

QUARTERLY REPORT 2

For the thirteen weeks
ended August 27, 2021



ENVIRONMENTAL TECTONICS CORPORATION

Quarterly Report
For the thirteen weeks ended August 27, 2021

County Line Industrial Park
125 James Way
Southampton, Pennsylvania 18966
(Address of Issuer's Principal Executive Office)

Telephone: (215) 355-9100

Website: www.etcusa.com

Investor Relations Contact:

Mark Prudenti, Chief Financial Officer
Environmental Tectonics Corporation
County Line Industrial Park
125 James Way
Southampton, PA 18966
Telephone: (215) 355-9100 ext. 1531
E-mail: mprudenti@etcusa.com
Website: www.etcusa.com

Table of Contents

Item 1.	Name of Issuer	Inside Cover
Item 2.	Security Information	1
Item 3.	Issuance History	1
Item 4.	Financial Statements	2
Item 5.	Description of Business Operations	6
Item 6.	Description of Facilities	17
Item 7.	Officers, Directors, and Control Persons	18
Item 8.	Legal/Disciplinary History.....	18
Item 9.	Third Party Providers	18
Item 10.	Management’s Certification.....	19

Item numbers above refer to the OTC Pink Basic Disclosure Guidelines created by the OTC Markets Group. The OTC Pink Basic Disclosure Guidelines are available on the Internet at <http://www.otcmarkets.com/marketplaces/otc-pink>.

When used in this Quarterly Report, except where the context otherwise requires, the terms “we”, “us”, “our”, “ETC”, and the “Company” refer to Environmental Tectonics Corporation and its subsidiaries.

Item 2. Security Information

Trading symbol: ETCC
CUSIP: 294092

Title of class of securities outstanding:	Common Stock	Preferred Stock, Series E
Par value:	\$0.05	\$0.05 (Stated value of \$1,000)
Total shares authorized:	50,000,000 as of August 27, 2021	25,000 as of August 27, 2021
Total shares outstanding:	9,443,785 as of August 27, 2021	12,127 as of August 27, 2021

Transfer Agent:

American Stock Transfer & Trust Company, LLC *
6201 15th Avenue
Brooklyn, NY 11219
Toll Free: (800) 937-5449
Telephone: (718) 921-8124
Website: www.astfinancial.com

* registered under the Exchange Act

List any restrictions on the transfer of security: N/A

Describe any trading suspension: N/A

List any stock split, stock dividend, recapitalization, merger, acquisition, spin-off, or reorganization either currently anticipated or that occurred within the past twelve months:

We have never paid any cash dividends on our Common Stock and do not anticipate that any cash dividends will be declared or paid on our Common Stock in the foreseeable future.

Dividends on the Company's Preferred Stock, as declared, are accrued according to the terms of the Preferred Stock and when paid, are paid in cash. The Preferred Stock is currently entitled to receive cumulative dividends at the rate of four percent (4%) per year in preference to the holders of the Company's Common Stock with respect to dividends. Series E Preferred Stock dividends accrued as of August 27, 2021, which totaled \$4,130 thousand, remained unpaid as of October 8, 2021, the date of issuance of the accompanying interim consolidated financial statements.

Item 3. Issuance History

- A. The nature of each offering of Common Stock in the last two fiscal years: N/A
- B. Any jurisdictions where the offering was registered or qualified: N/A
- C. The number of shares offered: N/A
- D. The number of shares sold: N/A
- E. The price at which the shares were offered, and the amount actually paid to the issuer: N/A
- F. The trading status of the shares: N/A
- G. Whether the certificates or other documents that evidence the shares contain a legend (1) stating that the shares have not been registered under the Securities Act and (2) setting forth or referring to the restrictions on transferability and sale of the shares under the Securities Act: N/A

Item 4. Financial Statements

Environmental Tectonics Corporation
Consolidated Statements of Operations and Comprehensive (Loss) Income
(unaudited)

<i>(in thousands, except per share information)</i>	Thirteen weeks ended		Twenty-six weeks ended	
	August 27, 2021	August 28, 2020	August 27, 2021	August 28, 2020
Net sales	\$ 4,386	\$ 4,354	\$ 10,466	\$ 9,268
Cost of goods sold	3,664	3,580	8,070	7,973
Gross profit	722	774	2,396	1,295
Operating expenses	1,863	2,321	3,585	4,314
Operating loss	(1,141)	(1,547)	(1,189)	(3,019)
Other expenses (income):				
Interest expense, net	138	181	289	337
Other expense (income), net	79	5	(2,330)	(12)
Other expenses (income), net total	217	186	(2,041)	325
(Loss) income before income taxes	(1,358)	(1,733)	852	(3,344)
Income tax provision	20	20	40	40
Net (loss) income	(1,378)	(1,753)	812	(3,384)
Loss attributable to non-controlling interest	8	35	11	37
Net (loss) income attributable to Environmental Tectonics Corporation	(1,370)	(1,718)	823	(3,347)
Foreign currency translation adjustment	(30)	(174)	17	54
Comprehensive (loss) income	\$ (1,400)	\$ (1,892)	\$ 840	\$ (3,293)
Preferred Stock dividends	(121)	(121)	(242)	(242)
(Loss) income attributable to common and participating shareholders	\$ (1,491)	\$ (1,839)	\$ 581	\$ (3,589)
Per share information:				
Basic earnings (loss) per common and participating share:				
Distributed earnings per share:				
Common	\$ -	\$ -	\$ -	\$ -
Preferred	\$ 0.02	\$ 0.02	\$ 0.04	\$ 0.04
Undistributed (loss) earnings per share:				
Common	\$ (0.10)	\$ (0.12)	\$ 0.04	\$ (0.23)
Preferred	\$ (0.10)	\$ (0.12)	\$ 0.04	\$ (0.23)
Diluted (loss) earnings per share	\$ (0.10)	\$ (0.12)	\$ 0.04	\$ (0.23)
Basic weighted average common and participating shares:				
Common weighted average number of shares	9,444	9,444	9,444	9,444
Participating preferred shares	6,125	6,125	6,125	6,125
Total basic weighted average common and participating shares	15,569	15,569	15,569	15,569
Diluted weighted average shares:				
Basic weighted average common and participating shares	15,569	15,569	15,569	15,569
Dilutive effect of stock options	-	-	-	-
Total diluted weighted average shares	15,569	15,569	15,569	15,569

The accompanying notes are an integral part of the consolidated financial statements.

Environmental Tectonics Corporation Consolidated Balance Sheets

<i>(in thousands, except share information)</i>	August 27, 2021 (unaudited)	February 26, 2021
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 618	\$ 961
Restricted cash	7,817	7,301
Accounts receivable, net	7,804	6,002
Contract assets	6,365	10,909
Inventories, net	1,519	1,705
Prepaid expenses and other current assets	2,046	783
Total current assets	26,169	27,661
Property, plant, and equipment, at cost, net	8,960	9,485
Right-of-use asset	527	780
Capitalized software development costs, net	52	46
Deferred tax assets, non-current, net	136	136
Total assets	\$ 35,844	\$ 38,108
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		
Current liabilities:		
Current portion of long-term debt obligations, net of debt issuance costs	\$ 15,669	\$ -
Accounts payable, trade	2,674	2,230
Contract liabilities	4,573	3,908
Accrued taxes	443	272
Accrued interest and dividends	4,176	3,936
Current portion of lease obligations	476	516
Other accrued liabilities, current	6,334	6,767
Total current liabilities	34,345	17,629
Long-term debt obligations, net of debt issuance costs:		
Credit facility payable to bank, net of debt issuance costs	3	16,984
Paycheck Protection Program loan	-	2,447
Total long-term debt obligations, net of debt issuance costs	3	19,431
Lease obligations, non-current	59	280
Other accrued liabilities, non-current	884	844
Total liabilities	35,291	38,184
Commitments and contingencies (Note 7)		
Shareholders' equity (deficit):		
Cumulative convertible participating Preferred Stock, Series E, \$0.05 par value, 25,000 shares authorized; 12,127 shares outstanding as of August 27, 2021 and February 28, 2020	12,127	12,127
Common Stock, \$0.05 par value, 50,000,000 shares authorized; 9,443,785 shares issued and outstanding as of August 27, 2021 and February 28, 2020	472	472
Additional paid-in capital	7,062	7,262
Accumulated deficit	(18,227)	(19,050)
Accumulated other comprehensive loss	(956)	(973)
Total shareholders' equity (deficit) before non-controlling interest	478	(162)
Non-controlling interest	75	86
Total shareholders' equity (deficit)	553	(76)
Total liabilities and shareholders' equity (deficit)	\$ 35,844	\$ 38,108

The accompanying notes are an integral part of the consolidated financial statements.

Environmental Tectonics Corporation
Consolidated Statements of Cash Flows
(unaudited)

<i>(in thousands)</i>	Twenty-six weeks ended	
	August 27, 2021	August 28, 2020
Cash flows from operating activities:		
Net income (loss)	\$ 812	\$ (3,384)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	598	563
Deferred income taxes	-	5
Increase (decrease) in allowance for doubtful accounts and inventory obsolescence	94	(2)
Forgiveness of Paycheck Protection Program loan	(2,447)	-
Stock compensation expense	42	42
Changes in operating assets and liabilities:		
Accounts receivable	(1,817)	4,384
Contract assets	4,544	(4,219)
Inventories	107	355
Prepaid expenses and other assets	(1,263)	154
Accounts payable, trade	444	(1,793)
Contract liabilities	665	(2)
Accrued taxes	171	(341)
Accrued interest and dividends	(2)	(5)
Other accrued liabilities	(401)	(226)
Net cash provided by (used in) operating activities	1,547	(4,469)
Cash flows from investing activities:		
Acquisition of property, plant, and equipment	(51)	(43)
Capitalized software development costs	(28)	-
Net cash used in investing activities	(79)	(43)
Cash flows from financing activities:		
(Repayments) borrowings under lines of credit	(1,312)	1,557
Proceeds from Paycheck Protection Program loan	-	2,447
Net cash (used in) provided by financing activities	(1,312)	4,004
Effect of exchange rate changes on cash	17	54
Net increase (decrease) in cash, cash equivalents, and restricted cash	173	(454)
Cash, cash equivalents, and restricted cash at beginning of period	8,262	9,090
Cash, cash equivalents, and restricted cash at end of period	\$ 8,435	\$ 8,636
Less: Restricted cash	(7,817)	(7,583)
Cash and cash equivalents at end of period	\$ 618	\$ 1,053
Supplemental schedule of cash flow information:		
Interest paid	\$ 282	\$ 360
Income taxes paid	\$ 5	\$ 2
Supplemental information on non-cash operating and investing activities:		
Preferred Stock dividends accrued during each respective fiscal period	\$ 242	\$ 242

The accompanying notes are an integral part of the consolidated financial statements.

Environmental Tectonics Corporation
Consolidated Statements of Changes in Shareholders' Equity (Deficit)
(unaudited)
(in thousands, except share information)

	<u>Common Stock</u>			<u>Additional Paid-in Capital</u>	<u>Accumulated Deficit</u>	<u>Accumulated Other Comprehensive Loss</u>	<u>Total Shareholders' Equity (Deficit)</u>
	<u>Preferred Stock</u>	<u>Shares</u>	<u>Amount</u>				
Balance, February 26, 2021	<u>\$ 12,127</u>	<u>9,443,785</u>	<u>\$ 472</u>	<u>\$ 7,262</u>	<u>\$ (19,050)</u>	<u>\$ (973)</u>	<u>\$ (76)</u>
Less: Prior year non-controlling interest	-	-	-	-	-	-	(86)
Net income attributable to Environmental Tectonics Corporation	-	-	-	-	823	-	823
Foreign currency translation adjustment	-	-	-	-	-	17	17
Preferred Stock dividends	-	-	-	(242)	-	-	(242)
Stock compensation expense	-	-	-	42	-	-	42
Balance before non-controlling interest, August 27, 2021	12,127	9,443,785	472	7,062	(18,227)	(956)	478
Non-controlling interest	-	-	-	-	-	-	75
Balance, August 27, 2021	<u>\$ 12,127</u>	<u>9,443,785</u>	<u>\$ 472</u>	<u>\$ 7,062</u>	<u>\$ (18,227)</u>	<u>\$ (956)</u>	<u>\$ 553</u>

The accompanying notes are an integral part of the consolidated financial statements.

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements
(unaudited)
(Dollars in thousands, except per share information)

Item 5. Description of Business Operations

ETC was incorporated in 1969 in Pennsylvania. For over five decades, we have provided our customers with products, services, and support. Innovation, continuous technological improvement and enhancement, and product quality are core values that are critical to our success. We are a significant supplier and innovator in the following areas: (i) software driven products and services used to create and monitor the physiological effects of flight, including high performance jet tactical flight simulation, fixed and rotary wing upset prevention and recovery and spatial disorientation, and both suborbital and orbital commercial human spaceflight, collectively, Aircrew Training Systems (“ATS”); (ii) altitude (hypobaric) chambers; (iii) hyperbaric chambers for multiple persons (multiplace chambers); (iv) Advanced Disaster Management Simulators (“ADMS”); (v) steam and gas (ethylene oxide) sterilizers; and (vi) environmental testing and simulation systems (“ETSS”). We operate in two primary business segments, Aerospace Solutions (“Aerospace”) and Commercial/Industrial Systems (“CIS”).

Aerospace encompasses the design, manufacture, and sale of: (i) ATS products; (ii) altitude (hypobaric) chambers; (iii) hyperbaric chambers for multiple persons (multiplace chambers); and (iv) ADMS, as well as integrated logistics support (“ILS”) for customers who purchase these products or similar products manufactured by other parties. These products and services provide customers with an offering of comprehensive solutions for improved readiness and reduced operational costs. Sales of our Aerospace products are made principally to U.S. and foreign government agencies and to civil aviation organizations. We offer integrated ATS products to commercial, governmental, and military defense agencies, and training devices, including altitude (hypobaric) and multiplace chambers (“Chambers”), to governmental and military defense agencies and civil aviation organizations both in the United States and internationally. We sell our ADMS line of products to governmental organizations both in the United States and internationally, original equipment manufacturers in the global special fire truck market (including Aircraft Rescue and Firefighting (“ARFF”) vehicles), fire and emergency training schools, universities, and airports. We also provide ILS for customers who purchase these products or similar products manufactured by other parties.

CIS encompasses the design, manufacture, and sale of: (i) steam and gas (ethylene oxide) sterilizers; and (ii) ETSS, as well as parts and service support for customers who purchase these products or similar products manufactured by other parties. Sales of our CIS products are made principally to the healthcare, pharmaceutical, and automotive industries. We sell our sterilizers to medical device manufacturers, pharmaceutical manufacturers, and universities. We sell ETSS primarily to commercial automotive and heating, ventilation, and air conditioning (“HVAC”) manufacturers. We also provide upgrade, maintenance, and repair services for our products and similar products manufactured by other parties.

The Company’s primary Standard Industrial Classification Code (“SIC Code”) is 3569. The Company’s fiscal year is the fifty-two week or fifty-three week annual accounting period ending the last Friday in February. References to the 2022 second quarter are references to the thirteen week period ended August 27, 2021. References to the 2021 second quarter are references to the thirteen week period ended August 28, 2020. References to the 2022 first half are references to the twenty-six week period ended August 27, 2021. References to the 2021 first half are references to the twenty-six week period ended August 28, 2020. References to fiscal 2022 are references to the fifty-two week period ending February 25, 2022. References to fiscal 2021 are references to the fifty-two week period ended February 26, 2021.

Note 1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying interim consolidated financial statements include the accounts of ETC and our 95%-owned subsidiary in Warsaw, Poland, ETC-PZL Aerospace Industries Sp. z o.o. (“ETC-PZL”). The Company’s corporate headquarters and main production plant (“ETC-SH”) are located in Southampton, Pennsylvania, USA. ETC-PZL manufactures certain simulators and provides software to support products manufactured domestically within our Aerospace segment. All significant intercompany accounts and transactions have been eliminated in consolidation.

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued

(Dollars in thousands, except per share information)

The accompanying interim consolidated financial statements have been prepared by ETC, without audit, in conformity with accounting principles generally accepted in the United States of America, consistently applied, and reflect all adjustments which, in the opinion of management, are necessary for a fair presentation of the results for the interim periods presented. All such adjustments are of a normal recurring nature.

Certain information in footnote disclosures normally included in financial statements prepared in conformity with accounting principles generally accepted in the United States of America has been condensed or omitted and the financial results for the periods presented may not be indicative of the full year's results; however, the Company believes that the disclosures are adequate to make the information presented not misleading. These interim consolidated financial statements should be read in conjunction with the audited financial statements and the notes thereto included in the Company's Annual Report to Shareholders for fiscal 2021 (the "2021 Annual Report").

Significant Accounting Policies Update

There have been no material changes in the Company's significant accounting policies during fiscal 2022 as compared to what was previously disclosed in the 2021 Annual Report.

Note 2. Earnings per Share

The Company utilizes the two-class method for computing and presenting earnings per share. The Company currently has one class of Common Stock (the "Common Stock") and one class of cumulative convertible participating Preferred Stock currently outstanding, Series E (the "Preferred Stock"). Under its terms, the Preferred Stock is entitled to participate in any cash dividends on a one-for-one basis for the equivalent converted common shares if the Preferred Stock were to be converted by the holder by the dividend record date; therefore, the Preferred Stock is considered a participating security requiring the two-class method for the computation and presentation of net income per share – basic.

The two-class computation method for each period segregates basic earnings per common and participating share into two categories: distributed earnings per share (i.e., the Preferred Stock stated dividend) and undistributed earnings per share, which allocates earnings after subtracting the Preferred Stock dividend to the total of weighted average common shares outstanding plus equivalent converted common shares related to the Preferred Stock. Basic earnings per common and participating share excludes the effect of Common Stock equivalents, and is computed using the two-class computation method.

Diluted earnings per share reflects the potential dilution that could result if securities or other contracts to issue Common Stock were exercised or converted into Common Stock. Diluted earnings per share continues to be computed using the if-converted method. Diluted earnings per share assumes the exercise of stock options and warrants using the treasury stock method. If the effect of the conversion of any financial instruments would be anti-dilutive, it is excluded from the diluted earnings per share calculation.

As of both August 27, 2021 and August 28, 2020, there was \$12,127 of cumulative convertible participating Series E Preferred Stock convertible at an exercise price of \$1.98 per share, equating to 6,124,567 shares of Common Stock, originally issued in July 2009.

As of August 27, 2021 and August 28, 2020, there were outstanding options to purchase the Company's Common Stock at an average price of \$0.95 totaling 1,017,450 and 1,027,450 shares, respectively. Due to the conversion price of Common Stock options, all 1,017,450 and 1,027,450 shares were excluded from the calculation of diluted earnings per share as of August 27, 2021 and August 28, 2020, respectively, because the effect of their conversion would be anti-dilutive.

Note 3. Revenue

The majority of our net sales are generated from long-term contracts with U.S. and foreign government agencies (including foreign military sales ("FMS") contracted through the U.S. Government) for the research, design, development, manufacture, integration, and sustainment of ATS products, including Chambers and the simulators manufactured and sold through ETC-PZL, collectively, Aeromedical Training Solutions. The Company also enters into long-term contracts with domestic customers for the sale of sterilizers and ETSS. Net sales of ADMS are generally much shorter term in nature and vary between domestic and international customers. We generally provide our products and services under fixed-price contracts.

Sales backlog (i.e., unfulfilled or remaining performance obligations) represents the sales we expect to recognize for our products and services for which control has not yet transferred to the customer. The estimated consideration is determined at the outset of the contract and considers the risks related to the technical, schedule, and cost impacts to complete the contract and an estimate of any variable consideration. We review these risks on a quarterly basis and may increase or decrease backlog accordingly. As the risks on such contracts are successfully retired, the estimated consideration from customers may be reduced, resulting in a reduction of backlog without a corresponding recognition of sales. As of August 27, 2021, our ending sales backlog was \$18,402. We expect to recognize approximately 66% over the next twelve (12) months and approximately 76% over the next twenty-four (24) months as revenue, with the remainder recognized thereafter.

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued

(Dollars in thousands, except per share information)

Comparability of our segment sales, operating income, and operating margin may be impacted favorably or unfavorably by changes in profit booking rates on our contracts for which we recognize revenue over a period of time using the percentage-of-completion cost-to-cost method to measure progress towards completion. Increases in the profit booking rates, typically referred to as risk retirements, usually relate to revisions in the estimated total costs to fulfill the performance obligations that reflect improved conditions on a particular contract. Conversely, conditions on a particular contract may deteriorate, resulting in an increase in the estimated total costs to fulfill the performance obligations and a reduction in the profit booking rate. Increases or decreases in profit booking rates are recognized in the current period and reflect the inception-to-date effect of such changes.

The aggregate impact of adjustments in contract estimates to net (loss) income attributable to ETC are presented below:

	Thirteen weeks ended					
	August 27, 2021			August 28, 2020		
	Aerospace	CIS	Total	Aerospace	CIS	Total
Net loss attributable to adjustments in contract estimates	\$ (4)	\$ -	\$ (4)	\$ (108)	\$ (212)	\$ (320)

	Twenty-six weeks ended					
	August 27, 2021			August 28, 2020		
	Aerospace	CIS	Total	Aerospace	CIS	Total
Net (loss) income attributable to adjustments in contract estimates	\$ (96)	\$ -	\$ (96)	\$ 571	\$ (212)	\$ 359

The following schedule presents the Company's net sales by segment, business unit, and geographic area for the 2022 second quarter compared to the 2021 second quarter:

	Thirteen weeks ended							
	August 27, 2021				August 28, 2020			
	Domestic	U.S. Gov't	Inter-national	Total	Domestic	U.S. Gov't	Inter-national	Total
Aerospace Solutions								
Aeromedical Training Solutions	\$ 36	\$ 268	\$ 1,813	\$ 2,117	\$ 50	\$ 1,119	\$ 1,044	\$ 2,213
Simulation (ADMS)	63	75	427	565	36	4	835	875
Subtotal	99	343	2,240	2,682	86	1,123	1,879	3,088
Commercial/Industrial Systems								
Sterilizers	974	-	(20)	954	362	-	(127)	235
Environmental (ETSS)	271	-	110	381	257	-	340	597
Service and Spares	369	-	-	369	434	-	-	434
Subtotal	1,614	-	90	1,704	1,053	-	213	1,266
Net sales total	\$ 1,713	\$ 343	\$ 2,330	\$ 4,386	\$ 1,139	\$ 1,123	\$ 2,092	\$ 4,354

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued
(Dollars in thousands, except per share information)

The following schedule presents the Company's net sales by segment, business unit, and geographic area for the 2022 first half compared to the 2021 first half:

	Twenty-six weeks ended							
	August 27, 2021				August 28, 2020			
	Domestic	U.S. Gov't	Inter-national	Total	Domestic	U.S. Gov't	Inter-national	Total
Aerospace Solutions								
Aeromedical Training Solutions	\$ 178	\$ 798	\$ 3,951	\$ 4,927	\$ 95	\$ 2,383	\$ 3,219	\$ 5,697
Simulation (ADMS)	334	80	736	1,150	38	8	1,156	1,202
Subtotal	512	878	4,687	6,077	133	2,391	4,375	6,899
Commercial/Industrial Systems								
Sterilizers	2,171	-	177	2,348	395	-	(106)	289
Environmental (ETSS)	717	-	312	1,029	876	-	378	1,254
Service and Spares	1,012	-	-	1,012	826	-	-	826
Subtotal	3,900	-	489	4,389	2,097	-	272	2,369
Net sales total	\$ 4,412	\$ 878	\$ 5,176	\$ 10,466	\$ 2,230	\$ 2,391	\$ 4,647	\$ 9,268

The Company's percentage of total recognized revenue by type of revenue was as follows:

Type of Revenue	Thirteen weeks ended	
	August 27, 2021	August 28, 2020
Products	72.2%	72.1%
Maintenance and support agreements	17.2%	10.1%
Services	7.7%	13.7%
Spare parts	2.9%	4.1%
Total	100.0%	100.0%

Type of Revenue	Twenty-six weeks ended	
	August 27, 2021	August 28, 2020
Products	63.6%	75.0%
Maintenance and support agreements	23.6%	10.0%
Services	9.4%	11.6%
Spare parts	3.4%	3.4%
Total	100.0%	100.0%

Note 4. Leases

The Company determines if an arrangement is a lease at the inception date. On the Consolidated Balance Sheets, operating leases are included in *Right-of-use asset*, with the related liabilities included in either *Current portion of lease obligations* or *Lease obligations, non-current*. Also on the Consolidated Balance Sheets, finance leases are included in *Property, plant, and equipment, at cost, net*, with the related liabilities included in either *Other accrued liabilities, current*, or *Other accrued liabilities, non-current*.

Right-of-use assets and operating lease liabilities are recognized based on the present value of the future minimum lease payments over the lease term at commencement date. If a lease does not implicitly state a rate, the Company uses its incremental borrowing rate based on the information available at commencement date in determining the present value of future payments. Variable components of the lease payments such as fair market value adjustments, utilities, and maintenance costs are expensed as incurred and not included in determining the present value. Lease expense for minimum lease payments are recognized on a straight-line basis over the lease term.

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued

(Dollars in thousands, except per share information)

The Company leases certain premises and office equipment under operating leases. As of August 27, 2021, these leases have remaining lease terms of one (1) month to twenty-two (22) months, with a weighted average remaining lease term of approximately thirteen (13) months. Maturities of operating lease liabilities are as follows:

<u>Fiscal Year</u>	<u>Amount</u>
Fiscal 2022	\$ 284
Fiscal 2023	268
Fiscal 2024	<u>2</u>
Total lease payments	554
Less: imputed interest	<u>(19)</u>
Total future long-term debt obligations	535
Less: current portion	<u>(476)</u>
Total future long-term debt obligations, less current portion	<u>\$ 59</u>

Total operating lease expense was \$154 for the 2022 second quarter, of which \$20 was attributable to variable lease expenses. For the 2021 second quarter, cash payments against operating lease liabilities totaled \$137.

Total operating lease expense was \$304 for the 2022 first half, of which \$34 was attributable to variable lease expenses. For the 2022 first half, cash payments against operating lease liabilities totaled \$273 and reclassifications of liabilities to comply with the presentation requirements of Accounting Standards Update (“ASU”) 2016-02, Leases (Topic 842) totaled \$11.

Note 5. Long-Term Obligations

On April 16, 2020, the Company was granted a loan from PNC Bank, National Association (“PNC Bank”) in the aggregate amount of \$2,447 pursuant to the Paycheck Protection Program (the “PPP”) under Division A, Title I of the CARES Act, which was enacted March 27, 2020. On June 10, 2021, subsequent to the end of the 2022 first quarter, the Company received notice of PPP forgiveness for the full amount of \$2,447 in principal and \$29 in interest. The forgiveness was accounted for as debt extinguishment, which resulted in a gain recorded as other income within our statement of operations.

On May 3, 2021, the Company entered into an amendment to the September 28, 2012 Loan Agreement with PNC Bank that provided for, among other things, the following:

- (i) The Revolving Line of Credit was decreased from \$25,000 to \$22,000, and was further reduced to \$20,000 on September 30, 2021.
- (ii) The maturity date of the 2016 PNC Credit Facilities was extended from June 30, 2021 to June 30, 2022.

Summary of Long-Term Debt Obligations

Long-term debt obligations consist of the following:

	August 27, 2021	February 26, 2021
	(unaudited)	
Credit facility payable to PNC bank	\$ 15,669	\$ 16,984
Borrowed under ETC-PZL Lines of Credit	3	
PPP loan	-	2,447
Total long-term debt obligations	15,672	19,431
Less: debt issuance costs	-	-
Total long-term debt obligations, net of debt issuance costs	15,672	19,431
Less: current portion	(15,669)	-
Total long-term debt obligations, net of debt issuance costs, less current portion	\$ 3	\$ 19,431

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued

(Dollars in thousands, except per share information)

Note 6. Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial and tax reporting purposes, as well as the valuation of net operating loss ("NOL") carryforwards and research and development tax credits. Valuation allowances are reviewed each fiscal period to determine whether there is sufficient positive or negative evidence to support a change in judgment about the realizability of the related deferred tax asset. Deferred tax assets and liabilities are offset and presented as a single non-current asset.

Generally, accounting standards require companies to provide for income taxes each quarter based on their estimate of the effective tax rate for the full year. The authoritative guidance for accounting for income taxes allows use of the discrete method when, in certain situations, the actual interim period effective tax rate may be used if it provides a better estimate of income tax expense.

An income tax provision of \$20, primarily related to an increase in unrecognized tax benefits, was recorded in both the 2022 second quarter and the 2021 second quarter. Effective tax rates were -1.5% and -1.2% for the 2022 second quarter and the 2021 second quarter, respectively. An income tax provision of \$40, also primarily related to an increase in unrecognized tax benefits, was recorded in both the 2022 first half and the 2021 first half. Effective tax rates were 4.7% and -1.2% for the 2022 first half and the 2021 first half, respectively. As of August 27, 2021, the Company had approximately \$24,698 of federal NOL carryforwards available to offset future income tax liabilities, \$19,958 of which begin to expire in 2025. The Company continues to record a valuation allowance on the entire NOL carryforward as it believes that it is more likely than not that the deferred tax asset associated with the NOL carryforwards will not be realized. The unrecognized tax benefits, which are recorded on the Company's balance sheet within other accrued liabilities, are primarily associated with U.S. federal tax issues such as the amount of research and development tax credits claimed and taxation of foreign earnings. Also included in these amounts are accruals for domestic state tax issues such as the allocation of income among various state tax jurisdictions.

Note 7. Commitments and Contingencies

Legal Proceedings

U.S. Air Force Research Altitude Chamber Contract

The Company was a party to a contract with the United States Air Force ("USAF"), namely a firm fixed-price contract dated June 14, 2010, to build a suite of research altitude chambers at the Wright-Patterson Air Force Base (the "RAC Contract"). Under the RAC Contract, the Company believed that the USAF had made changes to the scope and terms of said Contract that increased cost and resulted in delay to the program schedule. The Company made objection and claims with respect to these changes. Subsequent to the end of fiscal 2020, the parties executed a modification to the RAC Contract which, among other things, provided for the USAF's final acceptance, resulted in an addition to the RAC Contract base price of approximately two percent (2%), and resolved all potential claims regarding RAC Contract changes and program delay. All amounts owed pertaining to the RAC Contract have been collected.

International Aeromedical Center Contract

The Company is party to a contract with an international military customer to supply aeromedical training equipment and to provide certain equipment upgrades. The value of the contract is \$14,700. Due to delay in delivering the equipment required by the contract, the Company was notified that it was subject to liquidated damages of ten percent (10%) of the contract value. The parties have agreed to an additional \$201 reduction in the contract value (\$431 in total) and have signed a mutually agreeable document to further amend the contract value and delivery schedule. Subsequent to the issuance of the amended delivery schedule, the customer notified the Company of a construction delay unrelated to the Company's contract that will have an impact on the amended delivery schedule. At this time we are unable to predict the impact on the completion of the remainder of our contract.

Environmental Testing and Simulation Contract

The Company is a party to a contract to provide environmental testing and simulation equipment for use by a domestic original equipment manufacturer of transmissions and hybrid propulsion systems. Under the contract, there are unresolved discussions as to the scope of the contract's specification in addition to the Company believing that changes to the scope and terms of said contract has resulted in increased cost. The Company filed an action in the United States District Court for the Eastern District of Pennsylvania, alleging breach of contract. Discussions at an amicable resolution are ongoing and we do not at this time believe that this matter will have a material effect on the Company's financial position or results of operations.

Other Matters

Certain other claims, suits, and complaints arising in the ordinary course of business have been filed or are pending against us. We believe, after consultation with legal counsel handling these specific matters, all such matters are reserved for or adequately covered by insurance or, if not so covered, are without merit or are of such kind, or involve such amounts, as would not be expected to have a significant effect on our financial position or results of operations if determined adversely against us.

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued

(Dollars in thousands, except per share information)

Note 8. Subsequent Events

The Company has evaluated subsequent events through October 8, 2021, the date of issuance of the accompanying interim consolidated financial statements, and determined that there were no material subsequent events other than disclosed below requiring adjustment to, or disclosure in, the accompanying interim consolidated financial statements for the thirteen weeks ended August 27, 2021.

On September 27, 2021, the Company entered into the latest in a series of amendments to extend the period of due diligence related to an Agreement of Sale (the "Agreement") to sell its ETC-SH facility until October 11, 2021. The Agreement, originally entered into on June 18, 2021, provides the buyer with a period of due diligence during which it may elect not to proceed to closing. Per the terms of the Agreement, the sale, valued at \$4,700, excludes the aerospace training and research equipment listed in Item 6 of this report. The Agreement also provides that, following the closing, the Company shall remain in and occupy the facility pursuant to a lease, finalized prior to closing, with an anticipated term of approximately fifteen (15) years and other terms customary in the local market. The Company anticipates that closing on the sale may occur in the 2022 third quarter.

Management's Discussion and Analysis

Forward-looking Statements

Discussions of some of the matters contained in this Quarterly Report include forward-looking statements that may involve risks and uncertainties. Some of these discussions are contained under the caption "Management's Discussion and Analysis". We have based these forward-looking statements on our current expectations and projections about future events or future financial performance, which include implementing our business strategy, developing and introducing new technologies, obtaining, maintaining and expanding market acceptance of the technologies we offer, and competition in our markets. These forward-looking statements are subject to known and unknown risks, uncertainties and assumptions about ETC that may cause actual results, levels of activity, performance, or achievements to be materially different from any future results, levels of activity, performance, or achievements expressed or implied by these forward-looking statements.

These forward-looking statements include statements with respect to the Company's vision, mission, strategies, goals, beliefs, plans, objectives, expectations, anticipations, estimates, intentions, financial condition, results of operations, future performance, and business of the Company, including, but not limited to, (i) projections of revenues, costs of materials, income or loss, earnings or loss per share, capital expenditures, growth prospects, dividends, capital structure, other financial items, and the effects of foreign currency fluctuations, (ii) statements of our plans and objectives of the Company or its management or the Company's Board of Directors (the "Board of Directors"), including the introduction of new products, or estimates or predictions of actions of customers, suppliers, competitors, or regulatory authorities, (iii) statements of future economic performance, (iv) statements of assumptions and other statements about the Company or its business, (v) statements made about the possible outcomes of litigation involving the Company, (vi) statements regarding the Company's ability to obtain financing to support its operations and other expenses, and (vii) statements preceded by, followed by, or, that include, words such as "may", "will", "should", "expect", "plan", "anticipate", "believe", "estimate", "future", "predict", "potential", "intend", or "continue", and similar expressions. These forward-looking statements involve risks and uncertainties that are subject to change based on various important factors. Some of these risks and uncertainties, in whole or in part, are beyond the Company's control.

Results of Operations

Thirteen weeks ended August 27, 2021 compared to thirteen weeks ended August 28, 2020

Due to the nature of our business, we have historically experienced significant variability in our quarterly revenues, earnings, and other operating results, and our performance may fluctuate significantly in the future. This has been compounded since the 2021 first quarter due to COVID-19 global pandemic related lock downs, which have delayed orders and our ability to deliver.

Summary Table of Results

(unaudited)

<i>(in thousands, except per share information)</i>	Thirteen weeks ended		Variance (\$)	Variance (%)
	August 27, 2021	August 28, 2020		
Net sales	\$ 4,386	\$ 4,354	\$ 32	0.7
Cost of goods sold	3,664	3,580	84	2.3
Gross profit	722	774	(52)	(6.7)
<i>Gross profit margin %</i>	<i>16.5%</i>	<i>17.8%</i>	<i>-1.3%</i>	<i>-7.3%</i>
Operating expenses	1,863	2,321	(458)	(19.7)
Operating loss	(1,141)	(1,547)	406	(26.2)
<i>Operating margin %</i>	<i>-26.0%</i>	<i>-35.5%</i>	<i>9.5%</i>	<i>-26.8%</i>
Interest expense, net	138	181	(43)	(23.8)
Other expense, net	79	5	74	1480.0
Loss before income taxes	(1,358)	(1,733)	375	(21.6)
<i>Pre-tax margin %</i>	<i>-31.0%</i>	<i>-39.8%</i>	<i>8.8%</i>	<i>-22.1%</i>
Income tax provision	20	20	-	0.0
Loss attributable to non-controlling interest	8	35	(27)	(77.1)
Net loss attributable to ETC	\$ (1,370)	\$ (1,718)	\$ 348	(20.3)

Per share information:

Basic earnings (loss) per common and participating share:

Distributed earnings per share:

Common	\$ -	\$ -	\$ -	-
Preferred	\$ 0.02	\$ 0.02	\$ -	0.0
Undistributed loss per share:				
Common	\$ (0.10)	\$ (0.12)	\$ 0.02	(16.7)
Preferred	\$ (0.10)	\$ (0.12)	\$ 0.02	(16.7)
Diluted loss per share	\$ (0.10)	\$ (0.12)	\$ 0.02	(16.7)

Environmental Tectonics Corporation
Management's Discussion and Analysis, continued

Net Loss Attributable to ETC

Net loss attributable to ETC was \$1.4 million, or \$0.10 diluted loss per share, in the 2022 second quarter, compared to \$1.7 million during the 2021 second quarter, equating to \$0.12 diluted loss per share. The \$0.3 million variance is due to the combined effect of a \$0.5 million decrease in operating expenses, offset, in part, by a \$0.1 million decrease in gross profit and a \$0.1 million increase in other expense, net.

Net Sales

Net sales for both the 2022 second quarter and the 2021 second quarter were \$4.4 million. Although net sales remained flat, there was a shift in sales within Aeromedical Training Solutions from U.S. Government to International. There were also decreases in Simulation and ETSS sales to International customers that were offset by an increase in Domestic Sterilizers sales. Net sales were negatively impacted in both the 2022 second quarter and the 2021 second quarter due to the combination of a lower backlog entering fiscal 2021 compounded with the ongoing effects of the COVID-19 global pandemic, which has impacted the Company's ability to generate bookings, especially internationally.

Gross Profit

Gross profit for the 2022 second quarter was \$0.7 million compared to \$0.8 million in the 2021 second quarter, a decrease of \$0.1 million, or 6.7%. The decrease in gross profit was due primarily to the slight shift in net sales from Aerospace Solutions to CIS. Gross profit margin as a percentage of net sales decreased to 16.5% for the 2022 second quarter compared to 17.8% for the 2021 second quarter.

Operating Expenses

Operating expenses, including sales and marketing, general and administrative, and research and development, for the 2022 second quarter were \$1.8 million, a decrease of \$0.5 million, or 19.7%, compared to \$2.3 million for the 2021 second quarter. The decrease in operating expenses was due primarily to lower research and development expenses, for which there was an increase in offsetting reimbursements for research work performed internationally under government grant programs. There was also a decrease in general and administrative expenses due primarily to a reduction in legal fees now that the claim litigation pertaining to the RAC Contract has been settled, which was offset, in part, by a slight increase in selling and marketing expenses due to increase commission and travel related expenses.

Other Expense, Net

Other expense, net for the 2022 second quarter was \$79 thousand compared to \$5 thousand for the 2021 second quarter, an increase of \$0.1 million due primarily to higher letter of credit fees and realized exchange losses on foreign currency.

Environmental Tectonics Corporation
Management's Discussion and Analysis, continued

Gross Profit

Gross profit for the 2022 first half was \$2.4 million compared to \$1.3 million in the 2021 first half, an increase of \$1.1 million, or 85.0%. The increase in gross profit was due to the combined effect of an increase in net sales and an increase in gross profit margin. Gross profit margin as a percentage of net sales increased to 22.9% for the 2022 first half compared to 14.0% for the 2021 first half primarily due to the recognition in net sales of approximately \$3.0 million, or 28.3% of total 2022 first half net sales and 49.1% of the \$6.0 million International Aeromedical Training Solutions order, which traditionally produce our highest margins, received during the 2022 first quarter. The lower gross profit margin in the 2021 first half was a result of the lower net sales noted above not being able to support fixed overhead expenses.

Operating Expenses

Operating expenses, including sales and marketing, general and administrative, and research and development, for the 2022 first half were \$3.6 million, a decrease of \$0.7 million, or 16.9%, compared to \$4.3 million for the 2021 first half. The decrease in operating expenses was due primarily to lower research and development expenses, for which there was an increase in offsetting reimbursements for research work performed internationally under government grant programs, and lower general and administrative expenses, which included a reduction in headcount and legal fees now that the claim litigation pertaining to the RAC Contract has been settled.

Other Income, Net

Other income, net for the 2022 first half was \$2.3 million compared to other expense, net of \$12 thousand for the 2021 first half, an increase of \$2.3 million due almost entirely from accounting for the forgiveness of the PPP loan.

Cash Flows from Operating, Investing, and Financing Activities

During the 2022 first half, due primarily from a decrease in contract assets, offset, in part, by an increase in accounts receivable and an increase in prepaid expenses and other current assets, the Company was provided \$1.5 million of cash from operating activities compared to using \$4.7 million during the 2021 first half. Under Accounting Standards Codification ("ASC") 606, these accounts represent the timing differences of spending on production activities versus the billing and collecting of customer payments.

Cash used for investing activities primarily relates to funds used for capital expenditures of equipment and software development. The Company's investing activities used \$79 thousand during the 2022 first half compared to \$43 thousand during the 2021 first half.

The Company's financing activities used \$1.3 million of cash during the 2022 first half for repayments under the Company's credit facilities compared to providing \$4.0 million of cash during the 2021 first half with proceeds from the PPP loan and borrowings under the Company's credit facilities.

Item 6. Description of Facilities

We are an ISO 9001 certified manufacturer. We operate in four major locations consisting of manufacturing facilities, product development, and administration. A summary of square footage and use is presented below:

Location	Approximate Square Footage	Function	Owned/ Leased	Segment
Southampton, Pennsylvania *	83,800	Manufacturing (36,000 sq. ft.), NASTAR Center (22,100 sq. ft.), and Corporate Headquarters (25,700 sq. ft.)	Owned	Aerospace CIS
Orlando, Florida	8,700	Product development and administration	Leased	Aerospace
Warsaw, Poland	28,000	Manufacturing, product development, and administration	Leased	Aerospace
Ankara, Turkey	3,800	Software development	Leased	Aerospace CIS
Total	124,300			

* see Note 8 – Subsequent Events for additional disclosure relating to the Southampton, Pennsylvania location

We consider our machinery and plant to be in satisfactory operating condition, and adequate given our expected operations. Significant increases in the level of operations beyond what we expect in the current fiscal year might require us to obtain additional facilities and equipment.

Our National Aerospace Training and Research Center (the “NASTAR Center”), which is included in the Company’s Southampton, Pennsylvania owned property, includes the following aerospace training and research equipment:

- ATFS-400-25 PHOENIX High Performance Human Centrifuge;
- GYROLAB GL-2000 Advanced Spatial Disorientation Trainer;
- Altitude (Hypobaric) Chamber;
- Ejection Seat Simulator; and
- Night Vision Training System and Night Vision Goggle Training System.

Item 7. Officers, Directors, and Control Persons

	Name / Address **	Title	Ownership Percentage
Directors, Executive Officers, and Officers:	George K. Anderson, M.D.	Chairman of the Board of Directors	1.4%
	Linda J. Brent, Ed.D.	Director	1.1%
	Roger Colley	Director	1.1%
	Winston E. Scott	Director	1.2%
	Robert L. Laurent, Jr.	Chief Executive Officer, President, and Director	2.0%
	Mark Prudenti	Chief Financial Officer, Treasurer, and Corporate Secretary	1.2%
	Thomas G. Loughlin	Chief Operating Officer	1.3%
	Alper Kus	Senior Vice President, Aircrew Training Systems	*
Control Persons:	Estate of H.F. Lenfest <i>c/o The Lenfest Foundation Two Logan Square 100 N. 18th Street, Suite 800 Philadelphia, PA 19103</i>		*** 54.1%
	Peter H. Kamin and related family entities <i>2720 Donald Ross Road, 311 Palm Beach Gardens, FL 33410</i>		11.7%
	T. Todd Martin, III <i>50 Midtown Park East Mobile, AL 36606</i>		11.0%
	Estate of Pete L. Stephens		6.3%

* less than 1%

** address listed for all persons beneficially owning more than ten percent (10%)

*** the denominator for this ownership percentage calculation includes all participating preferred shares

Item 8. Legal/Disciplinary History

Information presented in the table above is accurate as of October 8, 2021, the date of issuance of the accompanying interim consolidated financial statements, based on information available to the Company. None of the foregoing Directors, Executive Officers, and Officers in the last ten (10) years has had a legal/disciplinary issue.

Item 9. Third Party Providers

Legal Counsel:

Lauletta Birnbaum
591 Mantua Blvd., Suite 200
Sewell, NJ 08080
(856) 232-1600

Independent Auditor:

RSM US LLP
751 Arbor Way
Blue Bell, PA 19422
(215) 641-8600

Item 10. Management's Certification

I, Mark Prudenti certify that:

- 1 I have reviewed this Quarterly Report of Environmental Tectonics Corporation;
- 2 Based on my knowledge, this disclosure statement 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 disclosure statement; and
- 3 Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations, and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.



Mark Prudenti
Chief Financial Officer, Treasurer, and Corporate Secretary
Date: October 8, 2021

I, Robert L. Laurent, Jr. certify that:

- 1 I have reviewed this Quarterly Report of Environmental Tectonics Corporation;
- 2 Based on my knowledge, this disclosure statement 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 disclosure statement; and
- 3 Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations, and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.



Robert L. Laurent, Jr.
Chief Executive Officer and President
Date: October 8, 2021