

AIRTECH INTERNATIONAL GROUP INC
Form SB-2/A
July 09, 2001

As filed with the Securities and Exchange Commission on July 9, 2001

Registration No. 333-60908

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

SECOND AMENDMENT TO FORM SB-2

REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933

Airtech International Group, Inc.
(Exact name of Registrant as specified in its charter)

Wyoming	3564	98-0120805
(State or other	(Primary Standard	(I.R.S. Employer
jurisdiction of	Industrial	Identification Number)
incorporation or	Classification Code	
organization)	Number)	

12561 Perimeter, Dallas, Texas 75228
(972) 960-9400
(Address and telephone number of Registrant's principal executive offices)

James R. Halter
Chief Financial Officer and General Counsel
Airtech International Group, Inc.
12561 Perimeter
Dallas, Texas 75228
(972) 960-9400

Copies to:
John G. Rebensdorf, Esq.
6116 N. Central Expressway
Suite 1313
Dallas, Texas 75206
(214) 696-9388
(Name, address and telephone number of agent for service)

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Approximate date of commencement of proposed sale to the public: From time to time after the effective date of this Registration Statement in light of market conditions and other factors.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box. [X]

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. []

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. []

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. []

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. []

Title of Each Class of Securities To Be Registered	Amount To Be Registered(2)	Proposed Maximum Offering Price Per Unit	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee(3)
Common Stock, \$0.05 Par Value(1).....	19,000,000	\$0.175	\$3,325,000	\$831

- (1) Includes shares of Common Stock which may be issued upon exercise of Common Stock Warrants and upon conversion of the Company's 12% Convertible Debentures or in payment of interest on the 12% Convertible Debentures by the Company. For purposes of estimating the number of shares of Common Stock to be included in this registration statement, the Company calculated 200% of the number of shares of Common Stock issuable upon conversion of the 12% Convertible Debentures and upon exercise of the Common Stock Warrants.
- (2) Also includes an indeterminate number of shares of Common Stock which may be issued with respect to such shares by way of a stock dividend, stock split, stock combination, recapitalization, merger, consolidation or otherwise in accordance with Rule 416.
- (3) The registration fee has been calculated in accordance with Rule 457(c) under the Securities Act of 1933, as amended, based upon the average of the closing bid and asked prices for the Registrant's Common Stock as reported on the OTC Bulletin Board on May 7, 2001. The registration fee was previously paid.

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The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until this Registration Statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.

+++++
+Information contained in this prospectus is subject to completion or +
+amendment. A registration statement relating to these securities has been +
+filed with the Securities and Exchange Commission on Form SB-2. These +
+securities may not be sold nor may an offer to buy be accepted prior to the +
+time the registration statement becomes effective. This prospectus shall not +
+constitute an offer to sell or the solicitation of an offer to buy nor shall +
+there be any sale of these securities in any state in which such offer, +
+solicitation or sale would be unlawful prior to registration or qualification +
+under the securities laws of any state. +
+++++

SUBJECT TO COMPLETION, DATED JULY 9, 2001

19,000,000 COMMON SHARES

AIRTECH INTERNATIONAL GROUP, INC.

Our common shares are traded on the over-the-counter Electronic Bulletin Board under the symbol "AIRG." The last reported sale price of our common shares on the OTC Bulletin Board on June 15, 2001 was \$0.14 per share. There is no public market for our warrants and we do not intend to list our warrants on any exchange.

This prospectus relates to the sale from time to time by the selling stockholders identified in the selling stockholder table appearing on page 14 of this prospectus of up to:

- . 1,200,000 shares of our common stock issuable upon exercise of the warrants;
- . 17,800,000 shares of our common stock issuable upon conversion of up to \$1,000,000 in principal amount of our 12% Convertible Debentures Due 2003.

We will receive no proceeds from the sale of our warrants or common stock by the selling stockholders identified in this prospectus. We will, however, receive proceeds from the sale of our common stock upon the exercise, if any, of the warrants.

You should read this prospectus and any supplement carefully before you invest in Airtech. This prospectus may not be used to make sales of our common stock or warrants unless accompanied by a prospectus supplement.

Investing in our common stock involves risks. Risk factors begin on page 5.

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Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this Prospectus is July , 2001.

The following table of contents has been designed to help you find important information contained in this prospectus.

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PROSPECTUS SUMMARY

This prospectus summary highlights selected information from this prospectus and does not contain all of the information that may be important to you. For a more complete description of this offering, you should read this entire prospectus as well as the additional documents we refer to under the heading "Where To Find Additional Information."

Our Company

Our principal business is the development, manufacturing, distribution and sale of air purification products for commercial and individual use. We currently manufacture and distribute a product line of purification units for commercial applications such as hotels, restaurants, bars, offices, print shops and casinos and residential purification units for individual use. We also manufacture and distribute a purification unit for use in automobiles, trucks

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and public transportation vehicles.

Our Products and Market

Our air purification products and technology can be applied to various commercial, residential, and medical markets. We market our air purification products through direct sales efforts from our principal offices, a distribution network with heating, ventilation and air conditioning companies and various industry distributors. We also market our products through our existing franchisees. We have also licensed the distribution rights to use our name and technology in the countries of Taiwan, the Philippines, Turkey, Canada, Spain, the Peoples Republic of China and countries in Central and South America. Our strategy is to identify national and international market niches which we believe are in need of air purification solutions and to exploit those markets through franchising, direct sales, licensing and strategic alliances with manufacturing representatives. The market for our products has grown based upon the increased public awareness of indoor air contamination. The Environmental Protection Agency has identified indoor air pollution as one of the five most urgent environmental crises in the United States. Air contamination includes bacteria, pollen, dust mites, smoke, plant and mold spores, dust, solvents, glues, formaldehyde, carbon monoxide and dioxide and various viruses.

Summary Financial and Other Data

We are providing the following summary financial information to aid you in your analysis of the financial aspects of an investment in us. The table includes summary historical financial data for Airtech for the years ended May 31, 1999 and 2000 and the nine months ended February 28, 2001 and pro forma accounting treatment reflecting the issuance of our 12% Debentures for the nine months ended February 28, 2001. We believe that this presentation is informative to you.

	Year Ended May 31, 1999	Year Ended May 31, 2000	Nine Months Ended February 28, 2001	Nine Months Pro Forma February 28, 2001
Assets.....	\$ 2,849,781	\$ 5,563,729	\$ 5,138,818	\$ 6,138,818
Total Stockholder's				
Equity (Deficit).....	\$ 366,612	\$ 373,894	\$ (335,827)	\$ 517,473
Retained Deficit.....	\$ 5,841,873	\$ 8,283,467	\$ 9,986,716	\$ 9,986,716
Revenues.....	\$ 1,030,469	\$ 1,627,476	\$ 1,437,617	\$ 1,437,617
Net Loss.....	\$ (4,311,459)	\$ (2,441,594)	\$ (1,703,249)	\$ (1,849,949)
Loss Per Share.....	\$ (0.41)	\$ (0.14)	\$ (0.07)	\$ (0.07)

Our Securities Purchase Agreement

On March 29, 2001, we entered into a securities purchase agreement with an investment group to raise up to \$1,000,000 through the sale to the investors of our 12% convertible debentures with attached warrants to purchase up to 600,000 shares of our common stock. Upon execution of the securities purchase agreement, the investors purchased \$800,000 in principal amount of our 12%

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debentures with attached warrants to purchase 500,000 shares of our common stock. The purchase price paid by the investors for the 12% debentures and attached warrants was \$800,000. Under the terms of the securities purchase agreement, the investors are obligated to purchase the remaining \$200,000 in principal amount of our 12% debentures with attached warrants to purchase 100,000 shares of our common stock on the date the registration statement relating to the common stock offered by this prospectus is declared effective by the SEC. This prospectus relates to the resale of our common stock by the selling stockholders identified in this prospectus either in the open market or pursuant to negotiated transactions.

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RISK FACTORS

Because we have a limited history of operations we may not be able to successfully implement our business plan.

We have only six years of operational history in our industry. Accordingly, our operations are subject to the risks inherent in the establishment of a new business enterprise, including access to capital, acceptance of our products in the market and limited revenue from operations. We cannot assure you that our intended activities or plan of operation will be successful or result in revenue or profit to us.

We have a history of losses and expect future losses.

We have incurred operating losses for our fiscal years ended May 31, 1999 and 2000 and the nine months ended February 28, 2001, and expect to sustain additional operating losses in the future. Our operating losses are attributable to the developing nature of our business and have resulted primarily from:

- . significant costs associated with the development of our products
- . marketing and distribution of our products
- . interest charges and expenses related to our current and previous debt and equity financings
- . minimal sales history of our recently developed products

If the proceeds from our recent debt offerings combined with our projected product sales are not sufficient to sustain our current business operations, our future profitability could be harmed substantially.

We have expended substantial capital in the development of our business and the development, marketing and distribution of our products. A substantial portion of these expenditures was made to improve the efficiency of our existing products and to develop new products. We cannot assure you that our recent expenditures will generate future revenues. Although we do not have a large capital expenditure program planned for fiscal year 2002, we will continue to incur expenditures in connection with our business operations, including the manufacturing, marketing and distribution of our existing products. Although we believe that our projected sales combined with the net proceeds from our recent debt offerings are sufficient to sustain our current business operations, we may require additional financing in the future. We cannot assure you that any required additional financing will be available to us or that any additional financing will not materially dilute the ownership of our stockholders. Our inability to secure any necessary funds to sustain our current business operations could severely limit our ability to manufacture,

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market and distribute our products and our future profitability.

Our 12% debentures contain an imbedded beneficial conversion feature. Conversion of a material amount of our 12% debentures could materially affect a stockholder's investment in Airtech.

As of April 30, 2001, \$800,000 in principal amount of 12% debentures were issued and outstanding. The 12% debentures are convertible into a number of shares of common stock determined by dividing the principal amount converted by the conversion price in effect. If converted on April 30, 2001, the 12% debentures would have converted into approximately 9,411,764 shares of our common stock. This number of shares, however, could be significantly greater in the event of a decrease in the trading price of our common stock. Purchasers of our common stock could therefore experience substantial dilution of their investment upon conversion of the 12% debentures. The 12% debentures are not registered and may be sold only if registered under the Securities Act or sold under an applicable exemption from registration. The shares of common stock into which the 12% debentures may be converted are being registered pursuant to the registration statement relating to this prospectus.

As of April 30, 2001, warrants to purchase 500,000 shares of common stock issued to the purchasers of the 12% debentures were outstanding. The warrants are exercisable over the next ten years at a price equal to

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the lesser of \$0.25 per share or a variable exercise price based upon the trading price of our common stock at the time of exercise. The exercise price of the warrants may be adjusted from time to time under certain antidilution provisions. The shares of common stock issuable upon exercise of the warrants are being registered pursuant to the registration statement relating to this prospectus.

Our 12% debentures are convertible by the debenture holders into shares of our common stock at any time at a conversion price equal to 50% of the market value of our common stock. Conversion of a material amount of our 12% debentures could significantly dilute the value of a stockholder's investment in Airtech.

Set forth in the table below is the potential dilution to the stockholders and ownership interest of the holders of our 12% debentures which would occur upon conversion of \$1,000,000 in principal amount of our 12% debentures. The calculations in the table are based upon the 30,991,578 shares of our common stock which are currently outstanding at 50% of the current market price of \$0.176 per share. The market price is based upon the ten day weighted average of the price of our common stock as quoted on the OTC Bulletin Board for the period from June 7, 2001 through June 17, 2001.

	Conversion at Current Market Price	Conversion at 25% Below Market Price	Conversion at 50% Below Market Price	Conversion at 75% Below Market Price
	-----	-----	-----	-----
Conversion Price.....	\$0.088	\$0.066	\$0.044	\$0.022
Shares Issued on Conversion.....	11,363,636	15,151,515	22,727,272	45,454,545

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Percentage of Outstanding				
Common Stock.....	26.8%	32.8%	42.3%	59.5%

Also, in the absence of a proportionate increase in our earnings and book value, an increase in the aggregate number of our outstanding shares of common stock caused by a conversion of the 12% debentures or exercise of the warrants would dilute the earnings per share and book value of all of our outstanding shares of common stock. If these factors were reflected in the trading price of our common stock, the potential realizable value of a stockholder's investment in Airtech could also be adversely affected.

As of April 30, 2001, we have reserved 5,800,00 shares of our common stock for issuance upon exercise of our outstanding warrants and options other than those issued in connection with the 12% debentures. We have reserved an additional 16,800,000 shares of common stock for issuance upon conversion of the 12% debentures and exercise of the attached warrants. As of April 30, 2001, the holders of our 6% debentures also have the right to convert the 6% debentures with attached warrants into approximately 13,800,000 shares of common stock.

A default by us under our 12% debentures would enable the holders of our 12% debentures to take control of substantially all of our assets.

Our 12% debentures are secured by a security agreement under which we pledged substantially all of our assets, including our goods, fixtures, equipment, inventory, contract rights and receivables. A default by us under the 12% debentures would enable the holders to take control of substantially all of our assets. The holders of our 12% debentures have no operating experience in the industry which could force us to substantially curtail or cease our operations. See "Events of Default" on page 12 of this prospectus for a detailed description of events of default under our 12% debentures.

Increased competition from our competitors could prevent us from penetrating new markets.

Our business is becoming increasingly competitive. Competition has increased with society's growing awareness of air quality problems and the related demand for air purification products. We believe competition will continue to increase with the identification of new markets, such as:

- . the food and beverage industry where smoking problems among smoking and non-smoking customers exist or local ordinances impose smoking restrictions

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- . the growth of cigar bars
- . the creation of smoking lounges in airports, office buildings, medical buildings and other public buildings
- . other smoking and non-smoking environmental demands
- . air contamination within hospitals and other medical facilities
- . air contamination within office buildings and other public buildings and facilities

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- . air contamination within vehicle air conditioning systems
- . air contamination within homes

As competition increases, we will compete with numerous companies in our market which have greater financial and technical resources than those available to us. Our inferior competitive position could have a material adverse affect on our ability to penetrate a new market and ultimately our profitability.

Increased technological developments in air purification products could render our products obsolete.

Our air purification products could be rendered noncompetitive or obsolete by future technological developments in our industry. We expect these technological developments to significantly increase competition in our industry. Many of the companies with which we compete and expect to compete have greater capital resources and more significant research and development staffs and marketing and distribution programs and facilities. Our ability to compete effectively may be adversely affected by the ability of these competitors to devote greater resources to technological developments and the sale and marketing of their products than us. Also, one or more of our competitors may succeed or may have already succeeded in developing technologies and products of which we are unaware and which may be more effective than the air purification products we are currently developing or marketing.

We may not receive approval codes for reimbursement of the cost of our Medicare Series 950 Unit which could significantly affect our future results of operations and profitability.

In October 1999, we applied to the Medicare Administration and, in February 2001, to the Health Care Financing Administration, for reimbursement code numbers for our Medicare Series 950 air purification unit. We cannot assure you that either of these applications will be approved by the appropriate agency which could significantly affect our future sales of the Medicare Series 950 and thus our operations and profitability.

Receipt of a reimbursement code number from the Medicare Administration would provide us with access to the large Medicare market. The reimbursement number would allow Medicare recipients to receive reimbursement for the cost of our Medicare Series 950. Issuance of the Medicare reimbursement number is within the sole discretion of the Medicare Administration and we cannot predict if, or when, we will receive Medicare approval.

Our application to the Health Care Financing Administration requests the issuance to us of a health care product code system number. This code number is commonly referred to in the medical insurance industry as an HCPCS Code. Although not as large a market as the Medicare market, the HCPCS Code would enable us to market our Medicare Series 950 directly to the private medical insurance industry. If a private insurance carrier accepts our Medicare Series 950 with the HCPCS Code, patients who purchase a Medicare Series 950 would be entitled to receive insurance reimbursement for the cost of the Medicare Series 950. If we receive a Medicare reimbursement code, we would automatically receive an HCPCS Code. If we obtain an HCPCS Code, however, we would not automatically receive a Medicare reimbursement code. We expect the Health Care Financing Administration to make a decision on our application on or before December 31, 2001.

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Approval of our Medicare Series 950 by either the Medicare Administration or the Health Care Financing Administration could significantly increase our profitability. We have not yet received approval of either of our applications and we cannot assure you that either application will be approved by the appropriate agency. If we do not receive Medicare approval or an HCPCS Code, we will continue to market our Medicare Series 950 through direct sales efforts and our existing distribution channels. To stimulate these sales efforts, we entered into an agreement with Southern Therapy, Inc. in April 2000 to market our Medicare Series 950 to home and durable medical equipment providers. We cannot assure you that our current marketing efforts will achieve the same sales results as we could achieve through Medicare approval or an HCPCS Code which could adversely affect our business and results of operations.

Our stock is traded on the OTC Bulletin Board and the tradability in our stock may be limited under the penny stock regulations.

Our common stock is traded on the OTC Bulletin Board under the symbol "AIRG". The OTC Bulletin Board is not a recognized national securities exchange. If the trading price of our common stock is less than \$5.00 per share, trading in our common stock would also be subject to the requirements of Rule 15c-9 under the Exchange Act. Under this rule, broker/dealers who recommend low-priced securities to persons other than established customers and accredited investors must satisfy special sales practice requirements. The broker/dealer must make an individualized written suitability determination for the purchaser and receive the purchaser's written consent prior to the transaction.

SEC regulations also require additional disclosure in connection with any trades involving a "penny stock", including the delivery, prior to any penny stock transaction, of a disclosure schedule explaining the penny stock market and our associated risks. Such requirements may severely limit the liquidity of our common stock in the secondary market because few brokers or dealers are likely to undertake such compliance activities. Generally, the term "penny stock" refers to a stock with a market price of less than \$5.00 per share which is not traded on a national securities exchange or quoted on NASDAQ. An active trading market in our common stock may never develop because of these restrictions.

There is a limited public market for our common stock and warrants and any future trading price of our common stock may decline, making it difficult for you to sell your stock.

Currently, there are a limited number of market makers for our common stock and there can be no assurance that a market for our shares will continue with any consistency. An illiquid market for our common stock may result in price volatility and poor execution of buy and sell orders for our investors. There is no public market for our warrants and we cannot assure you that one will develop. We do not intend to list our warrants on any exchange.

We depend on our key personnel for our future success including our founder, C J Comu.

Our future success depends to a significant extent upon the continued employment of our founder C J Comu. Competition for qualified personnel is intense in our industry, and we cannot assure you that we will be successful in attracting and retaining qualified, top-level personnel. The limited availability of qualified individuals could become an issue of increasing concern in the future. We do not maintain insurance on the lives of any of our officers or key employees. Our future success largely depends on the ability of our qualified personnel to manage and conduct our operations and implement our business plan. The loss of services of our founders or other key officers and directors could adversely affect our prospects for success.

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We recently suspended our franchise program and instituted a new program to market our residential products through distributors which may adversely affect our future sales.

We recently suspended our franchise program to market and sell our residential air purification products utilizing a retail store outlet concept. Since February 2000, we have sold 8 residential retail franchises of which 5 continue to operate. We suspended our retail franchise program to analyze whether the retail sale of our

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residential units is cost effective when compared to other direct sale distribution channels. We are currently marketing our residential products through direct sales from our corporate offices, manufacturing representatives and national distributors. We are also marketing our Medicare Series 950 to home and durable medical equipment providers through our agreement with Southern Therapy. We cannot assure you that these marketing efforts will be successful or that it will be economically feasible to reinstate our retail franchise program in the future. Either of these events could negatively impact our future residential product sales and thus our profitability.

We discontinued offering franchises to sell our commercial products and instituted a new program to sell these products through distributors which may adversely affect our future sales.

As of May 31, 2000, we had 18 franchisees who market our commercial products. During fiscal year 2000, we elected to discontinue offering additional commercial franchises. We elected to discontinue our commercial franchise program to enable us to pursue marketing our commercial products through manufacturing representatives and direct sales efforts from our corporate offices. In February 2001, we entered into an agreement with W&B Service Company for the exclusive national distribution of our commercial and automobile purification products. We cannot assure you that this new marketing approach for our commercial products will be successful. If unsuccessful, we may not be able to increase sales from our commercial products which could materially affect our future profitability.

We have not paid any dividends in the past and do not anticipate paying dividends in the future.

We anticipate using the proceeds received from our recent debt and equity sales and any future earnings to promote and increase our business and for other working capital uses. We have not paid or declared any dividends in the past. Based upon our present financial status and our contemplated financial requirements, we do not anticipate paying any dividends upon the shares offered by this Prospectus for the foreseeable future. While we may declare dividends at some time in the future, we cannot assure you of the timing of future dividends, if any.

FORWARD LOOKING STATEMENTS

The statements we make in this prospectus that are not historical fact are "forward-looking statements" as that term is defined in the Private Securities Litigation Reform Act of 1995. The words or phrases "will likely result," "are expected to," "will continue," "is anticipated," "believes," "estimates," "projects" or similar expressions are intended to identify these forward-looking statements. These statements are subject to risks and uncertainties beyond our reasonable control that could cause our actual business and results of operations to differ materially from those reflected in our forward-looking

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statements. The safe harbor provisions provided in the Securities Litigation Reform Act do not apply to forward-looking statements we make in this prospectus.

Forward-looking statements are not guarantees of future performance. Our forward-looking statements are based on trends which we anticipate in our industry and our good faith estimate of the effect on these trends of such factors as industry capacity, product demand and product pricing. In addition, our forward-looking statements are subject to our ability to reverse the current negative trend in our financial results.

The inclusion of projections and other forward-looking statements should not be regarded as a representation by us or any other person that we will realize our projections or that any of our forward-looking statements contained in this prospectus will prove to be accurate. We will not update any forward-looking statements other than as required by law.

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DESCRIPTION OF SECURITIES PURCHASE AGREEMENT

Our Agreement

On March 29, 2001, we entered into a securities purchase agreement with AJW Partners, LLC and New Millennium Partners II, LLC to raise up to \$1,000,000 through the sale to these investors of our 12% Convertible Debentures Due 2003 with attached warrants to purchase up to 600,000 shares of our common stock. Upon execution of the securities purchase agreement, the investors purchased \$800,000 in principal amount of 12% debentures with attached warrants to purchase 500,000 shares of our common stock. The purchase price paid by the investors for our 12% debentures and attached warrants was \$800,000 which represents the total amount we have received under the purchase agreement through April 30, 2001. Under the terms of our purchase agreement, the investors are obligated to purchase the remaining \$200,000 in principal amount of our 12% debentures with attached warrants to purchase 100,000 shares of common stock for a purchase price of \$200,000. The investors are obligated to purchase the additional 12% debentures on the date the registration statement relating to the common stock offered by this prospectus is declared effective by the SEC. If the registration statement is not declared effective, the investors have no obligation to purchase the additional 12% debentures or the attached warrants.

Description of 12% Debentures

Our 12% debentures have a maturity date of March 30, 2003 at which time the principal amount and all accrued interest on the 12% debentures is due and payable. Interest payments on the 12% debentures are due and payable quarterly commencing June 1, 2001 or at the option of the debenture holder upon conversion of the 12% debentures into shares of our common stock. If the debenture holder elects, we will pay any accrued interest on conversion by issuing shares of our common stock to the debenture holder at a price equal to the conversion price of our common stock as described below. The 12% debentures are secured by a security agreement under which we pledged substantially all of our assets, including our goods, fixtures, equipment, inventory, contract rights, and receivables.

The 12% debentures are convertible at any time at the option of the holder into shares of our common stock, provided at no time may a holder of our 12% debentures and its affiliates own more than 4.9% of our outstanding common stock without giving us 30 days prior written notice of the debenture holder's intent to waive the 4.9% ownership limitation. See "Limitation on Stock

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Ownership of Debenture Holder" on page 11 of this prospectus. The conversion price of our common stock used in calculating the number of shares issuable upon conversion, or in payment of interest on the 12% debentures, is the lesser of

- . 50% of the average of the lowest three trading prices of our common stock for the twenty trading days ending one trading day prior to the date we receive a conversion notice from a debenture holder; and
- . a fixed conversion price of \$0.25.

Also, under the terms of the 12% debentures, if we at any time

- . distribute any shares of our common stock in a consolidation, exchange of shares, recapitalization or reorganization, the 12% debenture holders are entitled to participate in the distribution as if the debenture holders had converted the 12% debentures;
- . distribute any of our assets to our stockholders as a dividend, stock repurchase, return of capital, or otherwise, the 12% debenture holders are entitled to participate in the distribution as if the debenture holder had converted the 12% debentures; or
- . issue or sell any shares of our common stock for no consideration or at a price less than \$0.25 per share, then the fixed conversion price of \$0.25 described above shall be reduced to the price per share we receive on the issuance or sale.

Our 12% debentures have an imbedded beneficial conversion feature which enables the debenture holders to convert the 12% debentures at the lesser of a 50% discount to the market price of our common stock and \$0.25 per share. As of the date of sale of the 12% debentures, the imbedded discount attributable to the 12%

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debentures was \$900,000. We have reflected this discount in our financial statements by writing off \$146,700 of the discount as of the date of sale of the 12% debentures. We will amortize the remaining \$753,300 of the discount over the three year term of the 12% debentures. If a 12% debenture is converted prior to the expiration of the three year term, we will write off to interest expense any remaining discount attributable to the converted 12% debenture.

Description of Warrants

The warrants purchased by the investors on March 29, 2001 entitle the investors to purchase 500,000 shares of our common stock at an exercise price equal to the lesser of

- . 90% of the average of the lowest three trading prices of our common stock for the twenty trading days ending one trading day prior to the date of exercise of the warrant; and
- . \$0.102 per share.

The warrants expire on March 29, 2004. The warrants are subject to exercise price adjustments upon the occurrence of certain events including stock dividends, stock splits, mergers, reclassifications of stock or our recapitalization. The exercise price of the warrants is also subject to reduction if we issue any rights, options or warrants to purchase shares of our common stock at a price less than the market price of our shares as quoted on

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the OTC Bulletin Board. Also, if at any time, we declare a distribution or dividend to the holders of our common stock in the form of cash, indebtedness, warrants, rights or other securities, the holders of the warrants are entitled to receive the distribution or dividend as if the holder had exercised the warrant.

The warrants attached to our 12% debentures have an imbedded beneficial exercise feature which enables the warrant holders to exercise the warrants at the lesser of a 10% discount to the market price of our common stock and \$0.102 per share. As of the date of sale of the warrants, the imbedded discount allocable to the warrants was \$100,000. The discount was determined from the Black-Scholes option pricing method. In our financial statements, we will amortize and write-off to interest expense the \$100,000 discount over the three year term of the warrants. If a warrant is exercised prior to the expiration of the three year term, we will write off to interest expense any remaining discount attributable to the exercised warrant.

Our Covenants with the 12% Debenture Holders

We may not, without the prior written consent of our 12% debenture holders, do any of the following:

- . pay, declare or set apart for payment any dividend or other distribution on shares of our capital stock other than shares issued in the form of a stock dividend;
- . redeem, repurchase or otherwise acquire any shares of our capital stock or any warrants, rights or options to purchase or acquire our shares of capital stock;
- . incur any indebtedness, except to trade creditors or financial institutions incurred in the ordinary course of our business or to pay the 12% debentures;
- . sell, lease or otherwise dispose of any significant portion of our assets outside of the ordinary course of our business;
- . lend money, give credit or make advances to any person or entity except in the ordinary course of our business;
- . negotiate with any party to obtain additional equity financing that involves the issuance of our common stock or securities convertible into our common stock for a period of 180 days from the date the registration statement relating to the securities offered by this prospectus is declared effective by the SEC;
- . conduct any equity financing during the period ending March 29, 2003 without providing the 12% debenture holders with the opportunity to participate in the equity financing on the same terms and conditions offered to the potential investors.

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Limitation on Ownership of our Shares of Common Stock by a 12% Debenture Holder

Our securities purchase agreement with the investors provides that at no time may a 12% debenture holder, together with its affiliates, maintain ownership of more than 4.9% of our outstanding common stock, unless the debenture holder gives us at least 30 days prior notice of their intent to waive the 4.9% ownership limitation.

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Registration Rights Agreement with the Investors

Simultaneously with the execution of the securities purchase agreement, we entered into a registration rights agreement with the investors. The securities offered by this prospectus are in compliance with our obligations under the registration rights agreement. The holders of the 12% debentures and attached warrants are also entitled under the registration rights agreement to certain "piggy-back" registration rights if we file a registration statement relating to the sale of securities for our own account. This means the holders of the warrants and 12% debentures may participate and sell shares in our public offering, except for shares registered by us for issuance under our employee stock option plans or in a merger or exchange in which our shares are issued in exchange for other securities.

Under the registration rights agreement, if the registration statement relating to the securities offered by this prospectus is not declared effective by the SEC on or before July 13, 2001, we are obligated to pay a registration default fee to the 12% debenture holders equal to \$2,000 for each \$100,000 in principal amount of outstanding 12% debentures. We are obligated to pay the default fee for each 30 day period, prorated for partial periods, that the registration statement is not declared effective. The default fee is due on the date the registration statement is declared effective and is payable in cash or at the option of the 12% debenture holder in shares of our common stock. Payments in shares of our common stock will be based upon the lowest three trading prices of our common stock for the twenty trading days prior to the payment date.

Consent and Standstill Agreement of 6% Debenture Holders

Our 6% debenture holders consented to the sale of our 12% debentures. The 6% debenture holders also agreed that neither they nor their affiliates would for a period beginning March 29, 2001 and ending 8 months from the date the registration statement relating to the securities offered by this prospectus is declared effective by the SEC

- . offer to sell, contract to sell, pledge, grant any rights or otherwise dispose of any shares of our common stock held by the 6% debenture holders without the prior consent of the 12% debenture holders; or
- . engage in any hedging transactions which are designed or reasonably expected to lead to or result in a disposition of the shares of our common stock held by the 6% debenture holders.

The 6% debenture holders may however

- . convert the 6% debentures into a maximum of 200,000 shares of our common stock per month on a non-cumulative basis; and
- . sell up to 100,000 shares per month of common stock converted after March 29, 2001 or 200,000 shares if the selling price is at least \$0.75 per share, with any unsold converted shares held in escrow by our legal counsel

Events of Default

If we commit an event of default under our agreements with the 12% debenture holders, the 12% debentures are immediately due and payable and we must pay to the 12% debenture holders an amount equal to the greater of

- . 120% of the outstanding principal amount plus accrued interest on the 12% debentures;

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- . or the value of the number of shares of our common stock into which the 12% debentures are convertible based upon the trading price of our common stock on the day preceding the date of payment.

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The 12% debenture holders would also have the right to exercise their rights under the security agreement securing the 12% debentures which could lead to control of substantially all of our assets.

Events of default include:

- . our failure to pay timely any principal and interest due on the 12% debentures;
- . our failure or inability to issue shares of our common stock upon conversion of the 12% debentures or exercise of the attached warrants;
- . our breach of any of the material covenants, representations or warranties included in the 12% debentures or the related securities purchase agreement; or
- . we file bankruptcy or a receiver or trustee is appointed for a substantial part of our business or assets.

PLAN OF DISTRIBUTION

The selling stockholders named in this prospectus or their pledgees, donees, transferees or other successors-in-interest are free to offer and sell their warrants and common stock at such times, in such manner and at such prices as they may determine. The types of transactions in which the warrants or common stock are sold may include transactions in the over-the-counter bulletin board market (including block transactions), negotiated transactions, the settlement of short sales of common stock, or a combination of these methods of sale. The sales will be at market prices prevailing at the time of sale or at negotiated prices. The transactions may or may not involve brokers or dealers. The selling stockholders have advised us that they do not have any agreements, understandings or arrangements with any underwriters or broker-dealers regarding the sale of their securities.

The selling stockholders may effect transactions by selling our warrants or common stock directly to purchasers or to or through broker-dealers, which may act as agents or principals. Broker-dealers may receive compensation in the form of discounts, concessions or commissions from the selling stockholders. Broker-dealers may also receive compensation from the purchasers of our warrants or common stock for whom they act as agents or to whom they sell as principal, or both. The compensation to a particular broker-dealer might be in excess of customary commissions.

The selling stockholders and any broker-dealer that acts in connection with the sale of warrants or common stock may be deemed to be an "underwriter" within the meaning of Section 2(11) of the Securities Act. Any commissions received by broker-dealers and any profit on the resale of our warrants or common stock sold by them while acting as a principal may be deemed to be underwriting discounts or commissions. The selling stockholders may agree to indemnify any agent or broker-dealer that participates in a transaction involving sales of our warrants or common stock against certain liabilities.

Because the selling stockholders may be deemed "underwriters" within the meaning of Section 2(11) of the Securities Act, the selling stockholders will be subject to prospectus delivery requirements. We have informed the selling

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stockholders that the anti-manipulation rules of the SEC, including Regulation M under the Exchange Act, may apply to sales by the selling stockholders in the market and have provided the selling stockholders with a copy of these rules and regulations.

USE OF PROCEEDS

We are registering our warrants and shares of common stock offered by this prospectus to satisfy our contractual obligation to the investors. We will not receive any of the proceeds from the sale of our warrants or common stock by the selling stockholders under this prospectus. We will, however, receive proceeds from the issuance of our common stock upon the exercise, if any, of our warrants.

On March 29, 2001, the investors purchased \$800,000 in principal amount of our 12% debentures with attached warrants to purchase 500,000 shares of our common stock. The purchase price for the 12% debentures

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and warrants was \$800,000. We intend to use the proceeds received from the sale of the 12% debentures as follows:

Reduction of payables.....	\$150,000
Inventory purchases.....	200,000
Product testing.....	110,000
Commissions and expenses on sale of 12% debentures.....	90,000
General corporate purposes.....	250,000

TOTAL.....	\$800,000
	=====

The investors are obligated to purchase an additional \$200,000 in principal amount of our 12% debentures on the date the registration statement relating to the common stock offered by this prospectus is declared effective by the SEC. We intend to use the proceeds from this additional sale of our 12% debentures for general corporate purposes.

INFORMATION ON SELLING STOCKHOLDERS

The following table includes certain information with respect to the selling stockholders as of April 30, 2001. The selling stockholders are not an affiliate of ours and have not had a material relationship with us or any of our predecessors or affiliates during the past three years. The selling stockholders are not registered broker-dealers or affiliates of any registered broker-dealers. The information listed below was furnished to us by the indicated selling stockholder. AJW Partners, LLC is a private investment fund that is owned by its investors and managed by SMS Group, LLC. SMS Group, LLC, of which Mr. Corey S. Ribotsky is the fund manager, will have voting and investment control over the shares listed below owned by AJW Partners, LLC. New Millennium Partners II, LLC is a private investment fund that is owned by its investors and managed by First Street Manager II, LLC. First Street Manager II, LLC, of which Mr. Glenn A. Arbeitman and Mr. Corey S. Ribotsky are the fund managers, will have voting and investment control over the shares listed below owned by New Millennium Partners II, LLC.

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Name -----	Beneficial Ownership of Common Stock as of April 30, 2001 -----	Maximum Number of Shares of Common Stock Offered for Sale -----	Approximate Percentage of Common Stock to be Owned After Offering -----
AJW Partners, LLC.....	6,377,647	12,350,000	0%
New Millennium Partners II, LLC.....	3,714,118	6,650,000	0%

The number of shares included in the above table represents an estimate of the number of shares of common stock to be offered by the selling stockholders. The actual number of shares of common stock offered by the selling stockholders is indeterminate, is subject to adjustment and could be materially less or more than the estimated number. The actual number of shares issuable upon conversion of the 12% debentures and exercise of the related warrants is dependent on the future market price of our common stock which we cannot predict. The actual number of shares of common stock offered in this prospectus, and included in the registration statement relating to this prospectus, includes an additional number of shares of our common stock which may be issued or issuable upon conversion of the 12% debentures and exercise of the related warrants because of any stock split, stock dividend or similar transaction involving our common stock, pursuant to Rule 416 of the Securities Act. Under the terms of the 12% debentures, if the 12% debentures were converted on April 30, 2001, the conversion price would have been \$0.085. Under the terms of the warrants, if the warrants were exercised on April 30, 2001, the exercise price would have been \$0.102 per share.

Under the terms of the 12% debentures and the related warrants, the 12% debentures are convertible and the warrants are exercisable by any holder only to the extent that the number of shares of our common stock issuable on conversion or exercise, together with the number of shares of our common stock owned by the

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holder and its affiliates (but not including shares of common stock underlying unconverted shares of 12% debentures or unexercised portions of the warrants) would not exceed 4.9% of our shares of outstanding common stock as determined in accordance with Section 13(d) of the Securities Exchange Act. Therefore, the number of shares of our common stock included in the above table exceeds the number of shares of common stock that a selling stockholder could own beneficially at any given time through its ownership of the 12% debentures and the warrants. For this reason, the beneficial ownership of our common stock by a selling stockholder included in the above table is not determined in accordance with Rule 13d-3 under the Securities Exchange Act.

AIRTECH INTERNATIONAL GROUP

Organization and Development

Airtech International Group, Inc. was incorporated in the State of Wyoming on August 8, 1991 under the name Interactive Technologies Corporation, Inc. Until May, 1998, Interactive Technologies was principally engaged in developing and producing interactive television and media programming for distribution through cable, broadcast, direct satellite television and the Internet. Interactive Technologies conducted this line of business through ownership of proprietary software and a trademark known as Rebate TV. Rebate TV offered

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network viewers rebates through an interactive program accessed by touch-tone phones. In addition, Interactive Technologies owned licensed rights obtained from the Federal Communications Commission to operate an interactive video and data service system in the Melbourne-Titusville, Florida metropolitan area. A second system owned by Interactive Technologies and located in the Charleston, South Carolina metropolitan area was sold in 1997.

On May 31, 1998, we acquired all of the outstanding shares of common stock of Airtech International Corporation, a Texas corporation. Airtech Corporation was founded in 1994 as a distributor of air purification products for Honeywell/Envirocaire. In January of 1996, Airtech Corporation outgrew the distributorship business and began manufacturing two of its own air purification products. The total purchase price of \$22,937,760.00 for the stock acquisition was paid through the issuance of 10,500,000 shares of Interactive Technologies' common stock, 11,858,016 shares of Interactive Technologies' Series "A" Convertible Preferred Stock and \$9,000,000.00 in principal amount of Interactive Technologies' convertible debentures. The shares of common stock and Series "A" preferred stock were each valued at \$0.625 per share. We accounted for the stock acquisition using the purchase method of accounting, with Airtech Corporation deemed the purchaser for purposes of our consolidated financial statements.

On July 31, 1998, the 11,858,016 shares of Series "A" preferred stock and the \$9,000,000 of convertible debentures, including accrued interest, were converted into 11,858,016 and 13,071,429 shares of our common stock. After conversion, the total number of outstanding shares of our common stock was approximately 50,000,000 shares. On October 5, 1998, our shareholders approved a one for five reverse split of our common stock which reduced the number of outstanding shares of our common stock to approximately 10,000,000 shares and increased the par value of our common stock from \$0.01 to \$0.05 per share. The reverse stock split was effective as of November 9, 1998.

In February 1998, we discontinued the original line of business of Interactive Technologies relating to interactive television and media programming, including the Rebate TV product. The software, trademark and license rights are the only assets of these discontinued lines of business. These assets have no carrying value on our financial statements because the products were discontinued prior to our acquisition of Airtech Corporation. We discontinued these original lines of business to enable us to concentrate on the development, manufacture, distribution and sale of the air purification products offered by Airtech Corporation and its subsidiaries. We are currently marketing the remaining assets for sale with no firm commitments or agreements in place.

Since the discontinuation of our original lines of business, we have been engaged with our wholly-owned subsidiaries, Airtech Corporation, Airsopure, Inc., and Airsopure International Group, Inc. in the development, marketing and sale of air purification systems for commercial, residential and automobile use. Airsopure was

incorporated on March 5, 1997 in the State of Texas to implement and operate a franchise program for the sale of commercial building air purification products developed and manufactured by Airtech Corporation. Airsopure International was incorporated on January 5, 2000 in the State of Nevada to implement and operate a franchise program to facilitate the opening of consumer retail stores for the sale of our residential air purification products.

On November 30, 1995, we incorporated McCleskey Sales and Service, Inc. in the State of Texas to integrate the distribution and sale of air purification

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products by Airtech Corporation with the heating, ventilation and air conditioning service business. Effective May 31, 1999, we discontinued the operations of McCleskey Sales based upon the incompatibility of the heating and air conditioning service business with Airtech Corporation's business of manufacturing and distributing high quality air purification products. Our cash expenses to discontinue the operations of McCleskey Sales were minimal.

In January 1999, we formed Airsopure 999, L.P., a Texas limited partnership, for the purpose of developing, marketing and distributing our Model S-999 automobile air purification system. Our wholly-owned subsidiary, Airsopure, is the general partner of the limited partnership.

In October 1999, we applied to the Medicare administration for a Medicare reimbursement code number for our Medicare Series 950. The reimbursement code number allows Medicare recipients to receive reimbursement for the cost of our Medicare Series 950. Our Medicare application is pending. We have not yet received approval for a specific reimbursement code number, although Medicare has allowed us to invoice Medicare using a non-assigned code number. The non-assigned code number does not guarantee Medicare reimbursement to Medicare recipients.

From February 2000 through June 2000, we opened four company owned retail stores in Addison, Texas, Arlington, Texas, Jackson, Tennessee and Kansas City, Missouri. During 2000, we sold the two stores located in Jackson, Tennessee and Kansas City, Missouri to the managers of those stores. We also consolidated the store located in Arlington, Texas with the store located in Addison, Texas. We opened these retail stores to facilitate the sale of our home consumer line of air purification products. We sold the store located in Addison, Texas in March 2001. As of April 30, 2001, we do not own any retail stores and do not intend to open any company owned stores in fiscal year 2002.

In February 2001, we applied to the Alpha Numeric Committee of the Health Care Financing Administration for a health care product code system number. The code number is commonly referred to in the medical insurance industry as an HCPCS Code. The HCPCS Code would enable us to market our Medicare Series 950 directly to the private medical insurance industry. If a private insurance carrier accepts our Medicare Series 950 with the HCPCS Code, patients who purchase a Medicare Series 950 would be entitled to receive insurance reimbursement for the cost of the Medicare Series 950. Our application is pending and we have not received an HCPCS Code.

On October 16, 1998, we changed our name from Interactive Technologies Corporation, Inc. to Airtech International Group, Inc. Our address is 12561 Perimeter, Dallas, Texas 75228. Our telephone number is (972) 960-9400 and our web site can be accessed at www.airtechgroup.com. The web site of Airsopure can be accessed at www.airsopure.com.

Business

We are engaged in the development, manufacturing, marketing and sale of indoor air purification products for commercial and residential use. We also manufacture and market an air purification system for use in automobiles. Our strategy is to identify those markets which we believe are in need of solutions to indoor air contamination problems. We propose to exploit these identified markets through direct sales, franchising, licensing and strategic alliances with manufacturing representatives.

Indoor air contamination exists in the form of particulates, gases or viruses in the air we breathe, whether in an office building, retail or

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commercial establishment or our homes. These air contaminants include bacteria, pollen, dust mites, smoke, plant and mold spores, dust, solvents, glues, formaldehyde, carbon monoxide, carbon dioxide, viruses, and diseases such as tuberculosis, meningitis, and hepatitis. Indoor air contaminants also include volatile organic compounds or "VOCs" which occur when airborne contaminants combine and become unstable. Examples of these volatile compounds are benzene, styrene, arsenic and polychlorinated biphenyls.

For millions of people, exposure to indoor air contaminants means experiencing headaches, watery eyes, dizziness, lethargy, digestive problems, nausea, nose and throat irritation. Historically, the methods of addressing and treating indoor air contamination were to open windows and doors to bring "fresh air" into an area or to use air cleaners such as ozone generators or electro-static air "cleaners" to attempt to purify the existing indoor air. We believe that these methods do not effectively handle the air contamination problems which exist today. Although considered effective at the time of conception, we regard these cleaners as obsolete in the current air purification marketplace.

Our air purification products provide an inexpensive solution to air contamination problems and concerns. Our products can be applied to various commercial and residential uses and are ideally suited for a variety of users that experience air contamination problems, including office buildings, restaurants, bars, public buildings, nursing homes, hospitals, schools, dental offices, waiting rooms, homes, airplanes, vehicles and residences. Our products substantially remove or destroy microorganisms in the air, eliminate organic odors and break down volatile compounds into harmless basic compounds.

Commercial Franchise Operations

We operate a franchise program designed to leverage our expertise with the energies and investment of a franchise network. We see this as a means of supplementing our revenues for cash flow purposes from franchise fees, sales of products to the market and royalty fees based upon the gross sales generated by the franchisee. We currently have 18 franchisees who sell our commercial products in various parts of the United States. These franchisees market and sell our commercial building products through franchise agreements with Airspure, Inc., our wholly owned subsidiary. Each franchise agreement has an initial term of five years and the franchisee may renew the franchise for successive additional five year periods. Five of our current franchises expire in fiscal year 2003 and thirteen in fiscal year 2004.

During fiscal year 2000, we elected to discontinue offering our commercial franchises through Airspure and began marketing our commercial products through direct sales efforts from our corporate office. We also implemented a program to pursue the marketing of our commercial products through manufacturing representatives. Based upon our estimate of approximately 260,000 manufacturing representatives nationwide, we believe this marketing approach will provide us with broader exposure of our commercial products. We also believe this broader exposure will increase the overall market of our commercial products above the levels previously recognized through our commercial franchise program.

Residential Franchise Operations

We also operate a franchise program designed to market our residential air purification units utilizing a retail store outlet concept. We operate this franchise program through Airspure International Group, Inc., our wholly owned subsidiary. Airspure International is qualified to offer our franchises in 38 states. The start-up costs for purchasing and establishing a retail store franchise range from \$90,000 to \$100,000, which includes up to a \$25,000 franchise fee to us. The remainder of the costs are estimates for the purchase

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of inventory, furniture and fixtures and minimum required working capital. Since February 2000, we have sold 8 residential retail franchises of which 5 are still operational.

We recently suspended our franchise program to market and sell our residential retail franchises. We suspended our retail franchise program to analyze whether the retail sale of our residential units is cost effective when compared to other direct sale distribution channels. We are currently marketing our residential

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products through direct sales from our corporate offices, manufacturing representatives, existing franchisees and national distributors. We are also marketing our Medicare Series 950 to home and durable medical equipment providers through our agreement with Southern Therapy.

Industry Overview

The Environmental Protection Agency has identified indoor air pollution as one of the five most urgent environmental concerns in the United States. According to the EPA, poor air quality may affect one third to one half of the commercial buildings in the United States. These affected commercial buildings are referred to in the industry as "sick buildings" and represent a potentially large market for our air purification systems. The term "sick building" can also be applied to any commercial or private environment where airborne contaminants pose a potential health hazard. The EPA asserts that the average American spends roughly 90 percent of his or her time indoors (Consensus 1988; EPA 1988) and can be breathing air more seriously polluted than outdoor air in even the largest and most industrialized cities. Government statistics indicate that 10 to 25 million people working in 800,000 to 1.2 million commercial buildings have developed respiratory symptoms related to indoor air pollution. These statistics translate to a loss in business productivity that we believe could approach \$60 billion a year. People in "vulnerable categories" are particularly sensitive to indoor air quality and indoor air pollution. These "vulnerable categories" include many older individuals, those individuals who are susceptible to allergies, asthma and other respiratory ailments, and young children. We estimate that more than 30 percent of the U.S. population falls within these categories.

The rising drug resistance within the U.S. population is also becoming a major health issue. There are approximately 160 antibiotics available to fight disease. Many of these antibiotics, however, are no longer effective on certain virulent organisms, including tuberculosis and certain types of hospital-based staphylococcus infections. Many viral and bacterial infections are airborne and are primarily transmitted through the air. The first line of defense against these diseases is prevention through improvement of indoor air quality.

Health experts have expressed special concern about people with asthma. These people have very sensitive airways that react to various irritants in the air which make breathing difficult. The number of people diagnosed with asthma has significantly increased in recent years. From 1970 to 2000, the number of asthmatics in the United States has increased 59 percent representing approximately 9.6 million people. We estimate that as of the year ended 2000, there are approximately seventeen million asthmatics in the United States. Asthmatics account for 500,000 hospitalizations and \$6.2 billion in health care costs annually. Asthma in children under 15 years of age has also increased 41 percent during the same period representing a total of 2.6 million children. The number of deaths from asthma has increased 68 percent since 1979 (Source: Asthma and Allergy Foundation of America).

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Bacteria, molds, pollen and viruses are types of biological contaminants. These biological contaminants breed in stagnant water and accumulate in air ducts, humidifiers, drain pans, and areas where water has condensed or collected on ceiling tiles, carpeting or insulation. Insect, bird and dust mite droppings can also be a source of biological contaminants. Physical symptoms related to biological contamination include fatigue, cough, chest tightness, fever, chills, head and muscle aches, and allergic responses such as mucous membrane irritation and upper respiratory congestion.

There is a growing awareness of the health hazards of airborne microbes, also referred to as bioaerosols. Bioaerosols are extremely small living organisms or fragments of organisms suspended in the air. Dust mites, molds, fungi, spores, pollen, bacteria, viruses, amoebas, fragments of plant materials, and human and pet dander are examples of bioaerosols. Bioaerosols are capable of causing severe health problems. Some bioaerosols, such as viruses and bacteria, cause infections, like a cold or pneumonia, and others cause allergic reactions. An allergic reaction occurs when a substance provokes formation of antibodies in a susceptible person. Bioaerosols may cause allergic reactions on the skin or in the respiratory tract. Rashes, hay fever, asthma, breathing difficulties, and runny noses are common allergic reactions.

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Bioaerosols build up in closed indoor environments and are passed through an entire building through central ventilation systems. The contamination of an entire building through bioaerosols is commonly referred to as "sick building syndrome." Bioaerosols are found in a variety of settings such as residences, office buildings, medical and dental offices and hospitals, but cannot be seen without a magnifying glass or microscope. Exposure to bioaerosols is much higher in most enclosed locations where people congregate, such as schools, theaters, airplanes, restaurants and shelters. Occurrences of sick building syndrome have escalated largely because of the increased demand for reduced operating costs in public buildings, particularly ventilation systems. The demand for reduced operating costs created construction of "tight" buildings which are dependent on mechanical air circulation systems rather than windows. These air circulation systems recycle bioaerosols throughout the building creating sick building syndrome.

Research has made it evident that air contaminants found in heating, ventilation and air-conditioning systems and airtight buildings are responsible to a large degree for sick building syndrome. The heating and air conditioning community and the American Society of Heating, Refrigeration and Air Conditioning Engineers have suggested that the use of higher ventilation rates utilizing fresh outside air would dilute air contaminants and alleviate the sick building syndrome to a great extent. In response to this suggestion and in an effort to improve air quality, building operators have increased ventilation by bringing in more fresh outside air. This process has resulted in increased building costs created by having to heat or cool and dehumidify the outside air. The process is also somewhat ineffective to the extent that polluted inside air is diluted with polluted outside air.

Products

Our product line consists of the following:

Series 12: Our Series 12 is designed to fit into a 2 x 4-foot space of a ceiling. This unit filters approximately 1200 cubic feet of air each minute removing particulates, gases and odors. Markets for this unit include the food and beverage industry, hospital and nursing homes, print shops, office buildings and other industries with problems involving cigarette or cigar

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smoke, odors and particulates. The retail price of our Series 12 is \$2,475.00. For the 30 months ended February 28, 2001, we have sold 314 of these units to our franchisees and national accounts.

Series 14: Our Series 14 is designed to mount against a wall at the joining point of the wall to the ceiling. The unit is approximately 36" x 14" x 14". The unit filters approximately 400 cubic feet of air per minute. Markets for this unit include those users having problems with any particulate, gas or odor found in rooms under 400 square feet, such as hotel rooms, offices, classrooms, patient rooms and small shops. Multiple units can be installed to accommodate larger rooms. The retail price of our Series 14 is \$1,090.00. For the 30 months ended February 28, 2001, we have sold 117 of these units to our franchisees and national accounts.

Series 18: Our Series-18 is a commercial unit which can service up to five offices or rooms with inexpensive flex duct work. The unit is installed above the ceiling and is out of view. The unit requires no modifications to the existing heating and air conditioning system and operates in a very quiet fashion. The retail price of our Series 18 is \$1,850.00. For the 30 months ended February 28, 2001, we have sold 50 of these units to our franchisees.

Series 30: Our Series 30 is in the preliminary marketing stage. The Series 30 is a residential unit which is adaptable to existing duct work used in existing heating, air conditioning and ventilation systems. The retail price of our Series 30 is \$970. For the two months ended February 28, 2001, we have sold 50 of these units.

Series 999: We developed our Series 999 as an automotive after market product for mounting in the trunk of new and used cars. The unit was designed to move 100 cubic feet of air per minute with complete air changes in an automobile every 20 seconds. The retail price of our Series 999 is \$354. For the 30 months ended February 28, 2001, we have sold 600 of these units. These sales were primarily to

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Airsopure 999, L.P. of which Airsopure, Inc., the Company's wholly owned subsidiary, is the general partner.

Medicare Series 950: Our Medicare Series 950 is a free standing, portable unit. In October 1999, our Medicare Series 950 unit was submitted to Medicare for approval and issuance of a Medical reimbursement code number. The Medicare reimbursement code number would enable Medicare recipients to receive reimbursement for the cost of the Medicare Series 950 unit. In February 2001, we also applied to the Health Care Financing Administration for an HCPCS Code. The HCPCS Code would allow us to market our Medicare Series 950 directly to private medical insurance carriers. We propose to offer our Medicare Series 950 to Medicare and private insurance recipients for a retail price of \$795. As of February 28, 2001, we have not sold any of our Medicare Series 950 units to either the Medicare or private insurance markets.

Consumer Series 950: Our Consumer Series 950 unit is similar to the Medicare Series 950 with alterations for a larger array of filtration for contaminants. The estimated retail price of the Consumer Series 950 is \$950.00. As of February 28, 2001, we have sold 438 of these units.

Down Draft Tables: Our down draft tables were designed for the nail manicure industry and first introduced in January 1996. The units have largely been discontinued with our remaining inventory of approximately 10

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units available for a retail price of \$2,000.00. We discontinued our down draft table line based upon a decline in market demand which resulted in production and marketing expenses exceeding proposed sales.

Replacement Filters: We manufacture our sorbent media filters by purchasing pre-filter material in bulk and cutting the material in our production facility to proper sizes to fit our units. Our hospital grade HEPA filters are out-sourced for production. The trisorbent filters are also outsourced for manufacture, but assembled at our production facility. The life of the filters required by our air purification units varies with the type of unit and the degree of contamination; however, we estimate that each unit sold will require an average of one to two complete filter changes per year. The filters required by our ceiling units have a retail price of \$268 to \$462 depending on uses. The automobile unit will require approximately \$100 in replacement filters per year and the portable residential units approximately \$150 per year.

Product Development and Redesign

We do not anticipate any major expenditures during fiscal year 2001 to develop or redesign our existing products or our products in the developmental stage which will not be offset by estimated product sales. Instead, we intend to focus our available capital resources on the marketing and distribution of our current line of marketable air purification products. We will, however, adapt or redesign our products to meet changing customer demands or to respond to requests in the market for made-to-order products. Our decision to redesign or develop a particular product will be based upon whether estimated sales to respond to a particular product need will be sufficient to offset estimated development or redesign costs.

We anticipate redesign costs on our Series 14 units and possibly our other units which utilize a hardened plastic case requiring injection molding. We estimate the engineering and mold tooling costs for these units to be in the range of \$500,000. We will not commit to these costs unless our estimated sales of these units are sufficient to offset the related development and design costs.

We also intend to evaluate the inclusion of photocatalytic oxidation technology into both our existing and developmental products for the purpose of increasing the air purification efficiency of these products. Photocatalytic oxidation occurs when ultra violet light waves are passed through a titanium screen creating a chemical reaction. The chemical reaction increases air purification efficiency by eliminating volatile compounds within the unit.

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Operations

We currently maintain a warehouse production facility of approximately 10,000 square feet in Dallas, Texas. In this facility, we are able to assemble a combined total of approximately 1,000 of our Series S-12, S-14, and S-18 units. We believe our warehouse facility is adequate for our current and estimated future production needs. The anticipated unit volume sales of the Series 999 automobile unit, the Series 950 unit and the S-30 unit during fiscal year 2001 caused management to select out-sourcing for production of these units.

Competing Products and Technologies

The current air filtration products and technologies available in the market

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which compete with our products include the following:

- . Activated carbon filters for use in heating, ventilation and air conditioning units
- . High Efficiency Particulate Air ("HEPA") filters
- . Ozone generators
- . Anti-microbial chemically treated filters
- . High energy UV light
- . Ionizers
- . Electrostatic precipitators
- . Media filtration
- . Photocatalytic oxidation technology
- . Various combinations of the above

These products and technologies are individually designed to provide various levels of "air filtration" of air contaminants and not "air purification." We believe a combination of several of these products and technologies must be implemented to achieve effective "air purification". The individual air purification ineffectiveness of these products is the result of the following factors:

Activated carbon filters absorb a number of volatile compounds and large microorganisms such as dust mite droppings, which stick to dust particles in the air, but do not remove other microorganisms from the air. The efficiency rate declines over time as the carbon filters are clogged with pollutants. The process alone is non-regenerating and the filters can be expensive to operate due to increased power usage resulting from pressure drops. These pressure drops occur when filters are clogged, thereby cutting the unit's capacity and ability to deliver air to remote areas. We use activated carbon filters in our products in combination with other air purification components.

HEPA filter technology reportedly removes up to 99.7% of air borne particles and is the dominant technology used in portable room air cleaners over the past six years. HEPA filters, however, are expensive to use in large applications such as multi-floor office buildings. HEPA filters are also ineffective in removing extremely small organic compounds, microorganisms and some viruses. HEPA filters are thick and produce pressure drops when installed within heating and air conditioning systems. These pressure drops increase maintenance and operating expenses. The increased expenses occur because the heating and air conditioning system must work continuously to compensate for pressure drops. On its own, HEPA technology does not have the ability to destroy bioaerosols or trap and breakdown volatile compounds or odors. Our products use HEPA filtration combined with other components of air purification.

Ozone generation is a type of air cleaner that uses a high-voltage electrical charge to change oxygen to ozone. A number of companies market ozone generators as indoor air cleaners. These ozone-producing units

break down volatile compounds because ozone is highly oxidizing. To achieve the high efficiency required, a very high level of ozone has to be released into

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the air. Ozone itself, however, is a respiratory irritant. OSHA has established a limit of workplace ozone levels over an eight-hour day. The FDA has also set a limit for ozone levels of electronic air cleaners. We do not employ ozone in our products.

Anti-microbial chemically treated filters can serve as a pre-filter to the more effective and expensive HEPA filter, capturing the larger particles flowing through the product and thereby prolonging the life of the HEPA filter, which captures the very small particles. On its own, an anti-microbial pre-filter can introduce additional contaminants into the air, such as volatile compounds, toxins, endotoxins, and allergens, by degrading microbial organisms trapped on the anti-microbial filter. We use these filters in our products in combination with other air purification components.

High energy UV light has proven to be effective in killing microbial life but is ineffective in destroying volatile compounds. High energy UV light, however, can pose a danger to humans similar to staring directly into sunlight. We use a level of UV light in several of our products which is not harmful to humans in combination with other air purification components.

Air cleaners such as ionizers can be up to 90% efficient which means they remove 90% of some types of pollutants. We are not aware of any medical evidence which recommends the use of ionizers to improve air quality for people suffering from asthma, allergies or upper respiratory problems. Most of these air cleaners ionize the air and place electrical charges on particles but do not have any charged collection plates. This means charged particles migrate through the air and stick to the first surface they run into such as walls, furniture or lung tissue. The charged particles remain on the surface until dislodged to re-enter the air again. We do not use ionizers in our products.

Electrostatic methods have no effect on the destruction of volatile compounds nor are they effective on small bioaerosols that are not attached to particulate matter. When electrostatic methods trap bioaerosols, either the bacteria will grow on the collection plates or if the bacteria is incapable of growing because of the rushing air past the surface, the bacteria will die, decompose and change to an organic compound and reenter the air stream. Electrostatic methods have no effect on reducing organic compounds or odors. We do not use electrostatic methods of air cleaning.

Charged media filters are made from an electric conducting material stretched across a frame. Applying a high electric voltage to the material creates an electrostatic field. However, these electrostatic fields are generally not sufficiently strong to eliminate most particles, severely reducing effectiveness. We do not use charged media filters in our products.

Photocatalytic oxidation creates a reduction in most volatile compounds. Photocatalytic oxidation occurs when ultra violet light waves are passed through a titanium screen creating a chemical reaction. The chemical reaction eliminates the volatile compounds collected in the air purification unit by reducing them to harmless components or carbon dioxide and water. We use photocatalytic oxidation in our products in combination with other air purification components.

Competition

Our business is becoming increasingly competitive. Competition has increased with society's growing awareness of air quality problems and the related demand for air purification technology. We compete in both the commercial and residential markets for air filtration and purification products.

The major competition for our products and markets is the domestic commercial and residential heating, ventilation and air conditioning market.

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This market is composed of a small number of large manufacturers. The two market leaders are the Carrier division of United Technologies and Trane Corp., a unit of American

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Standard. Carrier and Trane compete in all segments of our industry including commercial, residential, air conditioning, furnaces and heat pumps. Our other competitors include the following companies:

Fedders, Inc. (NASDAQ:FJC) is a holding company which manufactures and sells a full line of room air conditioners and dehumidifiers, principally for use in domestic residential markets.

Trion Inc., a newly acquired subsidiary of Fedders, Inc., has air purification operations which consist of two principal segments: engineered products and consumer products. The engineered products group designs, manufactures and sells commercial indoor air quality and dust collection equipment. The consumer products division manufactures and markets appliance air cleaners, including both table top and free standing console units.

Environmental Elements designs equipment and supplies systems and services to the air pollution industry through the design of large scale systems to control gaseous emissions. In addition, Environmental Elements designs electrostatic precipitators, fabric filters and scrubbing systems.

Honeywell, Inc. (NYSE:HON) has both commercial and consumer divisions of air filtration products with primary sales generated from the consumer division.

CECO Environmental Corp. (NASDAQ:CECE) has been in the air quality technologies and services business for over 30 years. CECO has expanded the applications for its technology to include wastewater treatment. CECO, through its four subsidiaries, provides a wide spectrum of air quality and wastewater treatment products and services. These products and services include industrial air filters, high performance filter fabrics, environmental maintenance, monitoring and management services, waste water treatment and air quality improvement systems. CECO is a full-service provider to the steel, aluminum, automotive, aerospace, semiconductor, chemical and metalworking industries.

United Air Specialists was established in 1966 to provide commercial and industrial environmental air cleaning solutions worldwide through a diverse product offering dust collection systems, industrial fluid coating systems and industrial oil cleaning equipment. The United Air product line includes the Smokeater, an electromatic precipitator cleaner. Designed to meet the needs of each customer, United Air equipment is backed by strong performance guarantees, technical support and years of experience.

Competition in the commercial indoor air quality market is very specialized with no one company offering a complete line of air filtration equipment. Commercial companies tend to specialize in very distinct market segments. In most major metropolitan areas of the United States, there are also various small commercial air filtration suppliers. We believe none of these suppliers has a product line competitive with our commercial units. In the residential indoor air quality market, many suppliers and manufacturers have a variety of air filtration products, generally in the lower retail price range of approximately \$250.

We are currently unaware of any company which manufactures or distributes a highly efficient or trunk-mounted air purification unit for the automobile comparable to our Series 999. We anticipate, however, that our proposed penetration of the automobile market will generate significant interest with

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competition coming from established automobile manufacturers.

We believe that the applications for our product lines will have broad appeal, since the implementation costs of our products are small compared to the cost benefits that typically accrue to the user. We also believe our technological approach of combining several air purification components into a single product is a superior method for removing and destroying pollutants in an indoor air environment. Some of the advantages and benefits of our products are as follows:

- . Biological air contaminants are substantially destroyed and or removed

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- . The process cleans and purifies the air through multiple air changes
- . The process is effective for microbes, endotoxins, toxins, allergens, and organic compounds
- . No toxic chemicals are employed
- . No ozone is generated or introduced into the air
- . The process works well at room temperature
- . The energy needs are low in stand alone systems outside of heating and air conditioning systems
- . Self-cleaning process does not reintroduce air contaminant residue into the air stream
- . After initial purchase, the products are very economical to operate, including the price of filter replacements

Markets

Our market research has identified the following markets which may benefit from our products:

- . Medical and specialty facilities such as hospitals, clinics, nursing homes, laboratories, day care centers, and emergency rooms. These facilities represent a large market for our products. Also, any facility where indoor air quality is critical to the safety and health of the patients/customers is a potential market.
- . The commercial heating, ventilation and air conditioning market consisting of office buildings and other public facilities.
- . The residential market consisting of homes with central heating, ventilation and air conditioning systems occupied by individuals with a need for better indoor air quality.
- . The industrial air quality market based upon increased local, state, and federal regulations which require cleaner indoor industrial air quality.
- . The transportation market consisting of automobiles, ambulances, buses, limousines, railroads, aircraft, and cruise ships which have a specific need for improved indoor air quality.
- . People who suffer from upper respiratory discomfort and allergic reactions due to poor indoor air quality at home, at work and in

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transportation vehicles.

- . People in vulnerable categories including older individuals in nursing homes and hospitals, individuals who are susceptible to allergies, asthma and other respiratory ailments, and young children.

Our technology provides an inexpensive solution to many of the indoor air quality problems which affect the daily lives of these individuals. Health conscious consumers are also becoming more particular about the air quality in their environments. We believe this trend will lead to an increase in demand for better air purification systems. We also believe that our combined technology approach will outrank the solutions provided by other air filtration systems that use traditional single methods for indoor air filtration and purification.

Business Plan and Marketing Strategy

Traditionally, air purification systems are marketed and sold through a single distribution channel comprised of heating and air conditioning contractors or repairmen. Our strategy is to approach the market through multiple distribution channels. We are not aware of any of our competitors who utilize a multiple channel approach. We have targeted several distribution channels for direct exposure of our products to educate consumers about the costs and solutions for indoor air contamination. We believe that this multiple channel

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approach combined with the quality of our products will separate us from our competition. For example, we currently utilize the following distribution channels:

Franchises. We currently have 18 commercial franchisees who market and sell our commercial building air purification products in various parts of the United States. We also have 5 residential retail franchisees who market and sell our residential air purification products. We provide a five day Indoor Air Quality Certification program for all of our approved franchisees. Each of our franchisees has a protected territory. We also coordinate an advertising program with our franchisees to provide an unlimited number of leads and future potential accounts to serve. Our franchisees are not required to exclusively market our products and may combine our products with competing products.

International Licenses. We have licensed the distribution rights to our name and technology in Turkey, Canada, Spain and Central and South America. Effective May 31, 2000, we entered into a development agreement with Aurora Products, Ltd. (Shanghai) for the distribution of our products in portions of Asia and the Pacific Rim through two subsidiaries of Aurora Products. Aurora Airsopure (China) markets our products in Hong Kong and the Peoples Republic of China. Aurora Airsopure (Asia) markets our products in Taiwan and the Phillipines. Aurora Airsopure (China) and Aurora Airsopure (Asia) each executed a \$500,000 demand promissory note payable to us in exchange for the distribution rights. The notes bear interest at 10% per annum with all principal and interest due May 31, 2008. As of April 30, 2001, we have received initial cash payments under each of the notes of \$40,200. Under the terms of the notes, the remaining principle balances are reduced based upon an allocation of 20% of purchase orders from us and 80% of gross sales by each distributor. As of April 30, 2001, we have allocated \$18,000 in principle reduction to the Aurora Airsopure (Asia) note.

Our existing international licenses are with one licensee for the entire

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country. We may in the future, however, divide a country into several licensed territories with multiple licensees. We intend to aggressively pursue additional international distribution relationships during fiscal year 2001. Our international licenses sell for a minimum of \$100,000 per country or a formula derived from guaranteed projected sales based upon the population of the licensed territory or country.

Manufacturer's Representatives. We estimate that there are approximately 260,000 heating and air conditioning representatives in the United States. This unconsolidated group of professionals accounts for a significant amount of the current sales of air purification and cleaning units. We intend to make our products available to these representatives through direct marketing efforts from our principal offices. As of April 30, 2001, we have entered into agreements with 30 local manufacturing representatives. These agreements include distribution agreements with Trinity Resources, Inc. for the exclusive distribution of our products through AES of Oklahoma (Carrier Corporation) in the State of Oklahoma and W&B Service Company for the exclusive national distribution of our commercial and automobile products in the United States and Canada.

Internet Sales. Internet usage has increased over the last several years and consumer purchasing is expected to continue to grow in accordance with this usage. Approximately 73% of website users search for information about products and services and 7.4 million users have made at least one purchase over the Internet. The demographics of website users also fit well with our products. Most website users are well educated and earn significantly more income than the national average. Our websites are www.airsopure.com or www.airtechgroup.com. Since June of 1999, the Airsopure website was accessed 104,994 times and the Airtech website 191,390 times. On these sites, visitors can educate themselves about our products, but cannot order our products on line.

We intend to spend additional funds to redesign and enlarge our websites in an effort to direct more Internet traffic to our websites. Our proposed redesign will include "hyper link" access to our products and the ability to order online. Hyper link access will enable website users to use generic words such as "air quality" or "air purification" for immediate referral to our website. Our websites also provide quicker advertising response times, direct feedback from customers and instantaneous updating of

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information. We believe the keys to successful marketing on the Internet will be exposure and association with other well-traveled websites, security, a clean design, ease of use and product testimonials.

Direct Sales. We currently market our products through our corporate offices to national accounts such as company owned or franchised TGI Fridays, Bennigan's and Sullivans, and other local and regional accounts involved in the food and beverage industry. We market our products directly and do not have agreements with any of these accounts. We also intend to employ the direct sales approach to school systems and government facilities during fiscal year 2001.

Retail Distribution. In February 2000, we opened our first company retail outlet in Addison, Texas to facilitate the retail sale of our home consumer products. Since February 2000, we also opened three additional retail outlets in Arlington, Texas, Jackson, Tennessee and Kansas City, Missouri. During August 2000, we sold the two stores located in Jackson, Tennessee and Kansas City, Missouri to the managers of those stores and consolidated the store located in Arlington, Texas with the Addison, Texas

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store.

The purchase price for each of the Jackson and Kansas City stores was \$15,000. The purchase price represents the purchase of existing inventory at the stores and the assumption by each purchaser of all lease and utility obligations. The purchase price is payable by each purchaser paying a premium for each unit of inventory purchased from us above the initial inventory. The inventory premium for the Jackson store is \$100 per unit and the Kansas City store is \$50 per unit. As of April 30, 2001, we have received \$2,600 on the sale of the Jackson store and \$2,500 on the Kansas City store.

In March 2001, we sold the store located in Addison, Texas for a purchase price of \$20,000. The purchase price was paid in \$4,000 cash and the assumption by the purchaser of all lease and utility obligations.

We are also actively pursuing the following additional distribution channels for our products:

Medicare and Durable Medical Equipment Distributors. Our research indicates that physicians regularly recommend the use of portable air filtration systems for patients suffering from chronic and acute episodes of illness related to allergies, asthma and general upper respiratory distress, many of whom are Medicare enrollees. These medical conditions are frequently elevated from a chronic status to acute episodes due to the inhaling by patients of various airborne contaminants. In the absence of a Medicare reimbursement code, Medicare patients are generally forced to incur the expense of such technology on a non-reimbursable basis.

In October 1999, we applied for a Medicare reimbursement code number for our Medicare Series 950. We have not yet received approval for a specific reimbursement code number to date, although Medicare has allowed us to invoice Medicare using a non-assigned code number. The use of the non-assigned code number does not guarantee Medicare reimbursement to Medicare recipients. We intend to continue the pursuit of the pending Medicare application by collecting and submitting additional information required by Medicare. The date of a final decision on our Medicare application cannot be determined at this time. The submission of additional information will allow Medicare to take additional time to evaluate our application. We cannot predict if, or when, Medicare will approve the Medicare Series 950 for direct cost reimbursement. We believe, however, that the time necessary to duplicate or invent the technology included in the Medicare Series 950, to create and test a prototype and to submit an application to Medicare gives us a competitive lead time advantage over our competitors in this market.

The Medicare reimbursement code is awarded through a review process conducted under the direction of the Health Care Financing Administration and its agencies that include the Statistical Agency for Durable Medical Equipment Regional Council and the Durable Medical Equipment Regional Council. Once awarded a Medicare reimbursement code, Medicare patients suffering from respiratory problems are able to secure through a variety of durable medical equipment providers, medical technology prescribed by their attending physicians that will be paid for by Medicare or their insurance carrier of record. Our research also indicates that third party payors such as managed care and indemnity insurance plans will

more readily reimburse patients for our Medicare Series 950 after the product receives a Medicare code. We estimate that approximately 31 million

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Medicare enrollees suffer from some sort of upper-respiratory problem. Although the number of Medicare enrollees has not changed significantly in the past three years, we believe that the number of enrollees will increase significantly in the future with the aging of the "baby boomers." These individuals represent the end-user market for our Medicare Series 950. We have also developed the Consumer Series 950 unit which is similar to the Medicare Series 950 unit with alterations for a larger array of filtration for contaminants.

In February 2001, we also applied to the Alpha Numeric Committee of the Health Care Financing Administration for a health care product code system number. The code number is commonly referred to in the medical insurance industry as an HCPCS Code. Although not as large a market as the Medicare market, the HCPCS Code would enable us to market our Medicare Series 950 directly to the private medical insurance industry. If a private insurance carrier accepts our Medicare Series 950 with the HCPCS Code, patients who purchase a Medicare Series 950 would be entitled to receive insurance reimbursement for the cost of the Medicare Series 950.

We have identified a national distribution network composed of durable medical equipment distributors that have existing sales forces and marketing infrastructures. Association with these distributors creates an immediate distribution network for the Medicare and Consumer Series 950 units. This distribution network would eliminate management challenges of creating and maintaining our own sales force or recreating the existing client bases of these distributors. The medical equipment distributors currently interact with physicians providing other medical devices such as walkers, wheelchairs, hospital beds and electronic monitoring devices. The Medicare and Consumer Series 950 units will be a new product for medical equipment distributors within an industry where the introduction of new products is not common. If we do not receive approval from Medicare of the Medicare Series 950, we intend to continue our efforts to market the Consumer Series 950 through direct sales to medical equipment distributors and by pursuing insurance carriers and health care providers outside of the Medicare system. To implement this marketing approach, we entered into an agreement with Southern Therapy, Inc. in April 2000 to market our Medicare Series 950 to home and durable medical equipment providers. We cannot predict or forecast the amount of any future sales which may be generated from the Medicare or Consumer Series 950.

Automobiles and Public Transportation. Our research indicates that there exists an increasing problem with abundant air contamination in automobiles and public transportation vehicles across the United States. Our research also indicates that not only is automobile air contamination immense and growing, but also that no real technological solutions are being applied to remove the harmful and irritating smells, gases and micro-particles that can cause and exacerbate respiratory problems. We have concluded that solving these issues for the public could provide tremendous economic rewards and higher auto resale values to a wide variety of customers, such as car rental companies, automobile dealers and government vehicles. One of the foremost complaints in the car rental industry and the new and used car industry, are the odors associated either with new material odors or with fabrics and materials in the automobile cabin that have absorbed pollutants like cigarette smoke for prolonged periods of time. The first indication that a problem exists is the odor detectable when the air conditioning unit or the air circulation system is activated. It is important, however, to note that the bacteria might be present before the odor is detected. This condition is caused by buildup of mold and bacteria in the air conditioner's evaporator. These fungi and spores can trigger allergic reactions and upper respiratory problems for car passengers.

Nearly 200 million vehicles are in use across the United States. Of

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these vehicles,

- . approximately 150 million are passenger vehicles,
- . approximately 2 million are owned by the major car rental companies, and
- . approximately 3 million vehicles are government owned and used.

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Each year in the United States, approximately 12 million new vehicles are sold by automobile dealers. The majority of automobiles fall into the category of used or more than one year old. The average American spends many hours per day in his vehicle. This much exposure, when added to outside contaminants such as road pitch, microscopic tire dust, allergens and hazardous gases and odors, leaves many car drivers with recurring headaches, eye irritation, nausea and even central nervous system problems. There are approximately 24,000 franchised new car dealers in the United States.

We believe that all of these vehicles represent potential installations for our Series S-999. We propose to initially penetrate this market through agreements with nationwide auto after-market companies. Our proposal is to wholesale our Series 999 automobile air purification unit for inclusion with other after-market packages offered in the auto after-market such as automobile customizing packages (custom pinstripping, gold ornamentation and custom wheel coverings), fabric sealants and window tints. We believe a very highly effective and affordable air purification device like our Series S-999 will be widely accepted in the automobile after-market. To implement our marketing strategy for the Series S-999, we are currently developing a marketing strategy with W&B Service Company, our North American distributor, to market the Series S-999 to auto after-market companies and the rental car, government vehicle, and automobile dealer markets.

Government Regulation

We operate under the disclosure document guidelines set forth by the Federal Trade Commission under an FTC Rule which became effective October 21, 1979. Under this FTC Rule, we are required to comply with the FTC disclosure format or issue a Uniform Franchise Offering Circular to all potential purchasers of a franchise. The uniform circular format is a standard form disclosure document which is accepted by the FTC and most states as an alternative to the FTC disclosure format. Our current uniform circular is compliant in 37 states. In addition to this format, fourteen states require additional information to be contained within the uniform circular for sales of new franchises within their states. We are approved in the State of California to offer our franchises, one of the additional information states. Although we intend to seek approval of our franchise in other additional information states in the future, we do not have any pending applications. Any violations under the FTC Rule are considered unfair or deceptive acts or practices within the meaning of Section 5 of the Federal Trade Commission Act. In response to the FTC Rule requirements, we formed wholly-owned subsidiaries, Airsopure, Inc., and Airsopure International Group, Inc., and registered each entity as a franchisor. Each entity is in compliance with the FTC Rules regarding its uniform circular.

Permits, Patents, Trademarks, Licenses and Copyrights

We do not own any patents or copyrights for our products or promotional

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materials. We do, however, have a registered trademark for the name "Airsopure" and the related service mark "The Essence of Clean Air." In addition, we have common law trademark protection for certain of our other trade names and service marks. We also intend to pursue copyrights for certain of our promotional and franchise training materials. While we believe our products are currently a unique implementation of filter and air purification components in the current market, our products are susceptible to duplication by utilizing current technology and components. Therefore, we do not believe any of our products are ultimately patentable and do not intend to apply for patent protection.

Suppliers

We purchase the supplies and materials used in our business from a number of suppliers. As of February 28, 2001, our five principal suppliers who provide us with materials used in our products were Revcor, Glasfloss, Tela Tool, Lesson Motor and RSE, Inc. We purchase motors, fans, filters and plastic casings from these suppliers. If we experience production difficulties from any of our principal suppliers, alternative suppliers and vendors exist in the marketplace. We may, however, experience production delays to enable an alternative supplier sufficient time to produce supplies to our specifications. We do not expect any delays to be material based upon our policy to maintain inventory levels necessary to avoid production delays.

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Estimate of Research and Development Expenditures

We incurred various research and development expenditures of approximately \$15,000 for the fiscal year ended May 31, 2000 and \$283,000 for the nine months ended February 28, 2001. These expenditures included salaries, materials, finished units, travel and correspondence.

Employees

As of April 30, 2001, we had 14 employees including one part-time employee.

Fiscal Year

Our fiscal year is from June 1 to May 31 of each year.

COMPANY PROPERTIES

We maintain our executive offices and a warehouse facility at 12561 Perimeter, Dallas, Texas. This facility has a total of approximately 10,400 square feet and a total rental cost for fiscal year 2000 of \$89,250. We are committed to our executive office and warehouse lease until August 15, 2001 and are currently in negotiations to renew our existing lease. We consider our facilities sufficient for our present and currently anticipated future operations and believe that these properties are adequately covered by insurance.

LITIGATION

In 1997, we were named as a defendant in a cause of action styled LLB Realty, L.P.C. v. Interactive Technologies Corp., Cause No. MER-L-1535-97, in the Superior Court of New Jersey, Mercer County. The complaint alleges damages relating to a lease agreement entered into with the plaintiff's for office facilities in New Jersey. We never occupied the space based upon the plaintiff (lessor) failing to finish-out the space pursuant to our specifications. The

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complaint alleges damages of approximately \$250,000. The court ruled in favor of the plaintiffs and set a hearing in June 2001 to determine damages. Although we are currently in negotiations for a favorable settlement relating to the complaint, the outcome of these negotiations is uncertain. We have established a reserve in our consolidated financial statements in the amount of \$200,000 in anticipation of a settlement.

On March 2, 2000, we were named as a defendant in a cause of action styled H.A.A., Inc. v. Airtech International Group, Inc., Cause No. 00CV-1603 (KMW), in the United States District Court for the Southern District of New York. The plaintiff is seeking the specific performance of an alleged contract providing for our sale to the plaintiff of 1,854,386 shares of our common stock for a cash purchase price of \$419,000. After the original filing, the plaintiffs amended their original complaint to include alleged damages of approximately \$1,000,000, as an alternative remedy to specific performance. On July 6, 2001, we entered into a settlement agreement with the plaintiffs. The terms and conditions of the settlement are subject to a confidentiality agreement with the plaintiffs. We do not believe, however, that the terms of the settlement will have a material adverse affect on our financial condition or future operations.

We have been named as a defendant in a number of routine lawsuits arising in the ordinary course of our business. In some of these cases a judgment was rendered against us. We have answered these routine causes of action where appropriate, negotiated settlements where appropriate and agreed to a payment schedule with respect to others. We have fully reserved for these claims and causes of action in our consolidated financial statements in the aggregate amount of \$45,000.

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MANAGEMENT'S DISCUSSION AND ANALYSIS

Background and General

In May 2000, we restated and refiled our financial statements for the year ended May 31, 1999 and the comparative period ended May 31, 1998. The reason for the restatement of our 1999 financial statements was to reflect the acquisition by Interactive Technologies Corporation, Inc., our predecessor in name, of all of the outstanding shares of common stock of Airtech International Corporation as a reverse merger as described below.

On May 31, 1998, Interactive Technologies acquired all of the outstanding shares of common stock of Airtech Corporation for a purchase price of \$22,937,760. Our prior 1999 financial statements reflected the combination between Interactive Technologies and Airtech Corporation as a merger using the purchase method of accounting with Interactive Technologies as the acquiring entity for legal and financial accounting and reporting purposes. This treatment resulted in reflecting the combination of Interactive Technologies' assets and the purchase of the goodwill and intellectual properties of Airtech Corporation at the appraised fair market value.

Our restated 1999 financial statements also reflected the merger between Interactive Technologies and Airtech Corporation utilizing the purchase method of accounting for Interactive's assets. Our 1999 restated financial statements, however, reflected the combination and purchase method as a reverse merger with Airtech Corporation as the acquiring entity for accounting and reporting purposes and Interactive Technologies as the surviving entity for legal purposes. As a result, Interactive Technologies effectively issued shares of common stock for the outstanding shares of Airtech Corporation, with the

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stockholders of Airtech Corporation ultimately acquiring control of Interactive Technologies. For this reason, Airtech Corporation is considered the acquiring entity for purposes of our 1999 restated financial statements.

On March 29, 2001, we entered into a securities purchase agreement with an investment group to raise up to \$1,000,000 through the sale to the investors of our 12% Convertible Debentures Due 2003 with attached warrants to purchase up to 600,000 shares of our common stock. Upon execution of the securities purchase agreement, the investors purchased \$800,000 in principal amount of 12% debentures with attached warrants to purchase 500,000 shares of our common stock. The purchase price paid by the investors for our 12% debentures and attached warrants was \$800,000 which represents the total amount we have received under the purchase agreement through April 30, 2001. Under the terms of our purchase agreement, the investors are obligated to purchase the remaining \$200,000 in principal amount of our 12% debentures with attached warrants to purchase 100,000 shares of common stock for a purchase price of \$200,000. The investors are obligated to purchase the additional 12% debentures on the date the registration statement relating to the warrants and common stock offered by this prospectus is declared effective by the SEC. If the registration statement is not declared effective, the investors have no obligation to purchase the additional 12% debentures or the attached warrants.

The conversion price of the 12% debentures and the exercise price of the attached warrants have a beneficial conversion and exercise feature enabling the holder of the securities to convert the 12% debentures or exercise the warrants at a discount to the market value of our common stock. For purposes of our financial statements the aggregate discount is \$1,000,000 which will be written off to interest expense. An amount of \$146,700 will be written off to interest expense as of the date of issuance of the 12% debentures and attached warrants. The remaining discount of \$853,300 attributable to the 12% debentures and attached warrants will be allocated to interest expense on an amortized basis over the three year term of the 12% debentures and warrants. If the 12% debentures are converted or the warrants exercised prior to the end of the three year term, any remaining discount attributable to the converted 12% debenture or exercised warrant will be written off to interest expense on the date of conversion or exercise.

Our current distributorship contractual agreement with Southern Therapy Inc. should result in additional sales to the medical market. In addition, our application for approval HCPCS Code for Series S-950 is in process. The actual granting of an HCPCS Code will not increase sales. We and our distributors, however, will

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be in a better position to market the Series S-950 to the larger medical insurance companies in the United States. The medical market, even without an HCPCS Code, could result in substantial sales. Our agreement with Southern Therapy calls for purchases of \$1,000,000 in the first year and substantial increases thereafter, however, Southern Therapy is under no obligation to purchase that amount.

We have also entered into a distributorship agreement with W & B Service, Inc. to serve as the commercial distributor for our commercial products in the United States and Canada. We cannot assure you that there will be additional sales for these markets, however, our contract requires W & B Service to purchase a minimum \$4,000,000 of our products during the first year, with increases in years two and three.

We believe that our recently completed financing resources along with increased sales of our products through industry distributors, increased

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foreign sales through in country distributors and increasing market acceptance of our new Model S-30 will enable us to aggressively pursue the indoor air purification market with adequate funding.

As the result of our distributorship agreements with Southern Therapy and W & B Services, we have decreased as of April 1, 2001 our corporate overhead by approximately \$75,000 per month. This represents a 40% decrease in our overhead expenses compared to August 2000. Our sales and marketing expenses will be absorbed by these new distributors. The lower profit margins on the sales through the distributors are expected to be mitigated by the increase in sales.

Results of Operations for Nine Months Ended February 28, 2001 Compared to the Nine Months Ended February 29, 2000

Revenues

Our consolidated total revenues for the nine months ended February 28, 2001 increased 84% or \$658,133 to total \$1,437,607 as compared to \$779,474 for the nine months ended February 29, 2000. This increase is due to sales of our products exceeding the prior period by \$808,133. The increase in sales was partially offset by a decrease of \$150,000 in franchise fee revenues and other income compared to the prior comparable nine-month period. We waived during the period franchise fees for prospective franchisees that possess direct marketing skills and indoor air quality experience. The waiver is in lieu of extensive training and start-up time lags which may exceed the waived franchise fee. We sold two new franchises for fees during the period as compared to one in the prior comparable nine month period.

Costs and Expenses

Our total costs and expenses increased \$575,195 or 24% to \$2,965,742 for the nine month period ended February 28, 2001 compared to \$2,390,547 for the prior comparable nine month period. Our costs and expenses are as follows:

Costs of sales increased \$265,108 to \$780,235 for the nine months ended February 28, 2001, compared to \$515,127 for the nine months ended February 29, 2000. The increase for the nine months ended February 28, 2001 is due to the product cost