
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

FORM 10-Q

(Mark One)

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

For The Quarterly Period Ended June 30, 2023

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

For the transition period from _____ to _____

Commission File No. 001-41096

Molekule Group, Inc.

(Exact name of Registrant as Specified in Its Charter)

Delaware
(State of Incorporation)

45-3213164
(I.R.S. Employer Identification No.)

**10455 Riverside Dr.
Palm Beach Gardens, FL 33410
833-652-5326**

(Address, including zip code, and telephone number, including area code, of principal executive offices of registrant)

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

| Title of each class | Trading Symbol(s) | Name of each exchange on which registered |
|--------------------------------|--------------------------|--|
| Common Stock, \$0.01 Par Value | MKUL | The Nasdaq Capital Market |

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

| | | | |
|-------------------------|-------------------------------------|---------------------------|-------------------------------------|
| Large accelerated filer | <input type="checkbox"/> | Accelerated filer | <input type="checkbox"/> |
| Non-accelerated filer | <input checked="" type="checkbox"/> | Smaller reporting company | <input checked="" type="checkbox"/> |
| | | Emerging growth company | <input checked="" type="checkbox"/> |

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

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

The registrant has one class of common stock, \$0.01 par value, of which 34,654,459 shares were outstanding as of August 9, 2023.

MOLEKULE GROUP INC.
FORM 10-Q
TABLE OF CONTENTS

| | |
|---|----|
| <u>PART I – FINANCIAL INFORMATION</u> | |
| <u>Item 1. Condensed Consolidated Financial Statements (Unaudited)</u> | |
| <u>Condensed Consolidated Balance Sheets as of June 30, 2023 (Unaudited) and December 31, 2022 (Audited)</u> | 1 |
| <u>Condensed Consolidated Statements of Operations for the Three and Six Months Ended June 30, 2023 and 2022 (Unaudited)</u> | 2 |
| <u>Condensed Consolidated Statements of Changes in Stockholders’ Equity for the Three and Six Months Ended June 30, 2023 and 2022 (Unaudited)</u> | 3 |
| <u>Condensed Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2023 and 2022 (Unaudited)</u> | 4 |
| <u>Notes to Condensed Consolidated Financial Statements (Unaudited)</u> | 5 |
| <u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u> | 23 |
| <u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u> | 32 |
| <u>Item 4. Controls and Procedures</u> | 32 |
| <u>PART II - OTHER INFORMATION</u> | 32 |
| <u>Item 1. Legal Proceedings</u> | 32 |
| <u>Item 1A. Risk Factors</u> | 33 |
| <u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u> | 33 |
| <u>Item 3. Defaults Upon Senior Securities</u> | 33 |
| <u>Item 4. Mine Safety Disclosures</u> | 33 |
| <u>Item 5. Other Information</u> | 33 |
| <u>Item 6. Exhibits</u> | 33 |
| <u>SIGNATURES</u> | 35 |

PART I – FINANCIAL INFORMATION**Item 1. Condensed Consolidated Financial Statements (Unaudited)****MOLEKULE GROUP, INC. AND SUBSIDIARIES (f/k/a AEROCLEAN TECHNOLOGIES, INC.)
CONDENSED CONSOLIDATED BALANCE SHEETS**

| | <u>June 30, 2023</u> (Unaudited) | <u>December 31, 2022</u> (Audited) |
|---|-------------------------------------|---------------------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash | \$ 5,269,376 | \$ 22,062,657 |
| Restricted Cash | 629,742 | — |
| Accounts receivable, net | 2,210,700 | 36,188 |
| Prepaid expenses and other current assets | 1,801,533 | 665,395 |
| Inventories | 29,432,880 | 2,020,713 |
| Total current assets | <u>39,344,231</u> | <u>24,784,953</u> |
| Property and equipment, net | 8,626,031 | 2,119,134 |
| Intangible assets, net | 45,301,689 | — |
| Goodwill | 21,031,064 | 626,647 |
| Operating lease right-of-use assets | 10,952,143 | 1,606,485 |
| Other assets | 184,854 | 21,667 |
| Total assets | <u>\$ 125,440,012</u> | <u>\$ 29,158,886</u> |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 6,568,044 | \$ 3,220,082 |
| Accrued expenses and other current liabilities | 5,868,740 | 1,228,402 |
| Current operating lease liabilities | 2,746,961 | 113,769 |
| Notes payable, current portion | 2,112,710 | — |
| Total current liabilities | <u>17,296,455</u> | <u>4,562,253</u> |
| Long-term liabilities: | | |
| Warrant liability, at fair value | 23,634,000 | 3,372,000 |
| Notes payable, net of current portion | 34,054,482 | — |
| Long-term operating lease liabilities | 8,245,493 | 1,521,431 |
| Deferred tax liability | 1,504,526 | — |
| Total liabilities | <u>84,734,956</u> | <u>9,455,684</u> |
| Stockholders' equity: | | |
| Common stock, \$0.01 par value per share; 110,000,000 shares authorized; 34,046,500 and 15,496,932 issued and outstanding as of June 30, 2023 and December 31, 2022, respectively | 340,465 | 154,969 |
| Additional paid-in capital | 83,184,034 | 27,465,024 |
| Accumulated deficit | (42,819,443) | (7,916,791) |
| Total stockholders' equity | <u>40,705,056</u> | <u>19,703,202</u> |
| Total liabilities and stockholders' equity | <u>\$ 125,440,012</u> | <u>\$ 29,158,886</u> |

See accompanying notes to unaudited condensed consolidated financial statements.

MOLEKULE GROUP, INC. AND SUBSIDIARIES (f/k/a AEROCLEAN TECHNOLOGIES, INC.)
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|--------------------------------|-----------------------|------------------------------|-----------------------|
| | 2023 | 2022 | 2023 | 2022 |
| Product revenues | \$ 13,242,959 | \$ 70,918 | \$ 21,592,380 | \$ 77,652 |
| Cost of sales | 8,763,888 | 36,126 | 13,438,147 | 39,890 |
| Gross profit | 4,479,071 | 34,792 | 8,154,233 | 37,761 |
| Operating expenses: | | | | |
| Selling, general and administrative | 15,005,356 | 4,105,066 | 28,666,969 | 6,247,290 |
| Research and development | 1,174,846 | 579,061 | 1,422,625 | 1,110,544 |
| Total operating expenses | 16,180,202 | 4,684,127 | 30,089,594 | 7,357,834 |
| Loss from operations | (11,701,131) | (4,649,335) | (21,935,361) | (7,320,073) |
| Change in fair value of warrant liability | (12,050,500) | (650,000) | (10,324,500) | (650,000) |
| Interest expense | (1,443,009) | — | (2,691,686) | — |
| Other expense | 132,242 | — | (44,257) | — |
| Total other expense | (1,310,767) | — | (2,735,943) | — |
| Loss before income tax benefit | (25,062,398) | (5,299,335) | (34,995,804) | (7,970,073) |
| Income tax benefit | 93,156 | (127,058) | 93,156 | (219,832) |
| Net loss | <u>\$ (24,969,242)</u> | <u>\$ (5,172,277)</u> | <u>\$ (34,902,648)</u> | <u>\$ (7,750,241)</u> |
| Net loss per share: | | | | |
| Basic and diluted | <u>\$ (0.76)</u> | <u>\$ (0.37)</u> | <u>\$ (1.12)</u> | <u>\$ (0.56)</u> |
| Weighted-average common shares outstanding: | | | | |
| Basic and diluted | <u>33,017,565</u> | <u>13,894,119</u> | <u>31,185,329</u> | <u>13,885,923</u> |

See accompanying notes to the unaudited condensed consolidated financial statements.

**MOLEKULE GROUP, INC. AND SUBSIDIARIES (f/k/a AEROCLEAN TECHNOLOGIES, INC.) CONDENSED
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(Unaudited)**

THREE AND SIX MONTHS ENDED JUNE 30, 2023:

| | Common Stock | | Additional Paid-In Capital | Accumulated Deficit | Total Stockholders' Equity |
|---------------------------------------|-------------------|-------------------|-------------------------------|------------------------|-------------------------------|
| | Shares | Amount | | | |
| Balance, March 31, 2023 | 30,427,750 | \$ 304,277 | \$ 81,284,515 | \$ (17,850,199) | \$ 63,738,593 |
| Issuance of common stock and warrants | 3,400,000 | 34,000 | — | — | \$ 34,000 |
| Stock-based compensation | — | — | 1,901,707 | — | 1,901,707 |
| Issuance of restricted stock units | 218,750 | 2,188 | (2,188) | — | — |
| Net loss | — | — | — | (24,969,244) | (24,969,244) |
| Balance, June 30, 2023 | <u>34,046,500</u> | <u>\$ 340,465</u> | <u>\$ 83,184,034</u> | <u>\$ (42,819,443)</u> | <u>\$ 40,705,056</u> |

| | Common Stock | | Additional Paid-In Capital | Accumulated Deficit | Total Stockholders' Equity |
|---|-------------------|-------------------|-------------------------------|------------------------|-------------------------------|
| | Shares | Amount | | | |
| Balance, December 31, 2022 | 15,496,932 | \$ 154,969 | \$ 27,465,024 | \$ (7,916,792) | \$ 19,703,201 |
| Acquisition of Molekule, Inc. | 14,930,818 | 149,308 | 52,316,767 | — | 52,466,075 |
| Issuance of restricted stock units | 3,400,000 | 34,000 | — | — | 34,000 |
| Stock-based compensation | — | — | 3,404,431 | — | 3,404,431 |
| Transactions related to employee share-based compensation plan | 218,750 | 2,188 | (2,188) | — | — |
| Net loss | — | — | — | (34,902,650) | (34,902,650) |
| Balance, June 30, 2023 | <u>34,046,500</u> | <u>\$ 340,465</u> | <u>\$ 83,184,034</u> | <u>\$ (42,819,443)</u> | <u>\$ 40,705,056</u> |

THREE AND SIX MONTHS ENDED JUNE 30, 2022:

| | Common Stock | | Additional Paid-In Capital | Accumulated Deficit | Total Stockholders' Equity |
|--------------------------|-------------------|-------------------|-------------------------------|------------------------|-------------------------------|
| | Shares | Amount | | | |
| Balance, March 31, 2022 | 13,877,636 | \$ 138,776 | \$ 23,990,337 | \$ (4,325,824) | \$ 19,803,289 |
| Issuance of equity units | 1,531,192 | 15,000 | 894,770 | — | 909,770 |
| Stock-based compensation | — | — | 708,540 | — | 708,540 |
| Net loss | — | — | — | (5,172,277) | (5,172,277) |
| Balance, June 30, 2022 | <u>15,408,828</u> | <u>\$ 153,776</u> | <u>\$ 25,593,647</u> | <u>\$ (9,498,101)</u> | <u>\$ 16,249,322</u> |

| | Common Stock | | Additional Paid-In Capital | Accumulated Deficit | Total Stockholders' Equity |
|----------------------------|-------------------|-------------------|-------------------------------|------------------------|-------------------------------|
| | Shares | Amount | | | |
| Balance, December 31, 2021 | 13,877,636 | \$ 138,776 | \$ 23,319,499 | \$ (1,747,860) | \$ 21,710,415 |
| Issuance of common stock | 1,531,192 | 15,000 | 894,770 | — | 909,770 |
| Stock - based compensation | — | — | 1,379,378 | — | 1,379,378 |
| Net loss | — | — | — | (7,750,241) | (7,750,241) |
| Balance, June 30, 2022 | <u>15,408,828</u> | <u>\$ 153,776</u> | <u>\$ 25,593,647</u> | <u>\$ (9,498,101)</u> | <u>\$ 16,249,322</u> |

See accompanying notes to the unaudited condensed consolidated financial statements.

MOLEKULE GROUP, INC. AND SUBSIDIARIES (f/k/a AEROCLEAN TECHNOLOGIES, INC.)
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

| | Six Months Ended June 30, | |
|---|------------------------------|----------------------|
| | 2023 | 2022 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net loss | \$ (34,902,648) | \$ (7,750,241) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Other non cash expense | — | — |
| Offering costs associated with warrant liability | — | 1,326,212 |
| Change in fair value of warrant liability | 10,324,500 | 650,000 |
| Deferred tax benefit | (93,156) | (219,832) |
| Depreciation and amortization | 1,082,488 | 72,047 |
| Equity-based compensation | 3,404,431 | 1,379,378 |
| Provision for doubtful accounts | 2,107 | — |
| Amortization of debt discounts | 188,088 | — |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (1,798,424) | 149,009 |
| Inventories | 3,669,072 | (358,755) |
| Other current and non-current assets | 664,757 | 596,390 |
| Accounts payable | (8,746,224) | (239,431) |
| Accrued expenses and other liabilities | (1,136,152) | 82,517 |
| Operating lease liabilities | 11,390 | — |
| Net cash used in operating activities | <u>(27,329,771)</u> | <u>(4,312,706)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchases of property and equipment | (1,196,104) | (154,065) |
| Cash acquired in acquisition of Molekule Inc. | 2,988,096 | — |
| Net cash provided by investing activities | <u>1,791,992</u> | <u>(154,065)</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Proceeds from issuance of common stock and warrants | 9,971,500 | 15,000,000 |
| Repayment of notes payable | (597,260) | — |
| Payment of issuance costs | — | (999,449) |
| Net cash provided by financing activities | <u>9,374,240</u> | <u>14,000,551</u> |
| Net decrease in cash | (16,163,539) | 9,533,780 |
| Cash and restricted cash, beginning of period | 22,062,657 | 19,629,649 |
| Cash and restricted cash, end of period | \$ 5,899,118 | \$ 29,163,429 |
| Supplemental schedule of non-cash activities: | | |
| Offering costs in private placement | \$ — | \$ 422,000 |
| Cash paid for interest | \$ 2,267,306 | \$ — |
| Supplemental schedule of investing activities: | | |
| Net asset acquired from Molekule Inc. | \$ 52,466,073 | \$ — |

See accompanying notes to unaudited condensed consolidated financial statements.

MOLEKULE GROUP, INC. (f/k/a AEROCLEAN TECHNOLOGIES, INC.)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Description of Business

Description of Business

Molekule Group, Inc. (f/k/a AeroClean Technologies, Inc.) (the “Company”) was initially formed as CleanCo Bioscience Group LLC (“CBG”) in the State of Florida on September 2, 2011. Subsequent to its formation, CBG established a team of scientists, engineers and medical experts to provide solutions for the challenges posed by harmful airborne pathogens and resultant hospital acquired infections. On September 15, 2020, CBG converted into AeroClean Technologies, LLC as a Delaware limited liability company. On November 23, 2021, AeroClean Technologies, LLC incorporated in the state of Delaware as AeroClean Technologies, Inc. The Company is an interior space air purification technology company focused on the sale and distribution of its high-performance interior air sterilization and disinfection products for the eradication of coronavirus and other harmful airborne pathogens. The Company was established to develop technology-driven, medical-grade air purification solutions for hospitals and other healthcare settings. The company is headquartered in Palm Beach Gardens, Florida.

On January 12, 2023, in connection with the acquisition of Molekule, Inc. (“Legacy Molekule”), the Company changed its name from AeroClean Technologies, Inc. to Molekule Group, Inc. (see Note 3). With the acquisition of Legacy Molekule, the Company is engaged in the manufacturing and selling of air purifiers and filters primarily in the United States, but also in Canada directly to consumers, through retail and distribution, and to commercial and enterprise customers. During 2020, Legacy Molekule began selling directly to distributors in Japan and South Korea. During 2021, Legacy Molekule also began selling directly to consumers in Europe. In 2022, sales continued to be primarily within the United States. Legacy Molekule incorporated in the state of Delaware in February 2015 as Transformair, Inc. and changed its name to Molekule, Inc. through an amendment to its articles of incorporation in June 2016. The accompanying condensed consolidated financial statements include the results of Legacy Molekule and its wholly owned subsidiary in the current period from the date of acquisition (January 12, 2023) and as of the most recent balance sheet date (June 30, 2023) and the results of GSI Germsweepusa Inc. (doing business as GSI Technology) (“GSI Technology”), which was acquired in 2022.

Liquidity and Going Concern

The provisions of Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) Topic 205-40, *Presentation of Financial Statements — Going Concern* (ASC 205-40) require management to assess an entity’s ability to continue as a going concern within one year of the date the financial statements are issued. In each reporting period (including interim periods), an entity is required to assess conditions known and reasonably knowable as of the financial statement issuance date to determine whether it is probable an entity will not meet its financial obligations within one year from the financial statement issuance date. Substantial doubt about an entity’s ability to continue as a going concern exists when conditions and events, considered in the aggregate, indicate it is probable the entity will be unable to meet its financial obligations as they become due within one year after the date the financial statements are issued.

The Company incurred a net loss of \$34,902,648 during the six months ended June 30, 2023 and its net cash used in operating activities was \$27,329,771 for the six months ended June 30, 2023. In addition, the Company’s accumulated deficit was \$42,819,441 at June 30, 2023. The Company’s recurring losses from operations, recurring cash used in operating activities, accumulated deficit, expected working capital needs to fund its combined operations and new debt obligations as a result of the acquisition of Molekule, Inc. in January 2023 (see Note 3), raise substantial doubt about its ability to continue as a going concern. The Company’s ability to fund its operations is dependent upon management’s plans, which include raising capital, managing costs and generating sufficient revenues to offset costs. There can be no assurances that the Company will be able to secure any such additional financing on acceptable terms and conditions, or at all. Accordingly, management has concluded there is substantial doubt as to the Company’s ability to continue as a going concern within one year after the date the financial statements were issued. Under its debt agreements (the Senior Term Loan and the Mezzanine Term Loan) with its lender, Silicon Valley Bank, now a division of First Citizens Bank (“SVB”), the Company is required to generate revenue of at least \$50 million for the twelve months ended March 31, 2024. Non-compliance with this requirement may result in the debt maturity dates becoming accelerated.

2. Summary of Significant Accounting Policies

Basis of Presentation

These unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) for interim financial information and pursuant to the rules and regulations of the U. S. Securities and Exchange Commission (the “SEC”) and include the Company’s wholly owned subsidiaries, GSI Technology, for the current period and Legacy Molekule since January 12, 2023. All significant intercompany accounts and transactions have been eliminated in consolidation.

Accordingly, the unaudited condensed consolidated financial statements do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. The condensed consolidated balance sheet as of June 30, 2023 has been derived from the Company’s unaudited condensed consolidated financial statements at such date. All adjustments that, in the opinion of the Company’s management, are considered necessary for a fair presentation of the results of operations for the periods shown have been reflected in these unaudited condensed consolidated financial statements. The results of operations for the periods presented are not necessarily indicative of the results expected for the full 2023 fiscal year or for any future period. The information included in these unaudited condensed consolidated financial statements should be read in conjunction with the Company’s audited consolidated financial statements and accompanying notes for the year ended December 31, 2022, contained in the Company’s Annual Report on Form 10-K, as amended, for the fiscal year ended December 31, 2022.

Use of Estimates

The preparation of the Company’s condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and expenses and related disclosure of contingent assets and liabilities. Significant estimates in these unaudited condensed consolidated financial statements include those related to the fair value of equity-based compensation, revenue recognition, the incremental borrowing rate for leases, the fair value of warrant liability, valuation in connection with business combination and the deferred tax valuation allowance. On an ongoing basis, the Company evaluates its estimates, judgments and methodologies. The Company bases its estimates on historical experience and on various other assumptions believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Due to the inherent uncertainty involved in making estimates, actual results could differ materially from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include cash and highly liquid investments with maturities at the date of investment of not more than three months. The Company held no cash equivalents as of June 30, 2023 and 2022.

Restricted Cash

The Company had a restricted cash balance of \$629,742 as of June 30, 2023 and nil as of December 31, 2022. The restricted cash balance constitutes collateral pursuant to the terms of an office lease. The restricted cash balance is held in a separate bank account.

Revenue Recognition

The Company recognizes revenues related to sales of products upon the customer obtaining control of promised goods, in an amount that reflects the consideration that is expected to be received in exchange for those goods. To determine revenue recognition for arrangements within the scope of ASC Topic 606, *Revenue from Contracts with Customers*, the following five steps are performed: (i) identify the contract(s) with a customer; (ii) identify the performance obligations in the contract; (iii) determine the transaction price; (iv) allocate the transaction price to the performance obligations in the contract; and (v) recognize revenue when (or as) the Company satisfies a performance obligation. The Company generates substantially all its revenue from sales contracts with customers. While the Company enters into separate sales contracts with each customer, all sales contracts are similarly structured. These contracts create an obligation to transfer product to the customer. Sales of purifier devices and filters are separate performance obligations. The Company

allocates the transaction price to filters based upon their standalone sales price. The transaction price allocated to the device is estimated based on the residual method, as the devices do not have an established standalone sales price and are never sold without filters.

All performance obligations are satisfied within one year; therefore, costs to obtain contracts are expensed as incurred. There is no financing component because the Company expects, at contract inception, the period between when the Company transfers product to the customer and when the customer pays for the product will be less than one year. Sales terms allow for the right of return, and the Company has recorded a related reserve based on historical, as well as post year-end, activity. Customers may, for any reason, return the product within 30 days for a full refund, excluding shipping charges. The Company establishes a liability for expected returns representing the amount of consideration the entity does not expect to be entitled to because it will be refunded to customers. The refund liability is remeasured at each reporting date to reflect changes in the estimate, with a corresponding adjustment to revenues. The Company satisfies the performance obligations and records revenues when transfer of control has passed to the customer based on the terms of sale. A customer is considered to have control once they are able to direct the use and receive substantially all of the benefits of the product.

Sales taxes collected from customers are not recorded within revenues and are remitted to the taxing authorities periodically. Shipping and handling are recorded in revenues and cost of revenues on the Statements of Operations and are charged to customers at varying rates.

The Company recognized revenue of \$13,242,959 and \$70,918 in the three months ended June 30, 2023 and 2022, respectively, and \$21,592,380 and \$77,652 for the six months ended June 30, 2023 and 2022, respectively.

Warranty Cost

The Company provides a three-year warranty on its Pürgo device and a two year warranty for the Legacy Molekule devices, in each case, from the date of sale to its customers. The Company's policy is to record a provision for estimated future costs related to warranty expense when they are probable and reasonably estimable, which is when revenue is recognized. There was a warranty accrual of \$385,748 as of June 30, 2023 and nil as of December 31, 2022.

Income Taxes

Income taxes are accounted for under ACS 740 utilizing the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences and operating loss and tax credit carry forwards are expected to be recovered, settled or utilized. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all the deferred tax assets will not be realized. If such an event occurs, a valuation allowance is recorded. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

The Company recognizes the effect of income tax positions only if those positions are more likely than not of being sustained upon examination. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. The Company records interest and penalties related to unrecognized tax benefits as income tax expense. At June 30, 2023 and December 31, 2022, the company did not record any uncertain tax positions.

Research & Development Expenses

Research and development expenses are expensed as incurred and consist principally of contract labor and third-party engineering, product development and testing costs related to the development of medical grade air purification devices and related components as well as concepts for future product development.

Stock-Based Compensation

The Company accounts for share-based payments to employees and non-employees in accordance with the provisions of FASB

ASC 718, Compensation — Stock Compensation (“ASC 718”). Under ASC 718, the Company measures the share-based compensation cost on the date of grant, based on the fair value of the award, and expense is recognized over the requisite service period.

Accounts Receivable

Trade accounts receivable are stated net of an allowance for doubtful accounts. The Company performs ongoing credit evaluations of its customers and adjusts credit limits based upon payment history and the customer’s current creditworthiness, as determined by review of their current credit information. The Company estimates the allowance for doubtful accounts based on review and analysis of specific customer balances that may not be collectible and how recently payments have been received. The Company also evaluates the need for a provision for estimated credit losses based upon historical experience and any specific customer collection issues that have been identified. Accounts are considered for write-off when they become past due and when it is determined that the probability of collection is remote. For more information on the adoption of Topic 326 *Current Expected Credit Losses*, see Recent Accounting Pronouncements.

Inventories

The Company values inventories at the lower of cost or net realizable value using the first-in, first-out or weighted average cost method. Net realizable value is the estimated selling price in the ordinary course of business, less reasonable predictable costs of completion, disposal and transportation. The costs related to inbound freight, tariffs and fees related to the purchases of inventories, are capitalized as part of the ending inventory, with the net change recorded as a component of cost of revenue.

Fair Value of Financial Instruments

Certain assets and liabilities are carried at fair value in accordance with U.S. GAAP. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants at the measurement date. A three-tier fair value hierarchy that prioritizes the inputs used in the valuation methodologies, is as follows:

- Level 1 Valuations based on quoted prices for identical assets and liabilities in active markets.
- Level 2 Valuations based on observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, or other inputs that are observable or that can be corroborated by observable market data.
- Level 3 Valuations based on unobservable inputs reflecting the Company’s own assumptions, consistent with reasonably available assumptions made by other market participants. These valuations require significant judgment.

At June 30, 2023 and December 31, 2022, the carrying amounts of the Company’s financial instruments, including cash and restricted cash, prepaid expenses and other current assets, accounts payable and accrued liabilities, approximated their respective fair value due to the short-term nature of these instruments.

Financial Instruments – Derivatives

The Company evaluates its financial instruments to determine if the financial instrument itself or any embedded component of a financial instrument potentially qualifies as a derivative required to be separately accounted for in accordance with FASB ASC 815, Derivatives and Hedging. The accounting for warrants issued to purchase shares of common stock of the Company is based on the specific terms of the respective warrant agreement. A warrant classified as a derivative liability is initially measured at its issue-date fair value, with such fair value subsequently adjusted at each reporting period, with the resulting fair value adjustment recognized as other income or expense. Upon the occurrence of an event resulting in the warrant liability being subsequently classified as equity, or the exercise of the warrant or the conversion option, the fair value of the derivative liability will be adjusted on such date-of-occurrence, with such date-of-occurrence fair value adjustment recognized as other income or expense, and then the derivative liability will be derecognized at such date-of-occurrence fair value.

Debt Issuance Costs

Costs incurred in connection with the issuance of any new term debt are treated as debt discount and recorded as a reduction of the debt balance. The Company amortized debt discount costs over the term of the related debt using the effective interest method.

Goodwill and Intangible Assets

The Company has recorded intangible assets, and goodwill, in connection with business combinations. Estimated useful lives of amortizable intangible assets are determined by management based on an assessment of the period over which the asset is expected to contribute to future cash flows.

In accordance with U.S. GAAP for goodwill and other indefinite-lived intangibles, the Company tests these assets for impairment annually and whenever events or circumstances make it more likely than not that impairment may have occurred. For the purposes of that assessment, the Company has determined to assign assets acquired in business combinations to a single reporting unit including all goodwill and indefinite-lived intangible assets acquired in business combinations.

Business Acquisition Accounting

The Company applies the acquisition method of accounting for acquisitions that meet the criteria of a business combination. The Company allocates the purchase price of its business acquisitions based on the fair value of identifiable tangible and intangible assets. The difference between the total purchase consideration and the sum of the fair values of acquired tangible and identifiable intangible assets less the fair value of the liabilities assumed is recorded as goodwill. Transaction costs are expensed as incurred in general and administrative expenses.

Recent Accounting Pronouncements

The Company has reviewed recent accounting pronouncements and, with the exception of the below, concluded they are either not applicable to the business or no material effect is expected on the financial statements as a result of future adoption.

In June 2016, the FASB issued Accounting Standards Update (“ASU”) No. 2016-13, Financial Instruments - Credit Losses, which was subsequently amended by ASU No. 2018-19 and ASU No. 2019-10, and which requires the measurement of expected credit losses for financial instruments carried at amortized cost held at the reporting date based on historical experience, current conditions and reasonable forecasts. The updated guidance also amends the current other-than-temporary impairment model for available-for-sale debt securities by requiring the recognition of impairments relating to credit losses through an allowance account and limits the amount of credit loss to the difference between a security’s amortized cost basis and its fair value. In addition, the length of time a security has been in an unrealized loss position will no longer impact the determination of whether a credit loss exists. The main objective of this ASU is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. ASU 2016-13 must be adopted using a modified retrospective transition method through a cumulative-effect adjustment to members’ equity in the period of adoption. The Company adopted ASU 2016-13 and related amendments as of January 1, 2023, and the adoption of the new standard did *not* have a material impact on the Company’s consolidated financial statements.

3. Business Combination

On January 12, 2023, the Company completed the acquisition of Legacy Molekule pursuant to the Agreement and Plan of Merger dated as of October 3, 2022 by and among the Company, Air King Merger Sub Inc., a Delaware corporation and direct wholly owned subsidiary of the Company (“Merger Sub”), and Legacy Molekule (the “Molekule Merger”). Pursuant to the Merger Agreement, Merger Sub merged with and into Legacy Molekule, with Legacy Molekule continuing as the surviving entity and a wholly owned subsidiary of the Company. In connection with the closing of the Molekule Merger, the Company changed its name from AeroClean Technologies, Inc. to Molekule Group, Inc.

At the effective date of the Molekule Merger, the outstanding shares of Legacy Molekule common stock, par value \$0.0001, that were issued and outstanding immediately prior to the effective time of the Molekule Merger (the “Legacy Molekule Common Stock”) (including shares of Legacy Molekule Common Stock resulting from the conversion of Legacy Molekule’s eligible preferred stock, but excluding dissenting shares and shares held in treasury), were converted automatically into, and the holders of such shares of Legacy Molekule Common Stock were entitled to receive, by virtue of the Molekule Merger and upon the terms and subject to the conditions set forth in the merger agreement, 14,907,210 fully paid and nonassessable shares of the Company’s common stock, which resulted in the Legacy Molekule stockholders in the aggregate, after taking into account the 23,608 shares of Company Common Stock underlying In-the-Money Company Warrants (as defined in the merger agreement) and the grants of 500,380 RSUs by the Company to certain continuing Legacy Molekule employees that were deemed vested and outstanding as of immediately following the effective time of the Molekule Merger, holding 49.5% of the Outstanding Shares (as defined in the merger agreement). Immediately following the closing of the Molekule Merger, there were 30,427,750 shares of Company Common Stock outstanding, which does not include Company Common Stock that may be issued upon the vesting of RSUs.

Based on the Company’s preliminary purchase price allocation, the excess of the purchase price over the fair value of the identifiable assets acquired approximated \$66 million, of which \$46 million was allocated to identifiable intangible assets consisting of customer relationships (approximately \$3 million), Molekule’s trade name (approximately \$27 million), and developed technology (approximately \$16 million) and \$20 million was allocated to goodwill.

The Molekule Merger was accounted for under FASB ASC 805, Business Combinations (“ASC 805”). The results of operations for Legacy Molekule are included in the accompanying condensed consolidated statements of operations from the date of acquisition. The valuation of certain assets, principally intangible assets including goodwill and identified intangible assets related to the acquisition, inventory and property, plant and equipment, is not yet complete, and as such, the Company has not yet finalized its allocation of the purchase price for the acquisition.

[Table of Contents](#)

The following table summarizes the provisional amounts allocated to the estimated fair values of assets acquired and fair values of liabilities assumed in the Legacy Molekule acquisition in accordance with ASC 805:

| | <u>Legacy Molekule</u> |
|---|------------------------|
| Cash and cash equivalents | \$ 2,988,100 |
| Accounts receivable | 378,195 |
| Inventories | 31,081,238 |
| Prepaid and other current assets | 1,138,784 |
| Property, Plant and Equipment | 6,402,425 |
| Goodwill | 20,404,413 |
| Intangible assets, net | 45,890,000 |
| Right of Use Assets | 10,479,883 |
| Other long-term assets | 220,779 |
| Accounts payable | (12,094,186) |
| Accrued expenses | (3,001,862) |
| Accrued sales tax | (516,530) |
| Notes payable | (36,576,443) |
| Operating lease liabilities | (10,480,088) |
| Deferred tax liabilities | (1,597,682) |
| Other current and non-current liabilities | (2,250,953) |
| Total consideration | <u>\$ 52,466,073</u> |

On a pro forma basis to give effect to the Molekule merger as if it occurred on January 1, 2022, revenues, net loss and loss per basic share for the six months ended June 30, 2023 and 2022 would have been as follows:

| | <u>June 30, 2023</u> | <u>June 30, 2022</u> |
|------------------------|----------------------|----------------------|
| | <u>Pro forma</u> | <u>Pro forma</u> |
| Revenues | \$ 22,762,753 | 25,226,575 |
| Net loss | (36,498,858) | (11,566,624) |
| Loss per diluted share | (1.17) | (0.83) |

4. Financial Instruments Fair Value Measurements

2022 Private Placement Warrants

The 2022 Warrant issued in connection with the 2022 Private Placement (as such terms are defined in Note 13) was accounted for as a liability and accordingly the warrant liability is re-measured at each balance sheet date until its exercise or expiration, and any change in fair value is recognized in the Company's condensed consolidated statement of operations.

2023 Private Placement Warrants

On May 3, 2023, the Company entered into the Securities Purchase Agreement ("SPA") with a selling stockholder (the "Selling Stockholder"), pursuant to which the Company agreed to sell (i) 3,400,000 shares of common stock, (ii) 3,125,000 shares of common stock that are issuable upon the exercise of the Series A Warrant, (iii) 6,250,000 shares of common stock that are issuable upon the exercise of the Series B Warrant and (iv) 2,850,000 shares of common stock that are issuable upon the exercise of the Pre-Funded Warrant collectively the "2023 Warrants", for an aggregate purchase price of approximately \$9,971,500 (the "2023 Private Placement") as such terms defined in Note 13. The SPA contains customary representations, warranties and agreements by the Company. The

[Table of Contents](#)

Company also agreed to reduce the exercise price of the 2022 Warrant owned by the Selling Stockholder from \$11.00 to \$2.00 per share of common stock.

The Company utilizes a Black-Scholes option pricing model to estimate the fair value of the 2022 Warrant, which is considered a Level 3 fair value measurement. The Black-Scholes option-pricing model considers several variables and assumptions in estimating the fair value of financial instruments, including the per-share fair value of the underlying common stock, exercise price, expected term, risk-free interest rate, expected stock price volatility over the expected term, and expected annual dividend yield. Certain inputs utilized in the Company's Black-Scholes pricing model may fluctuate in future periods based upon factors that are outside of the Company's control. A significant change in one or more of these inputs used in the calculation of the fair value may cause a significant change to the fair value of the warrant liability, which could also result in material non-cash gain or loss being reported in the accompanying unaudited condensed consolidated statements of operations.

The following table provides the significant inputs to the Black-Scholes pricing model for the fair value of the 2022 Warrant:

| | At May 3, 2023 | At May 5, 2023 | At June 30, 2023 |
|----------------------------|----------------|----------------|------------------|
| Stock price | \$ 1.57 | \$ 1.57 | \$ 2.34 |
| Expiration term (in years) | 4.39 | 4.39 | 4.24 |
| Volatility | 98.0 % | 98.0 % | 96.0 % |
| Risk-free rate | 3.50 % | 3.50 % | 4.3 % |
| Dividend yield | 0.0 % | 0.0 % | 0.0 % |
| Fair Value per Warrant | \$ 0.61 | \$ 1.07 | \$ 1.71 |

The following table provides the significant inputs to the Black-Scholes pricing model for the fair value of the Series A Warrant:

| | At May 5, 2023 | At June 30, 2023 |
|----------------------------|----------------|------------------|
| Stock price | \$ 1.57 | \$ 2.34 |
| Expiration term (in years) | 0.67 | 0.51 |
| Volatility | 85.0 % | 99.0 % |
| Risk-free rate | 5.00 % | 5.5 % |
| Dividend yield | 0.0 % | 0.0 |
| Fair Value per Warrant | \$ 0.43 | \$ 1.01 |

The following table provides the significant inputs to the Black-Scholes pricing model for the fair value of the Series B Warrant:

| | At May 5, 2023 | At June 30, 2023 |
|----------------------------|----------------|------------------|
| Stock price | \$ 1.57 | \$ 2.34 |
| Expiration term (in years) | 5.00 | 4.85 |
| Volatility | 98.0 % | 96.0 % |
| Risk-free rate | 3.40 % | 4.2 % |
| Dividend yield | 0.0 % | 0.0 % |
| Fair Value per Warrant | \$ 1.14 | \$ 1.80 |

The following table provides the significant inputs to the Black-Scholes pricing model for the fair value of the Pre-Funded Warrant:

| | At May 5, 2023 | At June 30, 2023 |
|----------------------------|----------------|------------------|
| Stock price | \$ 1.57 | \$ 2.34 |
| Expiration term (in years) | 5.00 | 4.85 |
| Volatility | 98.0 % | 96.0 % |
| Risk-free rate | 3.40 % | 4.2 % |
| Dividend yield | 0.0 % | 0.0 % |
| Fair Value per Warrant | \$ 1.56 | \$ 2.33 |

The private placement offering costs of \$673,290 were allocated to the Warrants entirely and were immediately expensed and recorded as selling, general and administrative expense in the statement of operations for the quarter ended June 30, 2023.

The 2023 Warrants issued in connection with the 2023 Private Placement are being accounted for as a liability and accordingly the warrant liability is re-measured at each balance sheet date until its exercise or expiration, and any change in fair value is recognized in the Company's condensed consolidated statement of operations.

A reconciliation of the 2022 Warrant liability and the 2023 Warrants liability for the three months ended June 30, 2023, as follows:

| | <u>2022 Warrant</u> | <u>2023 Warrants</u> |
|--|---------------------|----------------------|
| Balance at March 31, 2023 | \$ 1,646,000 | \$ — |
| Change in fair value on date of modification | 691,000 | — |
| Initial fair value on date of issuance | — | 12,956,000 |
| Change in fair value | 223,000 | 8,118,000 |
| Balance at June 30, 2023 | <u>\$ 2,560,000</u> | <u>\$ 21,074,000</u> |

A reconciliation of the 2022 Warrant liability and the 2023 Warrants liability for the six months ended June 30, 2023 as follows:

| | <u>2022 Warrant</u> | <u>2023 Warrants</u> |
|--|---------------------|----------------------|
| Balance at December 31, 2022 | \$ 3,372,000 | \$ — |
| Change in fair value on date of modification | 691,000 | — |
| Initial fair value on date of issuance | — | 12,956,000 |
| Change in fair value | (1,503,000) | 8,118,000 |
| Balance at of June 30, 2023 | <u>\$ 2,560,000</u> | <u>\$ 21,074,000</u> |

The fair value of the 2023 Warrants and the 2022 Warrant aggregated was \$23,634,000 at June 30, 2023 and the fair value of the 2022 Warrant was \$3,372,000 at December 31, 2022, respectively. The Company recognized a loss in connection with the change in the fair value of warrant liabilities of \$12,050,500 and \$10,324,500 in the statements of operations for the three months and six months ended June 30, 2023, respectively.

The fair value of the 2023 Warrants at the date of issuance was greater than the gross proceeds, resulting in \$3,018,500 being recognized as an expense and par value of \$34,000 being recognized for the 3,400,000 of shares of common stock issued.

5. Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets of \$1,801,533 and \$665,395 at June 30, 2023 and December 31, 2022, respectively, consisted primarily of prepaid insurance premiums and amounts paid to suppliers and vendors for inventories and retainers for engineering, product development, testing and other services to be performed.

6. Inventories

Inventories consisted of the following:

| | June 30, 2023 | December 31, 2022 |
|-------------------|----------------------|----------------------|
| Raw materials | \$ 4,002,445 | \$ 712,752 |
| Finished goods | 15,096,071 | 1,307,961 |
| Work in process | 10,334,364 | — |
| Total inventories | <u>\$ 29,432,880</u> | <u>\$ 2,020,713</u> |

7. Property and Equipment

Property and equipment consisted of the following:

| | Useful Life (Years) | June 30, 2023 | December 31, 2022 |
|--------------------------------|-------------------------------------|---------------------|----------------------|
| Leasehold improvements | Lesser of useful life or lease term | \$ 2,748,934 | \$ 847,217 |
| Machinery and tooling | 5 - 7 | 3,780,221 | 1,270,652 |
| Furniture and equipment | 3 - 10 | 928,208 | 241,835 |
| Software | 2-3 | 1,390,514 | — |
| Construction in progress | | 651,857 | — |
| | | <u>9,499,734</u> | <u>2,359,704</u> |
| Less: accumulated depreciation | | <u>873,703</u> | <u>240,570</u> |
| | | <u>\$ 8,626,031</u> | <u>\$ 2,119,134</u> |

Property and equipment are stated at cost and depreciated generally under the straight-line method over their estimated useful lives (or the lesser of the term of the lease for leasehold improvements, as appropriate), except for tooling. Tooling is depreciated utilizing either the units-of-production method or a straight-line method over a life of 5-7 years depending on the type of tooling. As a result of the fair value adjustments made during the three months ended June 30, 2023 the Company made an adjustment to decrease depreciation expense for the six months ended June 30, 2023 resulting in a total of (\$274,603) being recognized in the three months ended June 30, 2023 Depreciation expenses was \$36,219 for the three months ended June 30, 2023 and 2022, respectively, and \$633,133 and \$72,047 for the six months ended June 30, 2003 and 2022, respectively.

8. Goodwill and Intangible Assets

Goodwill

Goodwill was \$21,031,064 as of June 30, 2023 compared to \$626,647 as of December 31, 2022.

Intangible Assets

Identifiable intangible assets were \$45,890,000 and amortization expense associated with identifiable intangible assets was \$131,994 and \$522,238 for the three and six months and ended June 30, 2023, respectively, and nil for 2022. The Company currently expects to recognize amortization expense related to intangible assets of approximately \$1,260,666 in each of the next five fiscal years. The future amortization amounts are estimates.

The following sets forth the intangible assets by major asset class as of June 30, 2023, all of which were acquired through business purchase transactions:

| | Useful Life (Years) | Original Cost | Accumulated Amortization | Net Book Value |
|-------------------------------|------------------------|-------------------|-----------------------------|-------------------|
| Trademark | Indefinite | 26,980,000 | — | 26,980,000 |
| Internally-developed software | 15 | 15,660,000 | 487,200 | 15,172,800 |
| Customer Relationships | 15 | 3,250,000 | 101,111 | 3,148,889 |
| | | <u>45,890,000</u> | <u>588,311</u> | <u>45,301,689</u> |

9. Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consisted of the following:

| | June 30, 2023 | December 31, 2022 |
|--|---------------------|----------------------|
| Accrued wages and bonus | \$ 175,892 | \$ 514,169 |
| Research and development | 402,100 | 47,547 |
| Professional and consulting fees | 494,307 | 16,876 |
| Warranty reserve | 385,748 | — |
| Accrued legal fees | 2,153,956 | 439,901 |
| Other accrued liabilities | 2,256,736 | 209,909 |
| Total accrued expenses and other current liabilities | <u>\$ 5,868,740</u> | <u>\$ 1,228,402</u> |

10. Notes Payable

In connection with the Merger Agreement (Note 3) effective January 12, 2023, the Company became jointly and severally liable for the existing Senior Term Loan, Mezzanine Term Loan, and the Facility Term Loan with Legacy Molekule.

Senior Term Loan

In June 2016, Legacy Molekule entered into a Loan and Security Agreement (the “Senior Loan Agreement”), as amended with Silicon Valley Bank, now a division of First Citizens Bank (“SVB”) which provided for borrowings under two term loans (“Senior Term Loan”) aggregating \$7.6 million. On May 31, 2023, the Company amended the Senior Term Loan by entering into the Seventh Loan Modification Agreement of its Senior Loan Agreement, which extended the payment term from thirty-six months to fifty-nine months. The loan amendment included a restructuring fee of \$200,000. As of June 30, 2023, the outstanding principal balance under the Senior Term Loan was \$4.3 million. The Senior Term Loan bears interest at an annual rate equal to the greater of the Prime Rate plus 1% or 4.25%. As of June 30, 2023, the interest rate was 9.25% per year. The maturity date for the Senior Term Loan is March 1, 2028. Interest is payable monthly in arrears. The principal is repayable in 59 equal monthly installments beginning on May 12, 2023. The Senior Loan Agreement contains customary representations and warranties, affirmative and negative covenants (including financial covenants), events of default and termination provisions. Additionally, \$380,000 of debt issuance cost (related to the 2022 modification) is being amortized over the term of the loan.

Mezzanine Term Loan

In March 2021, Legacy Molekule entered into a Mezzanine Loan and Security Agreement (“Mezzanine Loan Agreement”), as amended, with SVB, consisting of a Mezzanine Term Loan A of \$15 million and a Mezzanine Term Loan B of \$15 million. On May 31, 2023, the Company amended the Mezzanine Term Loan by entering into a Fourth Loan Modification Agreement (“Fourth LMA”) to the Mezzanine Loan Agreement, which combined both Mezzanine Term Loan A, the principal payments for which were to begin on April 1, 2024 and Mezzanine Term Loan B, the principal payments for which were to begin on April 1, 2025, into one Mezzanine Term Loan, with principal payments beginning April 1, 2025. The loan amendment included a restructuring fee of \$300,000. As of June 30, 2023, the outstanding principal balance under the Mezzanine Term Loan was \$30 million. The Mezzanine Term Loan bears interest at a floating rate per annum equal to the greater of (x) the Prime Rate plus 6.00% or (y) 9.25%. As of June 30, 2023, the interest rate was 14.25% per year. The Mezzanine Term Loan matures on March 1, 2028. Interest is payable monthly in arrears. The principal of the Mezzanine Term Loan is repayable in 36 equal monthly installments beginning on April 1, 2025. The Mezzanine Loan Agreement contains customary representations and warranties, affirmative and negative covenants (including financial covenants), events of default and termination provisions.

Both the Senior Loan Agreement and Mezzanine Loan Agreement require the Company to maintain a minimum cash balance of \$2.0 million. In connection with the amendment in May 2023, the annual revenue target of \$50.0 million was amended from the calendar year ending December 31, 2023 to the calendar year ending March 31, 2024. Revenue targets for periods occurring after March 31, 2024 shall be mutually agreed by the Company and SVB. The Company is also required to maintain its primary operating and other deposit accounts and securities accounts with SVB and its affiliates.

Facility Term Loan

In June 2020, Legacy Molekule entered into a Facility Term Debt Agreement (the “Facility Term Loan”) with Trinity Capital, Inc. (“Trinity”) in order to obtain financing related to funding the build out of the Company’s filter manufacturing plant. The Company became a co-borrower under this agreement upon the closing of the Molekule Merger. Legacy Molekule drew down \$2.9 million in June 2020, \$0.6 million in September 2020, \$0.9 million in December 2020 and \$0.5 million in August 2021. Principal and interest are paid monthly with the principal being repaid in equal monthly installments from the month after the amount was drawn until April 1, 2026, with the last two months’ payments having been made at the inception of each loan. At the end of the term, Trinity also requires the Company to pay down an additional 10% of the total term draw down amount, which results in an additional payment of \$0.4 million in total for all the draws. This additional payment is being accreted to the total outstanding amount over the term of the Facility Term Loan and resulted in an incremental \$0.3 million of long-term debt to Trinity as of June 30, 2023. As of June 30, 2023, the outstanding principal balance under the Facility Term Loan was \$2.4 million. The Facility Term Loan contains customary representations and warranties, affirmative and negative covenants and events of default.

Notes payable consisted of the following:

| | June 30, 2023 | December 31, 2022 |
|--------------------------------------|------------------|----------------------|
| Senior term loan | \$ 4,860,367 | \$ — |
| Facility term loan | 2,202,167 | — |
| Mezzanine term loan | 30,300,000 | — |
| | 37,362,534 | — |
| Less: Unamortized debt issuance fees | 1,195,342 | — |
| Less: current portion | 2,112,710 | — |
| Total long-term notes payable | \$ 34,054,483 | \$ — |

11. Commitments and Contingencies

Lease Commitments – On February 1, 2021, the Company entered into a lease with Gardens Bio Science Partners, LLC, an entity controlled by the Company’s co-founder and Chairman of the Company’s Board of Directors (the “Board”). The leased premises consist of 20,000 square feet of office and warehouse space. The lease expires in February 2031. The annual base rent of \$260,000 is subject to escalation of 2.5% on an annual basis. Rent expense under this lease was \$118,549 and \$244,602 for the three and six months ended June 30, 2023, respectively. As of June 30, 2023, the future minimum lease payments under this arrangement approximated \$2,295,325.

In February 2019, Legacy Molekule entered into a lease agreement for office space in San Francisco, California. The leased premises consist of 38,000 square feet of office space. The lease expires in August 2026. The lease calls for monthly base rental payments of \$209,231 commencing in the first month and fixed annual base rental increases of 3%. Rent expense is accounted for on a straight-line basis. Rent expense under this lease was \$691,753 and \$1,286,468 for the three and six months ended June 30, 2023, respectively. The lease expires in August 2026. Since June 2023, the lessor has been drawing under an existing letter of credit, which was put in place as security for payment of the monthly base rental payments. Amounts available under such letter of credit will be fully utilized by September, 2023 after which the Company will be required to pay its monthly base rental payments to the lessor. The Company is currently in discussions with the lessor to renegotiate the terms of the lease. There is no assurance that any such renegotiation will be successful.

The Company leases office, warehouse and lab space under noncancelable leases with various expiration dates through 2026. Rent expense under these leases was \$161,529 and \$295,799 for the three and six months ended June 30, 2023, respectively. As of June 30, 2023, the future minimum lease payments under this arrangement approximated \$10,817,986.

Legal Proceedings

From time to time, the Company is subject to legal proceedings in the normal course of operating its business. The outcome of litigation, regardless of the merits, is inherently uncertain. In August 2022, the Company received notice of a complaint filed in the U.S. District Court for the Southern District of New York (the “Court”) by Sterilumen, Inc. (“Sterilumen”), a wholly-owned subsidiary of Applied UV, Inc., in connection with the marketing and sale of the Company’s patented air purification products. In the complaint, the plaintiff alleged trademark infringement, violation of fair competition practices and damages to Sterilumen. On March 13, 2023, the Court dismissed Sterilumen’s claims with prejudice and ruled that the Company’s counterclaims remained extant. The Company subsequently agreed with Sterilumen that Sterilumen will not challenge the Court’s dismissal and will not bring any future claim against the Company alleging infringement from the use of SteriDuct or AeroClean and that the Company will file a notice to dismiss its counterclaims without prejudice. The Company did not establish a contingency reserve related to this matter.

In November 2020, Legacy Molekule was named as the defendant in a class-action complaint in which the plaintiffs alleged that Legacy Molekule misrepresented the capabilities of its products. Legacy Molekule denied all allegations made by the plaintiffs. Without admitting any liability and solely for the purpose of eliminating the uncertainties and expenses of further protracted litigation, Legacy Molekule entered into a class-wide settlement of this matter, where the class was defined to include purchasers who bought Molekule

devices from third-party retailers (e.g. Amazon, Best Buy). The settlement required dismissal of all remaining class-action claims against Legacy Molekule. The Court approved this settlement and entered judgment in the matter on January 25, 2022. The settlement is currently being administered with the cash settlement payment of \$1,300,000 made in March 2022. The Company accrued a loss liability related to the matter of \$1,400,000 as of June 30, 2023 and nil as of December 31, 2022.

The Company enters into agreements with its customers, business partners and other parties in the ordinary course of business that include provisions for the indemnification, holding harmless and defense of indemnified parties of varying scope and terms with respect to certain matters, including, but not limited to, losses arising out of the Company's breach of such agreements and out of third-party IP infringement claims. In these circumstances, payment by the Company may be conditional on the other party making a claim pursuant to the procedures specified in the particular contract. In addition, the Company has indemnification agreements with its directors and executive officers. As of June 30, 2023, the Company had no other accrued liabilities related to other legal matters.

Indemnities, Commitments and Guarantees – Effective November 1, 2020, the Company executed employment agreements with two key members of management that will continue until terminated by either party. In the event of termination without cause, the Company is obligated to pay the executive their base salary for a period of six months. Further, in the event of termination without cause or resignation for good reason, or a change of control, each as defined in the agreements, within twelve months of such termination or resignation, each of the executives is entitled to accelerated vesting of any outstanding time-based equity awards. The employment agreements provide for a base salary and a discretionary annual bonus to be determined at the sole discretion of the Company's Board of Managers, for periods prior to the Company's incorporation in the State of Delaware (the "Corporate Conversion") when it was a limited liability company, and the Company's Board of Directors (in either case, the "Board"), for periods following the Corporate Conversion. The Company's employment agreements generally provide for certain protections in the event of a change of control. These protections generally include the payment of severance under certain circumstances in the event of a change of control. On May 1, 2021, the employment agreements were amended to provide for the eligibility of each executive to receive restricted stock units upon the conversion of the Company to a Delaware corporation. Accordingly, the executives were granted an aggregate of 443,269 restricted stock units contemporaneously with the Public Offering. The Company also had agreements in place with independent contractors whereby the Company was required to compensate the independent contractors fifty percent in cash and fifty percent in equity. The equity consideration was contingent upon future events, including the conversion to a Delaware corporation and a new round of equity financing from third-party sources. On October 3, 2022, the employment agreements were amended in connection with the merger with Legacy Molekule and the executives were granted an aggregate of 732,090 of additional restricted stock units.

Guaranteed Payment – Effective August 10, 2022, Legacy Molekule entered into a Sales Agency Agreement (the "Agency Agreement") with a company to develop a market for its products in the United States for a period of one year with mutual options to renew annually for up to a term of five years. The Agency Agreement provides for payments on a monthly basis to the agent of an amount equal to the greater of the commissions earned and a guaranteed minimum ranging from \$502,500 to \$667,500.

Registration Rights Agreement – In connection with the Company's initial public offering (the "Public Offering") the Company entered into a registration rights agreement with the Chairman of its Board and each of its other stockholders that held 10% or more of its outstanding common stock immediately upon completion of the Public Offering. On January 12, 2023, this registration rights agreement was amended and restated in connection with the Molekule Merger by and among the Company and certain stockholders of AeroClean Technologies, Inc. and Legacy Molekule (the "Registration Rights Agreement"). The Registration Rights Agreement provides the stockholders party thereto with certain "demand" and customary "piggyback" registration rights. The Registration Rights Agreement provides that the Company will pay certain expenses relating to such registrations and indemnify the registration rights holders against certain liabilities that may arise under the Securities Act of 1933, as amended.

12. Related Party Transactions

On February 26, 2023, the Company entered into an Agreement and Plan of Merger with Aura Smart Air Ltd. ("Aura"), an Israeli company listed on the Tel Aviv Stock Exchange (see Note 16 for more information). In connection with the transaction, the Company also entered into a Technology Collaboration Agreement and a Co-Distribution Agreement. Under the Technology Collaboration Agreement the Company paid \$250,000 to Aura for a perpetual license to Aura's Background Intellectual Property and other Intellectual Property owned or controlled by Aura for use in, amongst other items, selling Molekule products and services. Additionally, the Company paid \$68,182 under the Technology Collaboration Agreement, the monthly payment amount due to Aura, for services as part of the Company's collaboration with Aura on the statement of work specified in the agreement. The objectives of the statement of work include onboarding Company devices onto the Aura platform, sending and receiving data to the platform and implementing various internet of things and other Aura technologies into the Company's devices and software.

13. Stockholders' Equity

Long-term Incentive Plan

In conjunction with its IPO, on November 23, 2021, the Company adopted the Employee Stock Purchase Plan, the 2021 Incentive Award Plan (the "Long-Term Incentive Plan" or the "LTIP") and the Non-Employee Directors Stock and Deferred Compensation Plan (collectively, the "Plans") and has reserved 2,802,273 shares, collectively, for issuance or sale under the Plans. The Board approved an amendment to the LTIP to increase the shares authorized to be issued by 1,500,000, and the evergreen set forth in the LTIP resulted in an increase of 277,552 shares.

The Company's Compensation Committee has the authority under the LTIP to grant stock options; stock appreciation rights, restricted stock, restricted stock units, performance stock, performance units, and other forms of equity-based or equity-related awards. Compensation cost is generally recorded on a straight-line basis over the vesting term of the shares based on the grant date value using the closing trading price.

Stock-based compensation expenses were \$1,502,724 and \$708,540 for the three months ended June 30, 2023 and 2022, respectively, and \$3,404,431 and \$1,379,378 for the six months ended June 30, 2023 and 2022, respectively. During the three months ended June 30, 2023, the Company granted 500,000 restricted stock units to members of management and none to members of the Board under the LTIP. During the six months ended June 30, 2023, the Company granted 1,232,090 restricted stock units to members of management and 742,000 restricted stock units to members of the Board under the LTIP. The total number of restricted stock units issued at June 30, 2023 was 3,425,537.

Unrecognized compensation expense related to restricted stock awards made by the Company was \$10,957,851 at June 30, 2023. As of June 30, 2023, the Company had 2,530,859 shares available for issuance under the 2021 Plan.

| | <u>Number of RSUs</u> | <u>Weighted Average Grant-Date Fair Value</u> |
|------------------------------|-----------------------|---|
| Balance at December 31, 2022 | 1,451,448 | \$ 5.67 |
| Awarded Legacy AeroClean | 1,974,090 | \$ 2.78 |
| Awarded Molekule Merger | 2,964,241 | \$ 3.40 |
| Forfeited/Vested | (901,764) | \$ 3.40 |
| Balance at June 30, 2023 | <u>5,488,015</u> | \$ 3.73 |

A total of 799,965 RSUs are vested at June 30, 2023.

Private Placements

On June 29, 2022, the Company completed a private placement in connection with a securities purchase agreement dated June 26, 2022 (the "2022 Private Placement"). In the 2022 Private Placement, the Company received gross cash proceeds of \$15,000,000 in connection with the issuance of (i) 1,500,000 shares of common stock and (ii) a warrant to purchase up to 1,500,000 shares of common stock, as amended (the "2022 Warrant"). The Warrant had an exercise price of \$11.00 per share, which amount was adjusted to \$2.00 per share in connection with the 2023 Private Placement (as defined, and further described below) and is exercisable until July 21, 2027. Net proceeds amounted to \$13,578,551 after issuance costs of \$1,421,449.

As the 2022 Warrant was liability classified, the gross proceeds and issuance costs were allocated to the 2022 Warrant liability based on its fair value with the residual being allocated to the common stock, resulting in the allocation of gross proceeds of \$13,995,000 and \$1,005,000 to the 2022 Warrant liability and common stock, respectively, and issuance costs of \$1,326,212 and \$95,237 were charged to expense and additional paid in capital, respectively.

In conjunction with the 2022 Private Placement, the Company entered into a registration rights agreement whereby the Company was required to register for resale and maintain the effectiveness of the registration statement that registers the resale of shares of common stock held by the selling stockholder and the shares of common stock issuable upon exercise of the 2022 Warrant. Pursuant to the registration rights agreement, the Company is liable for certain liquidated damages upon failure to comply with such registration rights. On January 27, 2023, the Company's registration statement on Form S-3 relating to the resale of 3,000,000 shares of common

stock by the selling stockholder listed in the prospectus (including 1,500,000 shares of common stock issued in the 2022 Private Placement and 1,500,000 shares of common stock issuable upon the exercise of the outstanding 2022 Warrant acquired in the 2022 Private Placement) was declared effective by the SEC. The Company will not receive any proceeds in connection with the sale of common stock by the selling stockholder but will receive the exercise price of the 2022 Warrant to the extent the 2022 Warrant is exercised by the selling stockholder.

On May 3, 2023, the Company entered into a Securities Purchase Agreement with the Selling Stockholder, pursuant to which the Company agreed to sell (i) 3,400,000 Shares, (ii) 3,125,000 shares of common stock that are issuable upon the exercise of the Series A Warrant, (iii) 6,250,000 shares of common stock that are issuable upon the exercise of the Series B Warrant and (iv) 2,850,000 shares of common stock that are issuable upon the exercise of the Pre-Funded Warrant, for an aggregate purchase price of approximately \$9,971,500 (the “2023 Private Placement”). The Securities Purchase Agreement contains customary representations, warranties and agreements by the Company. The closing of the 2023 Private Placement occurred on May 5, 2023. The Company also agreed to reduce the exercise price of the 2022 Warrant owned by the Selling Stockholder to \$2.00 per share of common stock.

The Series A Warrant has an exercise price of \$1.60 per share of common stock, the Series B Warrant has an exercise price of \$1.84 per share of common stock, and the Pre-Funded Warrant has an exercise price of \$0.01 per share of common stock. The Series A Warrant, the Series B Warrant and the Pre-Funded Warrant are all exercisable as of June 30, 2023. The Series A Warrant will terminate on February 23, 2024. The Series B Warrant and the Pre-Funded Warrant will terminate on June 23, 2028.

As of June 30, 2023, the Selling Stockholder beneficially owns approximately 9.9% of the outstanding shares of common stock of the Company. Each of the Series A Warrant, the Series B Warrant and the Pre-Funded Warrant, contain an ownership limitation providing that the Selling Stockholder may not exercise the Series A Warrant, the Series B Warrant or the Pre-Funded Warrant with respect to any shares of common stock that would result in the Selling Stockholder beneficially owning more than 4.99% of the outstanding shares of common stock. The Selling Stockholder may increase or decrease this limitation upon notice to us, but in no event will any such limitation exceed 9.99%.

In connection with the 2023 Private Placement, the Company entered into a Registration Rights Agreement with the Selling Stockholder. Pursuant to the Registration Rights Agreement, the Company was required to file and maintain a resale registration statement with the SEC in order to register the shares sold to the Selling Stockholder and the shares underlying the Warrants. The Company will be obligated to pay certain liquidated damages to the Selling Stockholder if it fails to maintain the effectiveness of the registration statement pursuant to the terms of the Registration Rights Agreement. In accordance with the requirements of the Registration Rights Agreement, the Company filed a resale registration statement on Form S-3 covering the shares acquired by the Selling Shareholder and the shares issuable upon the conversion of the Series A Warrant, the Series B Warrant and the Pre-Funded Warrant. The Form S-3 was declared effective by the SEC on June 26, 2023.

14. Net Income (Loss) Per Common Share

Basic net income (loss) per common share is computed using the weighted average common shares outstanding during the period. Diluted net income (loss) per common share reflects the potential dilution from the assumed conversion of all dilutive securities such as unvested restricted stock units, the purchase option issued to the underwriters in the Public Offering (the “Underwriter Option”) and the 2022 Warrant using the treasury stock method. When the effects of the outstanding unvested restricted stock units, the Underwriter Option and the 2022 Warrant are anti-dilutive, they are not included in the calculation of diluted net loss per common share.

[Table of Contents](#)

The following table sets forth the computation of basic and diluted net loss per common share for the three months ended June 30, 2023 and 2022:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|-----------------------------|-----------------------|---------------------------|-----------------------|
| | 2023 | 2022 | 2023 | 2022 |
| Net loss | <u>\$ (24,969,242)</u> | <u>\$ (5,172,277)</u> | <u>\$ (34,902,648)</u> | <u>\$ (7,750,241)</u> |
| Basic and diluted weighted average common shares | <u>33,017,565</u> | <u>13,894,119</u> | <u>31,185,329</u> | <u>13,885,923</u> |
| Basic and diluted net loss per common share | <u>\$ (0.76)</u> | <u>\$ (0.37)</u> | <u>\$ (1.12)</u> | <u>\$ (0.56)</u> |

The following outstanding common stock equivalents were excluded from the computation of diluted net loss per share for the periods presented because including them would have been anti-dilutive:

| | Six Months Ended June 30, | |
|------------------------|---------------------------|------------------|
| | 2023 | 2022 |
| Outstanding Warrants | 13,725,000 | 1,500,000 |
| Restricted stock units | 5,488,015 | 626,268 |
| Total | <u>19,213,015</u> | <u>2,126,268</u> |

15. Income Taxes

Income tax benefit was \$93,156 and \$219,832 for the six months ended June 30, 2023 and June 30, 2022, respectively. The Company recorded a deferred tax liability of \$1,598,000 as a result of the acquisition of Legacy Molekule related mainly to the intangible assets acquired in the transaction. The Company maintains a valuation allowance on the deferred tax assets that are not more likely than not to be utilized.

16. Aura Smart Air Merger Agreement

On August 14, 2023, Molekule informed Aura that it was terminating the Merger Agreement, in accordance with Section 8.02 and Section 8.01(c)(i) of the Merger Agreement. The Company believes that Aura has committed a material and incurable breach of Section 6.02 of the Merger Agreement such that Molekule is entitled to terminate the Merger Agreement pursuant to Section 8.01(c)(i) (B) of the Merger Agreement. On August 14, 2023, Aura notified Molekule that it disputed the termination of the Merger Agreement and believes that Molekule has breached Section 6.09 of the Merger Agreement. Molekule disputes that it is in breach of the Merger Agreement.

Notwithstanding the termination of the Merger Agreement, Molekule intends to continue discussions with Aura regarding mutually beneficial future sales, marketing and technology collaboration and intends to continue discussions regarding the parties' current arrangements in connection with, and certain disagreements under, the Technology Collaboration Agreement and Co-Distribution Agreement entered into contemporaneously with the Merger Agreement.

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

The following discussion and analysis should be read in conjunction with the historical condensed consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q (this “Quarterly Report”) as well as our audited financial statements for the fiscal year ended December 31, 2022 included in our Annual Report on Form 10-K, as amended, for the fiscal year ended December 31, 2022, filed with the Securities and Exchange Commission (the “SEC”) on April 3, 2023 (our “Annual Report”). This discussion contains forward-looking statements reflecting our current expectations and estimates and assumptions concerning events and financial trends that may affect our future operating results or financial position. Actual results and the timing of events may differ materially from those contained in these forward-looking statements due to a number of factors, including those discussed in the sections entitled “Cautionary Statement Regarding Forward-Looking Statements” and “Risk Factors” appearing elsewhere in this Quarterly Report. You should review the “Risk Factors” section of our Annual Report as well, for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained in the following discussion and analysis.

Overview

Molekule Group, Inc. (formerly known as AeroClean Technologies, Inc.) is a pathogen elimination technology company on a mission to keep work, play and life going by improving indoor air quality. We have the largest range of proprietary and patented, FDA-cleared air purification devices to address the rapidly growing global air purification market. Our air hygiene product, Pürgo™, is an FDA 510(k) cleared, Class II medical device that provides continuous air filtration, sanitization and supplemental ventilation solutions with technology that can be applied in any indoor space – including in hospitals, offices and even in elevators. Pürgo™ products feature SteriDuct™, a proprietary germicidal UV-C technology. In addition, our Air Pro and Air Mini+ air purifiers leverage a PECO technology that can destroy viruses, bacteria, mold, allergens, VOCs, chemicals and more from the air. Our purpose is simple: to never stop innovating solutions that keep people healthy and safe, so life never stops.

In June 2022, the FDA granted our Pürgo technology 510(k) clearance for use in healthcare and other markets for which product performance to reduce the amount of certain airborne particles and infectious microbes in an indoor environment must be validated to specific standards.

On January 12, 2023, we completed our acquisition of Legacy Molekule (the “Molekule Merger”), which produces and sells air purification devices that can be used by both consumer and commercial users. These air purifiers incorporate our patented PECO technology to capture and destroy a wide range of organic material, such as bacteria, viruses, mold and volatile organic compounds.

On May 3, 2023 we entered into a securities purchase agreement with a single institutional investor pursuant to which we agreed to sell at an aggregate purchase price of approximately \$9,971,500, 3,400,000 shares of our common stock, a Series A warrant to purchase up to 3,125,000 shares of common stock at an exercise price of \$1.60 per share, a Series B Warrant to purchase up to 6,250,000 shares of common stock at an exercise price of \$1.84 per share and a Pre-Funded Warrant to purchase up to 2,850,000 shares of common stock with an initial exercise price of \$1.60 per share, with \$1.59 to be pre-funded, leaving a remaining nominal exercise price of \$0.01 per share (the “2023 Private Placement”). The Series A Warrant is exercisable until February 23, 2024 and the Series B Warrant and the Pre-Funded Warrant are exercisable until June 23, 2028.

As part of our business strategy, we continually evaluate a wide array of strategic opportunities, including the acquisition, disposition or licensing of intellectual property, mergers and acquisitions, joint ventures and other strategic transactions. We may seek to acquire technologies, product lines and companies that operate in businesses similar to our own or that are ancillary, complementary or adjacent to our own or in which we do not currently operate. Such businesses could operate in the air purification space or more generally in the health and wellness space or in other industries. We could also seek to merge with or into another company or sell all or substantially all of our assets to another company. In connection with these activities, we may enter into non-binding letters of intent as we assess the commercial appeal of potential strategic transactions. Any transactions that we enter into could be material to our business, financial condition and operating results.

As previously disclosed, on February 26, 2023, we entered into the Agreement and Plan of Merger, dated as of February 26, 2023 (the “Merger Agreement”), by and among us, Aura Smart Air Ltd., a company organized under the laws of the State of Israel (“Aura”) and Avatar Merger Sub Ltd., a company organized under the laws of the State of Israel, our wholly owned subsidiary.

On August 14, 2023, we informed Aura that we were terminating the Merger Agreement, in accordance with Section 8.02 and Section 8.01(c)(i) of the Merger Agreement. We believe that Aura has committed a material and incurable breach of Section 6.02 of the Merger Agreement such that we are entitled to terminate the Merger Agreement pursuant to Section 8.01(c)(i)(B) of the Merger Agreement. On August 14, 2023, Aura notified us that it disputed the termination of the Merger Agreement and believes that we have breached Section 6.09 of the Merger Agreement. We dispute that we are in breach of the Merger Agreement.

Notwithstanding the termination of the Merger Agreement, we intend to continue discussions with Aura regarding mutually beneficial future sales, marketing and technology collaboration and intend to continue discussions regarding the parties' current arrangements in connection with, and certain disagreements under, the Technology Collaboration Agreement and Co-Distribution Agreement entered into contemporaneously with the Merger Agreement.

Effects of Macroeconomic and Geopolitical Events on Our Business

We continue to monitor the COVID-19 pandemic and its variants, including the emergence of variant strains, which have impacted and could continue to adversely impact global commercial activity and have contributed to significant declines and volatility in financial markets. Across many industries, including the Company's, COVID-19 — among other factors — has negatively impacted personnel and operations at third-party manufacturing and component part supplier facilities in the United States and around the world. These disruptions have adversely impacted the availability and cost of raw materials and component parts. For example, various electronic components and semi-conductor chips have become increasingly difficult to source and, when available, may be subject to substantially longer lead times and higher costs than historically applicable. While the Company's manufacturing run rate is not currently being impacted, past shortages have impacted the Company's ability to manufacture units.

In addition, U.S. and global financial markets have experienced disruption due to various macroeconomic and geopolitical events. These include, but are not limited to, rising inflation, rising interest rates, the risk of a recession and other ongoing global conflicts. For example, on March 10, 2023, SVB was closed by the California Department of Financial Protection and Innovation, which appointed the FDIC as receiver. At the time of the closure, we held securities in sweep accounts purchased through SVB but managed in segregated custodial accounts by a third-party asset manager. On March 12, 2023, the FDIC announced that Signature Bank was closed and that the FDIC was appointed as receiver. On March 13, 2023, the FDIC announced that all of SVB's deposits and substantially all of its assets had been transferred to a newly created, full-service FDIC-operated bridge bank, SVBB. SVBB assumed all loans that were previously held by SVB. On March 27, 2023, First-Citizens Bank & Trust Company assumed all of SVBB's customer deposits and certain other liabilities and acquired substantially all of SVBB's loans and certain other assets from the FDIC. While we have had full access to the assets in our sweep accounts since March 13, 2023, we may be impacted by other disruptions to the U.S. banking system caused by the developments involving SVB, including potential delays in our ability to transfer funds and potential delays in making payments to vendors while new banking relationships are established. We cannot predict at this time to what extent our or our collaborators, employees, suppliers, contract manufacturers and/or vendors could be negatively impacted by these and other macroeconomic and geopolitical events.

Further, geopolitical events and global economic sanctions resulting from the ongoing conflict between Russia and Ukraine may impact new or existing projects and the prices and availability of raw materials, energy and other materials. These events may also impact energy and regulatory policy nationally or regionally for the impacted regions. In addition, we have experienced and are experiencing varying levels of inflation resulting in part from increased shipping and transportation costs, raw material costs and labor costs.

Management cannot predict the full impact of the COVID-19 pandemic, instability in the banking system and geopolitical events on our sales and marketing channels and supply chain, and, as a result, the ultimate extent of the effects on the Company are highly uncertain and will depend on future developments. Such effects could exist for an extended period of time. We continue to actively monitor the impacts of the foregoing events on our business and may take further actions that impact operations as may be required by federal, state or local authorities or that we determine is in the best interests of our employees, customers, suppliers and stockholders.

Results of Operations

The following table summarizes our results of operations for the periods indicated:

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

| | Three Months Ended June 30, | | | Six Months Ended June 30, | | |
|---|-----------------------------|--------------------|---------------------|---------------------------|--------------------|---------------------|
| | 2023 | 2022 | Change | 2023 | 2022 | Change |
| Product revenues | \$ 13,242,959 | \$ 70,918 | \$ 13,172,041 | \$ 21,592,380 | \$ 77,652 | \$ 21,514,728 |
| Cost of sales | 8,763,888 | 36,126 | 8,727,762 | 13,438,147 | 39,890 | 13,398,257 |
| Gross profit | 4,479,071 | 34,792 | 4,444,279 | 8,154,233 | 37,761 | 8,116,471 |
| Operating expenses: | | | | | | |
| Selling, general and administrative | 15,005,356 | 4,105,066 | 10,900,290 | 28,666,969 | 6,247,290 | 22,419,679 |
| Research and development | 1,174,846 | 579,061 | 595,785 | 1,422,625 | 1,110,544 | 312,081 |
| Total operating expenses | 16,180,202 | 4,684,127 | 11,496,075 | 30,089,594 | 7,357,834 | 22,731,760 |
| Loss from operations | (11,701,131) | (4,649,335) | (7,051,796) | (21,935,361) | (7,320,073) | (14,615,288) |
| Change in fair value of warrant liability | (12,050,500) | (650,000) | (11,400,500) | (10,324,500) | (650,000) | (9,674,500) |
| Interest expense | (1,443,009) | — | (1,443,009) | (2,691,686) | — | (2,691,686) |
| Other expense | 132,242 | — | 132,242 | (44,257) | — | (44,257) |
| Total other expense | (1,310,767) | — | (1,310,767) | (2,735,943) | — | (2,735,943) |
| Loss before income tax benefit | (25,062,398) | (5,299,335) | (8,362,563) | (34,995,804) | (7,970,073) | (14,615,289) |
| Income tax benefit | 93,156 | (127,058) | 220,214 | 93,156 | (219,832) | 312,988 |
| Net loss | <u>(24,969,242)</u> | <u>(5,172,277)</u> | <u>(10,763,883)</u> | <u>(34,902,648)</u> | <u>(7,750,241)</u> | <u>(19,774,187)</u> |

Revenues and Cost of Sales

Total revenues increased to \$13,242,959 from \$70,918, or by \$13,172,041, for the three months ended June 30, 2023, compared to the same period of 2022. Revenue increased primarily due to our acquisition of Legacy Molekule. Revenue primarily increased due to an increase in sales of purifiers (an increase of approximately \$5,117,510), an increase in the sale of filters (approximately \$9,635,273), offset by returns (approximately \$717,920) and discounts and promotions (approximately \$874,038).

Total revenues increased to \$21,592,380 from \$77,652, or by \$21,514,728, for the six months ended June 30, 2023, compared to the same period of 2022. Revenue increased primarily due to our acquisition of Legacy Molekule. Revenue primarily increased due to an increase in sales of purifiers (approximately \$8,192,653), an increase in sales of filters (an increase of approximately \$15,538,375), offset by returns (approximately \$1,076,844) and discounts and promotions (approximately \$1,187,612).

Cost of sales increased to \$8,763,888 from \$36,126, or by \$8,727,762, for the three months ended June 30, 2023, compared to the same period of 2022. Cost of sales increased primarily due to our acquisition of Legacy Molekule. Cost of sales increased in line with revenues.

Cost of sales increased to \$13,438,147 from \$39,890, or by \$13,398,257, for the six months ended June 30, 2023, compared to the same period of 2022. Cost of sales increased primarily due to our acquisition of Legacy Molekule. Cost of sales increased in line with revenues.

Operating Expenses

Selling, General and Administrative Expenses

Selling, general and administrative expenses (“SG&A”) consist primarily of costs related to our employees, independent contractors and consultants. Other significant general and administrative expenses include accounting and legal services and expenses associated with obtaining and maintaining patents as well as marketing and advertising services and expenses associated with establishing our brand and developing our website, marketing materials and call center.

For the three months ended June 30, 2023 and 2022, we incurred \$15,005,356 and \$4,105,066, respectively, of SG&A expenses. The increase of \$10,900,290 was primarily due to an increase in salaries and wages (approximately \$3,522,059), stock-based compensation (approximately \$1,193,165), marketing expense (approximately \$64,280), legal fees (approximately \$895,651), public company costs (an increase of approximately \$1,011,866), rent expense (approximately \$1,193,165), and digital advertising (approximately \$1,874,668).

For the six months ended June 30, 2023 and 2022, we incurred \$28,666,969 and \$6,247,290 respectively, of SG&A expenses. The increase of \$22,419,679 was primarily due to an increase in salaries and wages (approximately \$7,133,140), stock-based compensation (approximately \$2,025,052), legal fees (approximately \$3,243,948), public company costs (an increase of approximately \$1,234,716), rent expense (approximately \$1,825,965), and digital advertising (approximately \$3,045,805).

Research and Development Expenses

Since our inception, we have focused our resources on our research and development activities. We expense research and development costs as they are incurred. Our research and development expenses primarily consist of outsourced engineering, product development and manufacturing design costs. For the three months ended June 30, 2023 and 2022, we incurred \$1,174,846 and \$579,061, respectively, in research and development costs. Research and development expenses increased by \$595,785 in the three months ended June 30, 2023, as compared to the prior year period. Research and development expenses increased for the three months ended June 30, 2023 due to the research and development associated with the building of Molekule 360, our indoor air quality management solution platform, which was launched in July 2023.

For the six months ended June 30, 2023 and 2022, we incurred \$1,422,625 and \$1,110,544, respectively, in research and development costs. Research and development expenses increased by \$312,081 in the six months ended June 30, 2023, as compared to

the prior year period due to the launch of Molekule 360.

Change in Fair Value of Warrant Liability

The change in fair value of the warrant liability was a non-cash loss of \$12,050,500 and \$10,324,500 resulting from an increase in the fair value of the warrant liability, which was reported in our unaudited condensed consolidated statement of operations for the three and six months ended June 30, 2023, respectively. A significant transaction prompted the 2022 Warrant modification and additional issuance of the 2023 Warrants, leading to an increase in warrant liability and corresponding expenses during the quarter.

Net Income (Loss)

Our net losses were \$24,709,356 and \$5,172,277 for the three months ended June 30, 2023 and 2022, respectively, and \$34,642,763 and \$7,750,241 for the six months ended June 30, 2023 and 2022, respectively. Losses increased in the first and second quarters of 2023 as compared to the first and second quarters of 2022 for the reasons set forth above including higher cost of goods sold, higher SG&A expenses, change in fair value of the warrant liability and greater interest expenses.

Liquidity and Capital Resources

Sources of Liquidity

As of June 30, 2023, we had cash of \$5,269,376 compared to cash of \$22,062,657 as of December 31, 2022. The Company's net cash used in operating activities was \$27,329,771 for the six months ended June 30, 2023 as compared to \$4,312,706 used in operating activities for the prior year period.

On May 2, 2023, the Company reached an agreement with SVB to amend the mezzanine loan agreement so as to provide for the deferral of principal payments from April 2024 to April 2025. The Company also reached an agreement with SVB, to amend the Senior Term Loan to extend the maturity date from April 2026 to March 2028. The amendment of the Mezzanine Term Loan to defer principal payments and the amendment of the senior term loan agreement to extend the maturity date collectively resulted in a deferral of approximately \$6.1 million of principal payments through June 30, 2025.

On May 3, 2023, the Company entered into a Securities Purchase Agreement with the Selling Stockholder, pursuant to which the Company agreed to sell (i) 3,400,000 Shares, (ii) 3,125,000 shares of common stock that are issuable upon the exercise of the Series A Warrant, (iii) 6,250,000 shares of common stock that are issuable upon the exercise of the Series B Warrant and (iv) 2,850,000 shares of common stock that are issuable upon the exercise of the Pre-Funded Warrant, for an aggregate purchase price of approximately \$9,971,500 (the "Private Placement"). The Securities Purchase Agreement contains customary representations, warranties and agreements by the Company. The closing of the Private Placement occurred on May 5, 2023. The Company also agreed to reduce the exercise price of the 2022 Warrant owned by the Selling Stockholder to \$2.00 per share of common stock.

The Series A Warrant has an exercise price of \$1.60 per share of common stock, the Series B Warrant has an exercise price of \$1.84 per share of common stock, and the Pre-Funded Warrant has a nominal exercise price per share of common stock. The Series A Warrant is exercisable until February 23, 2024. The Series B Warrant and the Pre-Funded Warrant are exercisable until June 23, 2028.

As of June 30, 2023, the Selling Stockholder beneficially owns approximately 9.9% of the outstanding shares of common stock of the Company. The Series A Warrant, the Series B Warrant and the Pre-Funded Warrant each contains an ownership limitation providing that the Selling Stockholder may not exercise the Series A Warrant, the Series B Warrant or the Pre-Funded Warrant with respect to any shares of common stock that would result in the Selling Stockholder beneficially owning more than 4.99% of the outstanding shares of common stock. The Selling Stockholder may increase or decrease this limitation upon notice to us, but in no event will any such limitation exceed 9.99%.

In connection with the 2023 Private Placement, the Company entered into the Registration Rights Agreement with the Selling Stockholder. Pursuant to the Registration Rights Agreement, the Company was required to file and maintain a resale registration statement with the SEC in order to register the shares sold to the Selling Stockholder and the shares underlying the Warrants. The Company will be obligated to pay certain liquidated damages to the Selling Stockholder if it fails to maintain the effectiveness of the registration statement pursuant to the terms of the Registration Rights Agreement. In accordance with the requirements of the

Registration Rights Agreement, the Company filed a resale registration statement on Form S-3 covering the shares acquired by the Selling Shareholder and the shares issuable upon the conversion of the Series A Warrant, the Series B Warrant and the Pre-Funded Warrant. The Form S-3 was declared effective by the SEC on June 26, 2023.

Debt and Financing Arrangements

Upon the closing of our acquisition of Molekule, Inc. on January 12, 2023, we assumed indebtedness under (1) a Loan and Security Agreement with SVB, (2) a Mezzanine Loan and Security Agreement with SVB and (3) a Facility Term Loan with Trinity Capital, Inc (“Trinity”).

Senior Term Loan. In June 2016, Legacy Molekule entered into a Loan and Security Agreement with SVB (as amended, amended and restated, supplemented or otherwise modified from time to time, the “Senior Term Loan”). As of June 30, 2023, the outstanding principal balance under the Senior Term Loan was \$4.4 million. The Senior Term Loan bears interest at an annual rate equal to the greater of (x) the Prime Rate plus 1% or (y) 4.25%. As of June 30, 2023, the interest rate was 9.25% per year. The maturity date for the Senior Term Loan is March 1, 2028. Interest is payable monthly in arrears. The principal is repayable in 59 equal monthly installments beginning on May 12, 2023. The Senior Term Loan contains customary representations and warranties, affirmative and negative covenants (including financial covenants), events of default and termination provisions. The financial covenants include requirements to maintain a minimum cash balance of \$2.0 million and an annual revenue target of \$50.0 million for the calendar year ending March 31, 2024. Revenue targets for periods occurring after March 31, 2024 shall be mutually agreed by the Company and SVB. The Company is also required to maintain its primary operating and other deposit accounts and securities accounts with SVB and its affiliates. As of June 30, 2023, the Company had cash of \$5,269,376.

Under the Senior Loan Agreement, the Company initially had two term loans with original principal balances of \$5.1 million and \$2.5 million, respectively, and a \$15 million revolving line of credit. The agreement was modified first on March 9, 2020 (“First LMA”) and further amended on June 19, 2020 (“Second LMA”), March 22, 2021 (“Third LMA”), May 19, 2022 (“Fourth LMA”), October 1, 2022 (“Fifth LMA”), January 12, 2023 (“Sixth LMA”) and May 31, 2023 (“Seventh LMA”). The First LMA extended the maturity date of the revolving line of credit, while the Second LMA increased the principal balance of the term loan from \$5.0 million to \$5.1 million and extended the maturity date to December 31, 2023. The borrowing capacity of the revolver was increased from \$5.0 million to \$15.0 million with the Second LMA. The Third LMA extended the maturity date of the revolving line from March 31, 2021 to March 31, 2023. The revolving line of credit ceased with the execution of the Fourth LMA. Further, the two tranches of term loans were converted into a single term loan under the Fourth LMA. The Fifth LMA amended the minimum revenue target to \$50,000,000 for the period ending December 31, 2023. We joined the Senior Term Loan as a co-borrower under the Sixth LMA. Under the Seventh LMA, the parties agreed to extend the maturity date of the term loan from April 1, 2026 to March 1, 2028.

Mezzanine Term Loan. In March 2021, Legacy Molekule entered into a Mezzanine Loan and Security Agreement with SVB, pursuant to which SVB issued to Legacy Molekule a \$30.0 million mezzanine term loan (as amended, amended and restated, supplemented or otherwise modified from time to time, the “Mezzanine Term Loan”), initially consisting of a Mezzanine Term Loan A tranche of \$15.0 million and a Mezzanine Term Loan B tranche of \$15.0 million. On May 31, 2023, the Mezzanine Term Loan was amended to combine the Mezzanine Term Loan A tranche and the Mezzanine Term Loan B tranche. As of June 30, 2023, the outstanding principal balance under the Mezzanine Term Loan was \$30 million. The Mezzanine Term Loan bears interest at a floating rate per annum equal to the greater of (x) the Prime Rate plus 6.00% or (y) 9.25%. As of June 30, 2023, the interest rate was 14.25% per year. The Mezzanine Term Loan matures in March 2028. Interest is payable monthly in arrears. The principal of the Mezzanine Term Loan is repayable in 36 equal monthly installments beginning on April 1, 2025. The Mezzanine Loan and Security Agreement contains customary representations and warranties, affirmative and negative covenants (including financial covenants), events of default and termination provisions. The financial covenants include requirements to maintain a minimum cash balance of \$2.0 million and an annual revenue target of \$50.0 million for the calendar year ending March 31, 2024. Revenue targets for periods occurring after March 31, 2024 shall be mutually agreed by the Company and SVB. The Company is also required to maintain all of its deposit accounts, the cash collateral account and excess cash with SVB and its affiliates.

Facility Term Loan. In June 2020, Legacy Molekule entered into a Facility Term Debt Agreement (the “Facility Term Loan”) with Trinity in order to obtain lease financing related to funding the build out of the Company’s filter manufacturing plant. The Company became a co-lessee under this agreement upon the closing of the Molekule Merger. Legacy Molekule drew down \$2.9 million in June 2020, \$0.6 million in September 2020, \$0.9 million in December 2020 and \$0.5 million in August 2021. Principal and interest are paid monthly with the principal being repaid in equal monthly installments from the month after the amount was drawn until April 1, 2026,

with the last two months' payments having been made at the inception of each loan. At the end of the term, Trinity also requires the Company to pay down an additional 10% of the total term draw down amount, which results in an additional payment of \$0.4 million in total for all the draws. This additional payment is being accreted to the total outstanding amount over the term of the Facility Term Loan and resulted in an incremental \$0.3 million of long-term debt to Trinity as of June 30, 2023. As of June 30, 2023, the outstanding principal balance under the Facility Term Loan was \$2.4 million. The Facility Term Loan contains customary representations and warranties, affirmative and negative covenants and event of default provisions.

Leases

On February 1, 2021, we entered into a lease with Garden Bio Science Partners, LLC, an entity controlled by the chair of our board of directors, with a term of ten years at an annual base rent of \$260,000, subject to escalation of 2.5% on an annual basis. As of June 30, 2023, the future minimum lease payments under this arrangement are approximately \$2,317,000.

In February 2019, Legacy Molekule entered into a lease agreement for office space in San Francisco, California. The leased premises consist of 38,000 square feet of office space. The lease expires in August 2026. The lease calls for monthly base rental payments of \$209,231 commencing in the first month and fixed annual base rental increases of 3%. Rent expense is accounted for on a straight-line basis. Rent expense under this lease was \$691,753 and \$1,286,468 for the three and six months ended June 30, 2023, respectively. Since June 2023, the lessor has been drawing under an existing letter of credit, which was put in place as security for payment of the monthly base rental payments. Amounts available under such letter of credit will be fully utilized by September, 2023, after which the Company will be required to pay its monthly base rental payments to the lessor. The Company is currently in discussions with the lessor to renegotiate the terms of the lease. There is no assurance that any such renegotiation will be successful.

Future Funding Requirements and Outlook

We have incurred operating losses each year since our inception. These losses are expected to continue in the future because we plan to continue to make investments to develop and market our products and to establish our consumables and service business and otherwise adapt our business plan to changes in the marketplace and customer needs. We also expect to continue to incur increased costs to comply with corporate governance, internal controls and similar requirements applicable to public companies. The Company has historically relied on outside capital through the issuance of equity securities, securities convertible or exchangeable into equity securities and borrowings under financing arrangements (collectively, "capital"). The Company will need to continue to rely on outside capital for the foreseeable future and if capital is not raised by the third quarter of 2023, there is a substantial doubt about our ability to continue as a going concern.

The Company incurred a net loss of \$34,902,648 and its net cash used in operating activities was \$28,001,369 for the six months ended June 30, 2023. In addition, the Company's accumulated deficit was \$42,819,441 at June 30, 2023. The Company's recurring losses from operations, recurring cash used in operating activities, accumulated deficit, expected working capital needs to fund its combined operations and new debt obligations as a result of the acquisition of Molekule, Inc. in January 2023 (see Note 3), raise substantial doubt about its ability to continue as a going concern. The Company's ability to fund its operations is dependent upon management's plans, which include raising capital, managing costs and generating sufficient revenues to offset costs. There can be no assurances that the Company will be able to secure any such additional capital in the third quarter of 2023 on acceptable terms and conditions, or at all, or that the business will generate sufficient revenues to offset costs and generate a profit. Accordingly, management has concluded there is substantial doubt as to the Company's ability to continue as a going concern within one year after the date the financial statements are issued. Under our debt agreements (the Senior Term Loan and the Mezzanine Term Loan) with SVB, we are required to generate revenue of at least \$50 million for the twelve months ended March 31, 2024. Non-compliance with this requirement may result in the debt maturity dates becoming accelerated.

The design, manufacture, sale, marketing and servicing of our devices and other products is capital-intensive. We will require substantial additional capital to continue to develop our products and services, conduct research and development and fund operations for the foreseeable future. We will need to raise additional capital to scale our manufacturing, roll out other future products or services, and also to continue to offer our devices and any services relating to those products. In particular, we are especially focused on developing new devices, SaaS solutions, advanced sensor technology and smart building integrations and IoT devices, which will require additional capital. In addition, we may need to raise funds to finance future capital needs, such as making principal and interest payments under our loan agreements. Moreover, if we continue to pursue an acquisition strategy, we would need to raise incremental capital in order to finance the purchase price to be paid to target stockholders for any cash consideration. There can be no assurances that we will be able to raise the incremental capital needed on terms acceptable to us, or at all.

Over the long-term, we will continue to have significant capital requirements, and expect to devote resources to grow the Company's operations. As a result of these funding requirements, as discussed above, we will need to obtain additional financing by engaging in debt and/or equity offerings or seeking additional borrowings. To the extent that we raise additional capital through the sale of convertible debt or equity securities, or pay for acquisitions in whole or in part with the issuance of equity securities (either as merger consideration or to finance the cash portion of merger consideration), the ownership interests of our common stockholders will be diluted, and the terms of these securities may include liquidation or other preferences that adversely affect the rights of our common stockholders. Debt financing, if available, may involve agreements that include covenants limiting or restricting our ability to take specific actions, such as incurring additional debt, making capital expenditures or declaring dividends. The availability of debt financing or equity capital will depend upon our financial condition and results of operations as well as prevailing market conditions. There can be no assurances that we will be able to raise the incremental capital needed on terms acceptable to us, or at all.

Inflation

Inflation has adversely affected our business, and we expect this to continue through the end of 2023. We have been and expect to continue to be negatively impacted by increased component and logistics costs. In addition, our cost of labor and materials may increase, which would negatively impact our business and financial results. Alternatively, deflation may cause a deterioration of global and regional economic conditions, which could impact unemployment rates and consumer discretionary spending. These, and other factors that may increase the risk of significant deflation, could negatively impact our business and results of operations.

Critical Accounting Policies and Estimates

Our management's discussion and analysis of our financial condition and results of operations is based on our condensed financial statements, which we have prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"). The preparation of the financial statements in accordance with U.S. GAAP requires us to make estimates and assumptions that affect the reported amounts and related disclosures. We evaluate these estimates, judgments and methodologies on an ongoing basis. We base our estimates on historical experience and on various other assumptions that we believe are reasonable. Our actual results could differ from those estimates.

Our significant accounting policies are more fully described in Note 2, Summary of Significant Accounting Policies to our audited consolidated financial statements included in our Annual Report. We believe that the accounting policies are critical for fully understanding and evaluating our financial condition and results of operations.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements to encourage companies to provide prospective information to investors. This Quarterly Report includes forward-looking statements that reflect our current expectations and projections about our future results, performance and prospects. Forward-looking statements include all statements that are not historical in nature or are not current facts. When used in this Quarterly Report, the words "anticipate," "believe," "continue," "could," "estimate," "expect," "intend," "likely," "may," "might," "plan," "possible," "potential," "predict," "project," "should," "target," "will," "would" or the negative of these terms or similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain such identifying words. These forward-looking statements are based on our current expectations and assumptions about future events and are based on currently available information as to the outcome and timing of future events.

These forward-looking statements are subject to a number of risks, uncertainties, assumptions and other factors that could cause our actual results, performance and prospects to differ materially from those expressed in, or implied by, these forward-looking statements. Factors that might cause such a difference include, but are not limited to, those discussed in our filings with the SEC, in particular those discussed under the heading “Risk Factors” in our Annual Report, including the following:

- general economic conditions in the markets where we operate;
- the impact of the COVID-19 pandemic and related prophylactic measures;
- expected timing of regulatory approvals and product launches;
- non-performance of third-party vendors and contractors;
- risks related to our ability to successfully sell our products and the market reception to and performance of our products, including our new Molekule 360 indoor air quality management solutions;
- the possibility that our products do not ultimately perform in line with our testing or that prior test results may not be replicated in future studies;
- compliance with, and changes to, applicable laws and regulations;
- our limited operating history;
- our ability to manage growth;
- our ability to obtain additional financing when and if needed;
- our ability to expand product offerings;
- our ability to compete with others in our industry;
- our ability to protect our intellectual property;
- the ability of certain stockholders to determine the outcome of matters that require stockholder approval;
- our ability to retain the listing of our common stock on Nasdaq;
- our ability to defend against legal proceedings;
- success in retaining or recruiting, or changes required in, our officers, key employees or directors;
- our ability to achieve the expected benefits from the Molekule Merger, including within the expected time frames (if at all);
- the ability to successfully integrate Legacy Molekule;
- the incurrence of unexpected costs, liabilities or delays relating to the Molekule Merger;
- the risk that goodwill or identifiable intangible assets (including such items recorded with respect to the Molekule Merger) could become impaired; and our ability to successfully consummate acquisitions.

In light of these risks, uncertainties and assumptions, you are cautioned not to put undue reliance on any forward-looking

statements in this Quarterly Report. These statements should be considered only after carefully reading this entire Quarterly Report. Except as required under the federal securities laws and rules and regulations of the SEC, we undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Additional risks that we may currently deem immaterial or that are not presently known to us could also cause the forward-looking events discussed in this Quarterly Report not to occur.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

As a smaller reporting company, we are not required to provide the information required by Item 305 of Regulation S-K.

Item 4. Controls and Procedures.

Disclosure controls and procedures are controls and other procedures that are designed to ensure that the information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to provide reasonable assurance that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company’s management, including its principal executive and principal financial officers (who are our Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”), respectively), or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognized that disclosure controls and procedures can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met.

In connection with the preparation of this Quarterly Report on Form 10-Q for the three months ended June 30, 2023, an evaluation was performed under the supervision of and with the participation of management, including our CEO and CFO, of the effectiveness of the Company’s disclosure controls and procedures. Based on that evaluation, our CEO and CFO have concluded that our disclosure controls and procedures were effective as of June 30, 2023.

In addition, our management, including our CEO and CFO, has concluded that the financial statements included in this Quarterly Report fairly present, in all material respects, our financial position, results of operations and cash flows for the periods presented in this Quarterly Report in conformity with U.S. GAAP.

Inherent Limitations on Effectiveness of Controls

The design of any system of control is based upon certain assumptions about the likelihood of future events. There can be no assurance that any design will succeed in achieving its stated objectives under all future events, no matter how remote, or that the degree of compliance with the policies or procedures may not deteriorate. Because of its inherent limitations, disclosure controls and procedures may not prevent or detect all misstatements. Accordingly, even effective disclosure controls and procedures can provide only reasonable assurance of achieving their control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints, and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with policies and procedures may deteriorate.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the period covered by this Quarterly Report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings.

From time to time, we are subject to legal proceedings in the normal course of operating our business. The outcome of litigation, regardless of the merits, is inherently uncertain. In August 2022, the Company received notice of a complaint filed in the U.S. District Court for the Southern District of New York (the “Court”) by Sterilumen, Inc. (“Sterilumen”), a wholly-owned subsidiary of Applied

UV, Inc., in connection with the marketing and sale of the Company's patented air purification products. In the complaint, the plaintiff alleged trademark infringement, violation of fair competition practices and damages to Sterilumen. On March 13, 2023, the Court dismissed Sterilumen's claims with prejudice and ruled that the Company's counterclaims remained extant. We subsequently agreed with Sterilumen that Sterilumen will not challenge the Court's dismissal and will not bring any future claim against the Company alleging infringement from the use of SteriDuct or AeroClean and that the Company will file a notice to dismiss its counterclaims without prejudice.

We are not currently party to any legal proceedings, the adverse outcome of which, individually or in the aggregate, we believe will have a material adverse effect on our business, financial condition or results of operations.

Item 1A. Risk Factors.

There have been no material changes to our risk factors from those disclosed in our Annual Report.

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

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

During the fiscal quarter ended June 30, 2023, none of our directors or officers informed us of the adoption, modification or termination of a "Rule 10b5-1 trading arrangement" or "non-Rule 10b5-1 trading arrangement," as those terms are defined in Regulation S-K, Item 408.

Item 6. Exhibits.

The following exhibits are filed as part of, or incorporated by reference into, this Quarterly Report.

- 3.1 [Amended and Restated Certificate of Incorporation \(incorporated by reference to Exhibit 3.1 to the Company's Annual Report on Form 10-K \(File No. 001-41096\), filed with the SEC on June 30, 2023\).](#)
- 3.2 [Second Amended and Restated Bylaws \(incorporated by reference to Exhibit 3.3 to the Company's Current Report on Form 8-K \(File No. 001-41096\), filed with the SEC on January 12, 2023\).](#)
- 31.1* [Certification of Principal Executive Officer Pursuant to Rules 13a-14\(a\) and 15d-14\(a\) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.](#)
- 31.2* [Certification of Principal Financial Officer Pursuant to Rules 13a-14\(a\) and 15d-14\(a\) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.](#)
- 32.1** [Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.](#)
- 32.2** [Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.](#)
- 101.INS* Inline XBRL Instance Document
- 101.SCH* Inline Taxonomy Extension Schema Document
- 101.CAL* Inline Taxonomy Extension Calculation Linkbase Document

[Table of Contents](#)

| | |
|----------|---|
| 101.DEF* | Inline Taxonomy Extension Definition Linkbase Document |
| 101.LAB* | Inline Taxonomy Extension Label Linkbase Document |
| 104* | Cover Page Interactive Data File (Embedded within the Inline XBRL document and included in Exhibit 101) |

* Filed herewith

** Furnished herewith

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

MOLEKULE GROUP, INC.

By: /s/ Jason DiBona

Jason DiBona

Chief Executive Officer

Date: August 14, 2023

By: /s/ Ryan Tyler

Ryan Tyler

Chief Financial Officer

Date: August 14, 2023

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO RULE 13a-14(a) AND RULE 15d-14(a)
OF THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED,
AS ADOPTED PURSUANT TO SECTION 302 OF
THE SARBANES-OXLEY ACT OF 2002**

I, Jason DiBona, certify that:

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

Date: August 14, 2023

/s/ Jason DiBona

Jason DiBona
Principal Executive Officer

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO RULE 13a-14(a) AND RULE 15d-14(a)
OF THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED,
AS ADOPTED PURSUANT TO SECTION 302 OF
THE SARBANES-OXLEY ACT OF 2002**

I, Ryan Tyler, certify that:

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

Date: August 14, 2023

/s/ Ryan Tyler

Ryan Tyler
Principal Financial Officer

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

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, in connection with the Quarterly Report of Molekule Group, Inc. (the "Company") on Form 10-Q for the period ended June 30, 2023, as filed with the Securities and Exchange Commission on the date hereof (the "Periodic Report"), I, Jason DiBona, as Principal Executive Officer of the Company, hereby certify that:

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

Date: August 14, 2023

/s/ Jason DiBona

Jason DiBona

Principal Executive Officer

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

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, in connection with the Quarterly Report of Molekule Group, Inc. (the "Company") on Form 10-Q for the period ended June 30, 2023, as filed with the Securities and Exchange Commission on the date hereof (the "Periodic Report"), I, Ryan Tyler, as Principal Financial Officer of the Company, hereby certify that:

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

Date: August 14, 2023

/s/ Ryan Tyler

Ryan Tyler

Principal Financial Officer
