUITE 120
BASS LAKE BUSINESS CENTER I
5.17.06
NORTH
NOT TO SCALE

EXHIBIT C
RULES AND REGULATIONS

1. No sign, placard, picture, advertisement, name, notice or sun screening shall be inscribed, displayed, printed or affixed on or to any part of the outside or inside of the Building without the written consent of Landlord first had and obtained and in the absence thereof, Landlord shall have the right to remove any such sign, placard, picture, advertisement, name or notice without notice to and at the expense of Tenant. All approved signs of lettering on doors shall be printed, painted, affixed or inscribed at the sole risk and expense of Tenant by a licensed contractor approved by Landlord and subject to all laws, ordinances rules, regulations and recommendations of all governmental and quasi-governmental authorities having jurisdiction thereover and all insurance companies and fire rating agencies which insure the Building. Tenant shall not place anything or allow anything to be placed near the glass of any window, door, partition or wall which may appear unsightly from outside the Premises. Landlord may specify a Building standard window covering for all exterior windows.

2. All parking shall be within the property boundaries of the Property and within marked parking spaces. There should be no on-street parking and at no time shall any Tenant obstruct any driveways or loading areas intended for the use of other tenants, their employees, agents, customers and invitees. The driveways and parking areas at the Property are for the joint and non-exclusive use of Landlord's tenants, -their employees, agents, customers and invitees, unless specifically marked to the contrary. In the event Tenant, its agents, customers and/or invitees use a disproportionate portion of the parking areas, Landlord shall have the right to restrict Tenant, its agents, customers and/or invitees to certain parking areas. Tenant shall not permit any fleet trucks to park overnight in the Property's parking areas without Landlord's prior written approval.

3. Unless specifically approved by Landlord in writing, no materials, supplies or equipment shall be stored anywhere in, on or about the Building except inside the Premises. Trash receptacles may not be placed in the service areas except by Landlord. If Landlord does not supply trash receptacles, Tenant shall furnish its own receptacles, and shall place such receptacles in a location designated by Landlord.

4. No additional locks, other than Landlord approved entry systems, shall be placed on the doors of the Premises by Tenant nor shall any existing locks be changed unless Landlord is immediately furnished with two keys thereto. Landlord will, without charge, furnish Tenant with two keys for each lock on the entrance doors to the Premises when Tenant assumes possession, with the understanding that at the termination or expiration of the Term of this Lease the keys to the Premises shall be returned to Landlord.

5. Tenant will refer all contractors, contractor's representatives and installation technicians rendering any service on or to the Premises for Tenant to Landlord for its approval and supervision before performance of any service. This provision shall apply to all work performed in the Building, including, but not limited to, installation of electrical devices and attachments and installations of any nature affecting floors, walls, woodwork, trim, windows, ceilings, equipment or any other portion of the Building.

6. No Tenant shall at any time occupy or allow any person to occupy any part of the Premises or the Property as sleeping or lodging quarters.

7. Tenant shall not place, install or operate on the Premises or in any part of the Property, any engine, stove or machinery, or conduct mechanical operations or cook thereon or therein, or place or use in or about the Premises any explosives, gasoline, kerosene, oil, acids, caustics or any other flammable, explosive or Hazardous Material without the prior written consent of Landlord. The foregoing shall not prohibit the use of microwave ovens.

8. Windows facing the Building exterior shall at all times be wholly clear and uncovered (except for such blinds or curtains or other window coverings Landlord may provide or approve) so that a full unobstructed view of the interior of the Premises may be had from outside the Building.

9. The sidewalks, parking lots and exits shall not be obstructed by Tenant, its employees, agents, contractors, subtenants or assigns or used for any purpose other than for ingress to and egress from the Premises.

10. Tenant shall not use, keep or permit to be used or kept any foul or noxious gas or substance in the Premises, or permit or suffer the Premises to be occupied or used in a manner offensive or objectionable to Landlord or other occupants of the Building by reason of noise, odors and vibrations, or interfere in any way with other Tenants or those having business in the Building, nor shall any animals or birds be brought in or kept in or about the Premises or the Building.

11. Landlord reserves the right to exclude or expel from the Property any person who, in the judgment of Landlord, is intoxicated or under the influence of liquor or drugs, or who may in any manner do any act in violation of any law or any rule or regulations of the Property.

12. Landlord shall have the right, exercisable without notice and without liability to Tenant, to change the name of the Building and street address of the Building of which the Premises are a part.

13. Tenant shall not disturb, solicit or canvass any occupant of the Building and shall cooperate to prevent same.

14. Without the prior written consent of Landlord, Tenant shall not use the name of the Building or Property in connection with or in promoting or advertising the business of Tenant except as Tenant's address.

15. Landlord shall have the right to control and operate the common areas of the Property, the public facilities thereof, as well as the facilities furnished for the common use of all Tenants, in such manner as it deems appropriate.

16. No satellite dish, radio, television or other aerial or equipment of any kind may be placed or installed on the roof or on any exterior wall of the Premises or on the grounds or common areas of the Property without the prior written consent of Landlord in each instance. Any equipment so installed without such written consent shall be at the sole risk of Tenant and shall be subject to removal without notice at any time and Tenant shall pay to Landlord, on demand, as additional rent, the cost of any damages occasioned thereby including, but not limited to, the cost to replace any warranty voided or diminished by such installation and the cost of removal and repairs.

17. Landlord shall have the right from time to time to modify, add to or delete any of these rules and regulations at Landlord's discretion, provided that any changes are uniformly applied to all Tenants.

EXHIBIT D
DESCRIPTION OF LANDLORD'S WORK

Landlord shall make the improvements to the Premises shown on the attached space plan prepared by WCL Architects dated September 21, 2005, updated on January 20, 2006, and further updated on March 3, 2006, using building standard colors, materials and finishes, mutually agreed upon by Landlord and Tenant.

If Tenant does not choose a color, material, finish, or other items needed in connection with Landlord's Work within two (2) days of the date of Landlord's request, Landlord shall, in its sole discretion, choose such color, material, finish or other item on Tenant's behalf.

[Insert Space Plan]

EXHIBIT 'D'
DESCRIPTION OF LANDLORD'S WORK

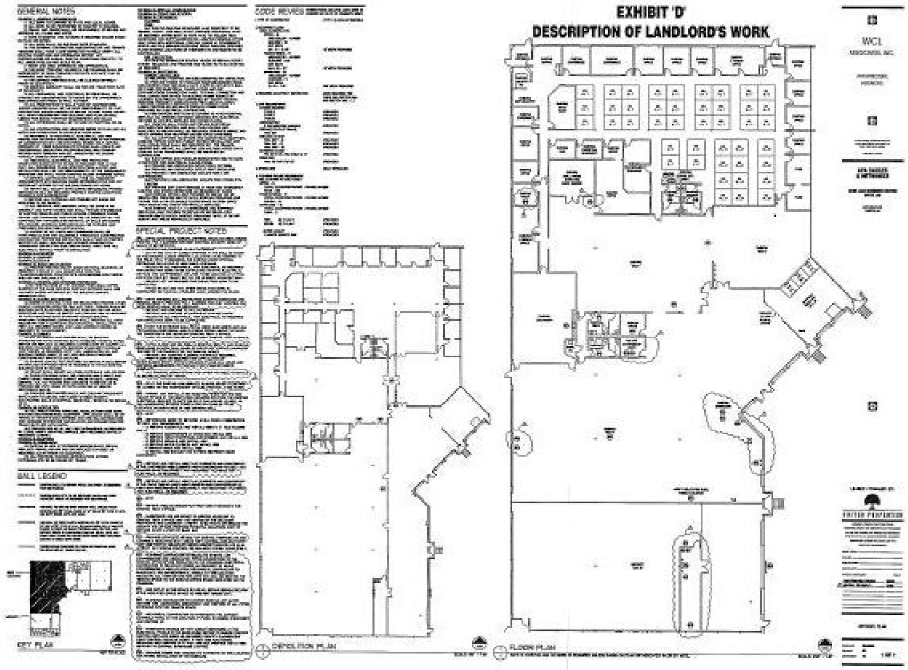

EXHIBIT E
FORM OF LETTER OF CREDIT

______, 2006

Irrevocable Letter of Credit No. ______________

Beneficiary:

Bass Lake Realty LLC
c/o Great Point Investors LLC
Two Center Plaza, Suite 410
Boston, MA 02108
Attn: Joseph A. Versaggi

Applicant:

APA Cables & Networks, Inc.
5480 Nathan Lane
Plymouth, MN 55442
Attn: Cheri Podzimek

Expiration Date: November 30, 2007

Ladies and Gentlemen:

________________ ("Issuer") hereby issues our Irrevocable Letter of Credit No. _____ in Beneficiary's favor in the amount of One Hundred Thousand ($100,000.00) U.S. Dollars available by your sight drafts drawn on us and accompanied by a written statement signed on behalf of Beneficiary, stating as follows:

Either: "The undersigned certifies that the Beneficiary is entitled to draw under the Irrevocable Letter of Credit No. _____ pursuant to the terms of a Lease, dated May____, 2006, as amended, between Beneficiary, as landlord, and Applicant, as tenant (the "Lease")."

Or: In the event that the Lease has not expired and/or this Irrevocable Letter of Credit has not been reduced to $0: "The undersigned certifies that the Beneficiary has received a written notice from the Issuer that Irrevocable Letter of Credit No. will not be renewed for an additional one (1) year period beyond the expiration date thereof."

Or: "The undersigned certifies that the Beneficiary is entitled to draw under the Irrevocable Letter of Credit No. ____ because Applicant has filed a voluntary bankruptcy petition under 11 USC 101 et seq., as amended, or under the insolvency laws of any jurisdiction."

Or: "The undersigned certifies that the Beneficiary is entitled to draw under the Irrevocable Letter of Credit No. _____ because an involuntary petition under 11 USC 101 et seq., as amended, or under the insolvency laws of any jurisdiction has been filed against Applicant."

Partial drawings are permitted.

Upon receipt of Exhibit A from Beneficiary, this Letter of Credit shall be automatically reduced.

We engage with you that all drafts drawn under and in compliance with the terms of this Irrevocable Letter of Credit will be duly honored if presented to us on or before the expiration date set forth above. Any draft drawn by you under this Irrevocable Letter of Credit must bear the clause "Drawn on Irrevocable Letter of Credit No. ______ of ____________________".

This credit is transferable in its entirety (but not in part). Any transferee shall succeed to all of the rights of the transferor hereunder. A transfer of the right to draw under this credit shall be effected by our receipt of this credit and a signed completed request for transfer in the form of Exhibit B hereto. We shall effect the transfer and advise the parties accordingly.

It is a condition of this Letter of Credit that it shall be considered automatically extended without amendment for one year from the present or any future expiration date unless we notify you in writing at least thirty (30) days prior to any such expiration date that this letter of Credit will not be renewed.

Notwithstanding any other provision herein this Letter of Credit will not extend beyond November 3 0,2013.

This Irrevocable Letter of Credit sets forth in full the terms of our undertaking, and such undertaking shall not in any way be limited, modified, amended or amplified, except by a written document executed by the parties hereto.

Except as otherwise expressly stated herein, this Irrevocable Letter of Credit is subject to the "International Standby Practices" (ISP98) International Chamber of Commerce (Publication No. 590)."

Very truly yours,

By: ______________________________

Name:

Title:

EXHIBIT A
Reduction Certificate

U.S. Bank National Association
800 Nicollet Mall, BC-MN-H20G
Minneapolis, Minnesota 55402

RE: Standby Letter of Credit Number XXXX
Dated: (ISSUE DATE)

To Whom It May Concern:

We hereby certify to U.S. Bank National Association that the available balance of Letter of Credit Number XXXXX may be reduced by $ _________ to a new balance of $ _________.

In witness hereof, I have executed and delivered this certificate as of the ____________________ day of ___________, 20__.

____
(BENEFICIARY'S NAME)

Its: ______________________

TRANSFER OF LETTER OF CREDIT IN ITS ENTIRETY
EXHIBIT B TO STANDBY LETTER OF CREDIT NO. XXXXX

TO: **U.S. BANK NATIONAL ASSOCIATION**
800 Nicollet Mali, BC-MN-H20G
Minneapolis, Minnesota 55402
612-303-7396/7395

FROM:

Re: Letter of Credit No. ____________ Issued by: U.S. Bank National Association

We, the undersigned beneficiary, hereby authorize and direct you to transfer irrevocably the referenced letter of credit in its entirety

To: ______________________________
Whose Address is: ______________________________
____
____
____

(Herein called the "transferee") with no changes in terms and conditions of the Letter of Credit.

We are returning the original instrument, including original amendments, if any, to you herewith in order that you may deliver it to the transferee together with your customary Letter of Transfer. Enclosed is our check/draft for the transfer fee of 0.25% of the face amount of the letter of credit (minimum $250.00).

Any amendments to the Letter of Credit that you may issue or receive are to be advised by you directly to the transferee, and the documents (including drafts if required under the Credit) of the transferee are to be processed by you (or any intermediary) without our intervention and without any further responsibility on your part to us.

We understand that pursuant to U.S. law, you are prohibited from issuing, transferring, accepting or paying letters of credit to any party or entity identified by the Office of Foreign Assets Control, U.S. Department of Treasury, or subject to the denial of export privileges by the U.S. Department of Commerce.

**THE SIGNATURE OF THE BENEFICIARY WITH TITLE AS STATED CONFORMS WITH THAT ON FILE WITH US AND IS AUTHORIZED FOR THE EXECUTION OF SUCH INSTRUCTION.

____
(Official Bank Stamp)

____
(Name of Bank)

____
(Address of Bank)

By: ______________________________
(Authorized Signature)

____
(Title)

____
(Telephone Number)

Date: ______________________________

____
(Name of Beneficiary)

By: ______________________________
(Authorized Signature)

____
(Title)

____
(Telephone Number)

Date: ______________________________

Exhibit 21

APA Enterprises, Inc. had two subsidiaries as of March 31, 2006, as set forth below. Both subsidiaries are wholly-owned by APA Enterprises, Inc.

Name	Jurisdiction of Incorporation
APA Cables and Networks, Inc.	Minnesota
APA Optronics (India) Private Limited	India

Exhibit 23.1

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We have issued our reports dated May 12, 2006, accompanying the consolidated finan-cial statements and schedule included in the Annual Report of APA Enterprises, Inc. on Form 10-K for the year ended March 31, 2006. We hereby consent to the incorporation by reference of said reports in the Registration State-ments of APA Enterprises, Inc. on Forms S-8 (File No. 333-74214, effective November 30, 2001; File No. 333-44500, effective August 25, 2000; File No. 333-44488, effective August 25, 2000; and File No. 333-44486, effective August 25, 2000).

/s/GRANT THORNTON LLP

Minneapolis, Minnesota
June 28, 2006

Exhibit 31.1

CERTIFICATION

I, Anil K. Jain, certify that:

1. I have reviewed this annual report on Form 10-K of APA Enterprises, Inc.;

2. Based on my knowledge, this annual 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 annual report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual 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 annual report;

4. APA Enterprises, Inc.'s other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a and 15(e)) for APA Enterprises, Inc. and we have:

   a) Designed such disclosure controls and procedures to ensure that material information relating to APA Enterprises, Inc., including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

   b) Evaluated the effectiveness of our disclosure controls and procedures as of a date and presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation.

   c) Disclosed in this report any change in APA Enterprises, Inc.'s internal control financial reporting that occurred during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's control over financial reporting.

5. APA Enterprises, Inc.'s other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to our auditors and the audit committee of our board of directors:

   a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect APA Enterprises, Inc.'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.

June 28, 2006

Signature: /s/ Anil K. Jain
Print Name: Anil K. Jain
Print Title: Chief Executive Officer and Chief Financial Officer

Exhibit 32.1

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 Annual Report of APA Enterprises, Inc. (the “Company”) on Form 10-K for the period ending March 31, 2006, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Anil K. Jain, Chief Executive Officer and 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, to the best of my knowledge 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 and Chief Financial Officer