
UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended April 1, 2006

or

Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934
for the transition period from _____ to _____

Commission file number 0-20852

ULTRALIFE BATTERIES, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction
of incorporation or organization)

16-1387013

(I.R.S. Employer Identification No.)

2000 Technology Parkway, Newark, New York 14513

(Address of principal executive offices)

(Zip Code)

(315) 332-7100

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act (Check One)

Large Accelerated Filer Accelerated Filer Non-accelerated filer

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

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

Common stock, \$.10 par value – 14,779,841 shares of common stock outstanding, net of 727,250 treasury shares, as of April 1, 2006.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

ULTRALIFE BATTERIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands, Except Per Share Amounts)
(unaudited)

	April 1, 2006	December 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 3,491	\$ 3,214
Trade accounts receivable (less allowance for doubtful accounts of \$435 at April 1, 2006 and \$458 at December 31, 2005)	12,869	10,965
Inventories	18,868	19,446
Due from insurance company	311	482
Deferred tax asset — current	2,470	2,508
Prepaid expenses and other current assets	1,408	2,747
Total current assets	<u>39,417</u>	<u>39,362</u>
Property, plant and equipment, net	<u>19,602</u>	<u>19,931</u>
Other assets:		
Security deposits and other	243	243
Deferred tax asset — non-current	21,169	21,221
	<u>21,412</u>	<u>21,464</u>
Total Assets	<u>\$ 80,431</u>	<u>\$ 80,757</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Short-term debt and current portion of long-term debt	\$ 7,184	\$ 7,715
Accounts payable	5,336	5,218
Income taxes payable	4	—
Other current liabilities	4,761	5,450
Total current liabilities	<u>17,285</u>	<u>18,383</u>
Long-term liabilities:		
Debt and capital lease obligations	25	25
Other long-term liabilities	282	242
Total long-term liabilities	<u>307</u>	<u>267</u>
Commitments and contingencies (Note 9)		
Shareholders' equity:		
Preferred stock, par value \$0.10 per share, authorized 1,000,000 shares; none outstanding	—	—
Common stock, par value \$0.10 per share, authorized 40,000,000 shares; issued - 15,507,091 at April 1, 2006 and 15,471,446 at December 31, 2005	1,551	1,547
Capital in excess of par value	131,045	130,530
Accumulated other comprehensive loss	(981)	(1,054)
Accumulated deficit	(66,398)	(66,538)
	<u>65,217</u>	<u>64,485</u>
Less — Treasury stock, at cost — 727,250 shares	2,378	2,378
Total shareholders' equity	<u>62,839</u>	<u>62,107</u>
Total Liabilities and Shareholders' Equity	<u>\$ 80,431</u>	<u>\$ 80,757</u>

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

ULTRALIFE BATTERIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Dollars in Thousands, Except Per Share Amounts)
(unaudited)

	Three-Month Periods Ended	
	April 1, 2006	April 2, 2005
Revenues	\$ 18,319	\$ 15,363
Cost of products sold	14,349	13,340
Gross margin	3,970	2,023
Operating expenses:		
Research and development	960	846
Selling, general, and administrative	2,782	2,901
Total operating expenses	3,742	3,747
Operating income/(loss)	228	(1,724)
Other income (expense):		
Interest income	45	60
Interest expense	(205)	(193)
Gain on insurance settlement	148	—
Miscellaneous	8	(3)
Income/(loss) before income taxes	224	(1,860)
Income tax provision/(benefit)-current	4	(17)
Income tax provision/(benefit)-deferred	80	(293)
Total income taxes	84	(310)
Net Income/(Loss)	\$ 140	\$ (1,550)
Earnings/(Loss) per share — basic	\$ 0.01	\$ (0.11)
Earnings/(Loss) per share — diluted	\$ 0.01	\$ (0.11)
Weighted average shares outstanding — basic	14,756	14,376
Weighted average shares outstanding — diluted	15,130	14,376

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

ULTRALIFE BATTERIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in Thousands)
(unaudited)

	<u>Three-Month Periods Ended</u>	
	<u>April 1, 2006</u>	<u>April 2, 2005</u>
OPERATING ACTIVITIES		
Net income (loss)	\$ 140	\$ (1,550)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	835	802
Gain on asset disposal	—	(4)
Gain on insurance settlement	(148)	—
Foreign exchange gain	8	10
Non-cash stock-based compensation	258	20
Change in deferred taxes	80	(281)
Changes in operating assets and liabilities:		
Accounts receivable	(1,883)	(815)
Inventories	614	(2,090)
Prepaid expenses and other current assets	1,355	390
Insurance receivable relating to fires	251	795
Income taxes payable	4	—
Accounts payable and other liabilities	(558)	2,536
Net cash provided by (used in) operating activities	<u>956</u>	<u>(187)</u>
INVESTING ACTIVITIES		
Purchase of property and equipment	(383)	(533)
Proceeds from asset disposal	—	8
Sales of securities	—	1,000
Net cash (used in) provided by investing activities	<u>(383)</u>	<u>475</u>
FINANCING ACTIVITIES		
Net change in revolving credit facilities	(37)	(176)
Proceeds from issuance of common stock	261	714
Principal payments on long-term debt and capital lease obligations	(500)	(667)
Net cash used in financing activities	<u>(276)</u>	<u>(129)</u>
Effect of exchange rate changes on cash	<u>(20)</u>	<u>23</u>
Increase in cash and cash equivalents	277	182
Cash and cash equivalents at beginning of period	3,214	10,529
Cash and cash equivalents at end of period	<u>\$ 3,491</u>	<u>\$ 10,711</u>
SUPPLEMENTAL CASH FLOW INFORMATION		
Taxes paid	<u>\$ 2</u>	<u>\$ —</u>
Interest paid	<u>\$ 184</u>	<u>\$ 158</u>

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

ULTRALIFE BATTERIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollar Amounts in Thousands – Except Share and Per Share Amounts)
(unaudited)

1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals and adjustments) considered necessary for a fair presentation of the condensed consolidated financial statements have been included. Results for interim periods should not be considered indicative of results to be expected for a full year. Reference should be made to the consolidated financial statements contained in the Company's Form 10-K for the twelve-month period ended December 31, 2005.

The year-end condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

The Company's monthly closing schedule is a weekly-based cycle as opposed to a calendar month-based cycle. While the actual dates for the quarter-ends will change slightly each year, the Company believes that there are not any material differences when making quarterly comparisons.

2. EARNINGS (LOSS) PER SHARE

Basic earnings per share are calculated by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per share are calculated by dividing net income by potentially dilutive common shares, which include stock options and warrants.

Net loss per share is calculated by dividing net loss by the weighted average number of common shares outstanding during the period. The impact of conversion of dilutive securities, such as stock options and warrants, are not considered where a net loss is reported as the inclusion of such securities would be anti-dilutive. As a result, basic loss per share is the same as diluted loss per share.

The computation of basic and diluted (loss) earnings per share is summarized as follows:

(In thousands, except per share data)	Three-Month Periods Ended	
	April 1, 2006	April 2, 2005
Net Income/(Loss) (a)	\$ 140	\$ (1,550)
Average Shares Outstanding – Basic (b)	14,756	14,376
Effect of Dilutive Securities:		
Stock Options / Warrants	374	—
Average Shares Outstanding – Diluted (c)	15,130	14,376
EPS – Basic (a/b)	\$.01	\$ (0.11)
EPS – Diluted (a/c)	\$.01	\$ (0.11)

The Company also had the equivalent of 720,094 options and warrants outstanding for the three-month period ended April 2, 2005, which were not included in the computation of diluted EPS because these securities would have been anti-dilutive for that period.

3. STOCK-BASED COMPENSATION

The Company has various stock-based employee compensation plans. Effective January 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment" ("FAS 123R") requiring that compensation cost relating to share-based payment transactions be recognized in the financial statements. The cost is measured at the grant date, based on the calculated fair value of the award, and is recognized as an expense over the employee's requisite service period (generally the vesting period of the equity award). The Company adopted FAS 123R using the modified prospective method and, accordingly, did not restate prior periods presented in this Form 10-Q to reflect the fair value method of recognizing compensation cost. Under the modified prospective approach, FAS 123R applies to new awards and to awards that were outstanding on January 1, 2006 that are subsequently modified, repurchased or cancelled.

The shareholders of the Company have approved four stock option plans that permit the grant of options. In addition, the shareholders of the Company have approved the grant of options outside of these plans. Under the 1991 stock option plan, 100,000 shares of Common Stock were reserved for grant to key employees and consultants of the Company. These options expired on September 13, 2001, at which date the plan terminated. All options granted under the 1991 plan were Non-Qualified Stock Options ("NQSOs").

The shareholders of the Company have also approved a 1992 stock option plan that is substantially the same as the 1991 stock option plan. The shareholders approved reservation of 1,150,000 shares of Common Stock for grant under the plan. During 1997, the Board of Directors approved an amendment to the plan increasing the number of shares of Common Stock reserved by 500,000 to 1,650,000. Options granted under the 1992 plan are either Incentive Stock Options ("ISOs") or NQSOs. Key employees are eligible to receive ISOs and NQSOs; however, directors and consultants are eligible to receive only NQSOs. All ISOs vest at twenty percent per year for five years and expire on the sixth year. The NQSOs vest immediately and expire on the sixth year. On October 13, 2002, this plan expired and as a result, there are no more shares available for grant under this plan. As of April 1, 2006, there were 113,900 stock options outstanding under this plan.

Effective July 12, 1999, the Company granted the current CEO options to purchase 500,000 shares of Common Stock at \$5.19 per share outside of any of the stock option plans. Of these, 50,000 options were exercisable on the grant date, and the remaining options became exercisable in annual increments of 90,000 over a five-year period commencing July 12, 2000 through July 12, 2004, and expire on July 12, 2005. As of April 1, 2006, there were no options outstanding under this plan. Since these options were granted without shareholder approval, any gains resulting from exercises of these options that cause the CEO compensation to exceed \$1,000 in any year may not be deductible by the Company for income tax purposes.

Effective December 2000, the Company established the 2000 stock option plan which is substantially the same as the 1991 stock option plan. The shareholders approved reservation of 500,000 shares of Common Stock for grant under the plan. In December 2002, the shareholders approved an amendment to the plan increasing the number of shares of Common Stock reserved by 500,000, to a total of 1,000,000. In June 2004, shareholders approved an amendment to the 2000 Plan, increasing the number of shares of Common Stock by 750,000, as well as adding flexibility to award restricted stock, among other things. Options granted under the revised 2000 plan are either ISOs or NQSOs. Key employees are eligible to receive ISOs and NQSOs; however, directors and

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consultants are eligible to receive only NQSOs. Most ISOs vest at twenty percent per year for five years and expire within the sixth or seventh year. Certain ISOs granted to officers vest over three years and expire in the seventh year. All NQSOs issued to non-employee directors vest immediately and expire in either the sixth or seventh year. Some NQSOs issued to non-employees vest immediately and expire within three years; others have the same vesting characteristics as options given to employees. As of April 1, 2006, there were 1,316,471 stock options outstanding under this plan.

As a result of adopting FAS 123R on January 1, 2006, the Company recorded compensation cost related to stock options of \$258 for the three-month period ended April 1, 2006. As of April 1, 2006, there was \$1,025 of total unrecognized compensation costs related to outstanding stock options, which is expected to be recognized over a weighted average period of 1.58 years.

Prior to January 1, 2006, the Company applied Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations which required compensation costs to be recognized based on the difference, if any, between the quoted market price of the stock on the grant date and the exercise price. As all options granted to employees under such plans had an exercise price at least equal to the market value of the underlying common stock on the date of grant, and given the fixed nature of the equity instruments, no stock-based employee compensation cost relating to stock options was reflected in net income (loss).

The effect on net loss and loss per share if the Company had applied the fair value recognition provisions of Statement of Financial Accounting Standards ("SFAS") No. 148, "Accounting for Stock-Based Compensation – Transition and Disclosure, an Amendment of SFAS No. 123", to stock-based employee compensation for the three month period ended April 2, 2005 was as follows:

Net loss, as reported	\$ (1,550)
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects	—
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	<u>(518)</u>
Pro forma net loss	\$ (2,068)
Loss per share:	
Basic – as reported	\$ (0.11)
Basic – pro forma	\$ (0.14)
Diluted – as reported	\$ (0.11)
Diluted – pro forma	\$ (0.14)

The Company uses the Black-Scholes option-pricing model to estimate fair value of stock-based awards. The following weighted average assumptions were used to value options granted during the first quarter of 2006:

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Risk-free interest rate	4.31%
Volatility factor	61.25%
Dividends	0%
Weighted average expected life (years)	3.12

The Company calculates expected volatility for stock options by taking an average of historical volatility over the past 5 years and a computation of implied volatility. Prior to 2006, the computation of expected volatility was based solely on historical volatility. The computation of expected term was determined based on historical experience of similar awards, giving consideration to the contractual terms of the stock-based awards and vesting schedules. The interest rate for periods within the contractual life of the award is based on the U.S. Treasury yield in effect at the time of grant.

Stock option activity for the first quarter of 2006 is summarized as follows (dollars in thousands, except per share amounts):

	Number of Shares	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Shares under option at January 1, 2006	1,430,271	\$ 10.94		
Options granted	41,500	\$ 12.68		
Options exercised	(35,100)	\$ 7.30		
Options forfeited	(1,800)	\$ 6.58		
Options expired	(4,500)	\$ 16.03		
Shares under option at April 1, 2006	1,430,371	\$ 11.07	4.48 years	\$ 4,454
Vested and expected to vest at April 1, 2006	1,383,206	\$ 11.10	4.44 years	\$ 4,328
Options exercisable at April 1, 2006	976,745	\$ 12.42	4.51 years	\$ 2,271

The weighted average fair value of options granted during the three months ended April 1, 2006 was \$5.51. The total intrinsic value of options (which is the amount by which the stock price exceeded the exercise price of the options on the date of exercise) exercised during the three months ended April 1, 2006 was \$164. During the three months ended April 1, 2006, the amount of cash received from the exercise of stock options was \$256. The total fair value of shares vested during the period is \$175.

Prior to adopting FAS 123R, all tax benefits resulting from the exercise of stock options were presented as operating cash flows in the Condensed Statement of Cash Flows. FAS 123R requires cash flows from excess tax benefits to be classified as a part of cash flows from financing activities. Excess tax benefits are realized tax benefits from tax deductions for exercised options in excess of the deferred tax asset attributable to stock compensation costs for such options. The Company did not record any excess tax benefits in the first quarter of 2006. Cash received from option exercises during the first quarter of 2006 and 2005 was \$261 and \$714, respectively.

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4. COMPREHENSIVE INCOME (LOSS)

The components of the Company's total comprehensive income (loss) were:

	Three-Month Periods Ended	
	April 1, 2006	April 2, 2005
Net income (loss)	\$ 140	\$ (1,550)
Foreign currency translation adjustments	52	(152)
Change in fair value of derivatives, net of tax	21	119
Total comprehensive income (loss)	<u>\$ 213</u>	<u>\$ (1,583)</u>

5. INVENTORIES

Inventories are stated at the lower of cost or market with cost determined under the first-in, first-out (FIFO) method. The composition of inventories was:

	April 1, 2006	December 31, 2005
Raw materials	\$ 8,965	\$ 8,817
Work in process	8,221	8,648
Finished goods	2,473	2,849
	<u>19,659</u>	<u>20,314</u>
Less: Reserve for obsolescence	791	868
	<u>\$ 18,868</u>	<u>\$ 19,446</u>

6. PROPERTY, PLANT AND EQUIPMENT

Major classes of property, plant and equipment consisted of the following:

	April 1, 2006	December 31, 2005
Land	\$ 123	\$ 123
Buildings and leasehold improvements	4,229	4,229
Machinery and equipment	38,984	37,876
Furniture and fixtures	789	788
Computer hardware and software	2,205	2,197
Construction in progress	474	1,059
	<u>46,804</u>	<u>46,272</u>
Less: Accumulated depreciation	27,202	26,341
	<u>\$ 19,602</u>	<u>\$ 19,931</u>

During the quarter ended April 1, 2006, the Company recorded a non-cash addition of \$71 of property, plant and equipment related to the extinguishment of a receivable.

7. DEBT

On June 30, 2004, the Company closed on a new \$25,000 credit facility, comprised of a five-year \$10,000 term loan component and a three-year \$15,000 revolving credit component. The facility is collateralized by essentially all of the assets of the Company, including its subsidiary in the U.K. The term loan component is paid in equal monthly installments over 5 years. The rate of interest, in general, is based upon either a LIBOR rate or Prime, plus a Eurodollar spread (dependent upon a debt to

earnings ratio within a predetermined grid). This facility replaced the Company's \$15,000 credit facility that expired on the same date. Availability under the revolving credit component is subject to meeting certain financial covenants, whereas availability under the previous facility was limited by various asset values. The lenders of the new credit facility are JP Morgan Chase Bank and Manufacturers and Traders Trust Company, with JP Morgan Chase Bank acting as the administrative agent. The Company is required to meet certain financial covenants, including a debt to earnings ratio, an EBIT (as defined) to interest expense ratio, and a current assets to total liabilities ratio.

On June 30, 2004, the Company drew down the full \$10,000 term loan. The proceeds of the term loan, to be repaid in equal monthly installments of \$167 over five years, were used for the retirement of outstanding debt and capital expenditures. From June 30, 2004 through August 1, 2004, the interest rate associated with the term loan was based on LIBOR plus a 1.25% Eurodollar spread. On July 1, 2004, the Company entered into an interest rate swap arrangement in the notional amount of \$10,000 to be effective on August 2, 2004, related to the \$10,000 term loan, in order to take advantage of historically low interest rates. The Company received a fixed rate of interest in exchange for a variable rate. The swap rate received was 3.98% for five years. The total rate of interest paid by the Company is equal to the swap rate of 3.98% plus the Eurodollar spread stipulated in the predetermined grid associated with the term loan. From August 2, 2004 to September 30, 2004, the total rate of interest associated with the outstanding portion of the \$10,000 term loan was 5.23%. On October 1, 2004, this adjusted rate increased to 5.33%, on January 1, 2005 the adjusted rate increased to 5.73%, and on April 1, 2005, the adjusted rate increased to 6.48%, the maximum amount under the current grid structure, and remains at that rate as of April 1, 2006. Derivative instruments are accounted for in accordance with SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" which requires that all derivative instruments be recognized in the financial statements at fair value. The fair value of this arrangement at April 1, 2006 resulted in an asset of \$123, all of which was reflected as short-term.

As of April 1, 2006, the Company had \$6,667 outstanding under the term loan component of its credit facility with its primary lending bank and nothing was outstanding under the revolver component. At April 1, 2006, the Company was not in compliance with the EBIT (as defined) to interest covenant, as amended. Subsequent to the end of the quarter, however, the banks provided the Company with a waiver of the financial covenant violation as of the end of the first quarter of 2006. (See Note 13 concerning a bank waiver for this financial covenant violation.) As a result of the uncertainty of the Company's ability to comply with the more restrictive financial covenants within the next year, the Company continued to classify all of the debt associated with this credit facility as a current liability on the Condensed Consolidated Balance Sheet as of April 1, 2006. While the revolver arrangement provides for up to \$15,000 of borrowing capacity, including outstanding letters of credit, the actual borrowing availability may be limited by the financial covenants. At April 1, 2006, the Company had \$2,200 of outstanding letters of credit related to this facility. In addition, the Company's additional borrowing capacity under the revolver component of the credit facility as of April 1, 2006 was approximately \$4,500.

As of April 1, 2006, the Company's wholly-owned U.K. subsidiary, Ultralife Batteries (UK) Ltd., had approximately \$494 outstanding under its revolving credit facility with a commercial bank in the U.K. This credit facility provides the Company's U.K. operation with additional financing flexibility for its working capital needs. Any borrowings against this credit facility are collateralized with that company's outstanding accounts receivable balances. There was approximately \$280 in additional borrowing capacity under this credit facility as of April 1, 2006.

8. INCOME TAXES

The liability method, prescribed by SFAS No. 109, "Accounting for Income Taxes", is used in accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are

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measured using the enacted tax rates and laws that may be in effect when the differences are expected to reverse.

For the three-month period ended April 1, 2006, the Company recorded an income tax provision of \$84, related mainly to the income reported for U.S. operations during the period. The Company has not recognized a deferred tax asset pertaining to cumulative historical losses for its U.K. subsidiary, as management does not believe it is more likely than not that they will realize the benefit of these losses. As a result, there is no provision for income taxes for the U.K. subsidiary reflected in the Condensed Consolidated Statement of Income.

At April 1, 2006, the Company has a deferred tax asset of \$23,639 reflecting significant net operating losses related to past years' cumulative losses. The Company believes that it is more likely than not that it will be able to utilize the U.S. net operating loss carryforwards that have accumulated over time. Management's belief is based on the expectation that the U.S. federal and state deferred tax assets will be realized primarily through future taxable income from operations, and partly from reversing taxable temporary differences. The Company will continually monitor the assumptions and performance results to assess the realizability of the tax benefits of the U.S. net operating losses and other deferred tax assets.

The Company has determined that a change in ownership as defined under Internal Revenue Code Section 382 occurred during the fourth quarter of 2003 and again during the third quarter of 2005. As such, the domestic net operating loss carryforward will be subject to an annual limitation. Management believes such limitation will not impact the Company's ability to realize the deferred tax asset. In addition, certain of the Company's NOL carryforwards are subject to U.S. alternative minimum tax such that carryforwards can offset only 90% of alternative minimum taxable income. This limitation did not have an impact on income taxes determined for 2005.

9. COMMITMENTS AND CONTINGENCIES

As of April 1, 2006, the Company had open capital commitments to purchase approximately \$146 of production machinery and equipment.

The Company estimates future costs associated with expected product failure rates, material usage and service costs in the development of its warranty obligations. Warranty reserves are based on historical experience of warranty claims and generally will be estimated as a percentage of sales over the warranty period. In the event the actual results of these items differ from the estimates, an adjustment to the warranty obligation would be recorded. Changes in the Company's product warranty liability during the first three months in 2006 were as follows:

Balance at December 31, 2005	\$ 464
Accruals for warranties issued	18
Settlements made	<u>(22)</u>
Balance at April 1, 2006	<u>\$ 460</u>

A retail end-user of a product manufactured by one of the Company's customers (the "Customer"), made a claim against the Customer wherein it asserted that the Customer's product, which is powered by an Ultralife battery, does not operate according to the Customer's product specification. No claim has been filed against Ultralife. However, in the interest of fostering good customer relations, in September 2002, Ultralife agreed to lend technical support to the Customer in defense of its claim. Additionally, Ultralife assured the Customer that it would honor its warranty by replacing any batteries that may be

determined to be defective. Subsequently, the Company learned that the end-user and the Customer settled the matter. In February 2005, Ultralife and the Customer entered into a settlement agreement. Under the terms of the agreement, Ultralife has agreed to provide replacement batteries for product determined to be defective, to warrant each replacement battery under the Company's standard warranty terms and conditions, and to provide the Customer product at a discounted price for a period of time in recognition of the Customer's administrative costs in responding to the claim of the retail end-user. In consideration of the above, the Customer released Ultralife from any and all liability with respect to this matter. Consequently, the Company does not anticipate any further expenses with regard to this matter other than its obligations under the settlement agreement. The Company's warranty reserve as of April 1, 2006 includes an accrual related to anticipated replacements under this agreement. Further, the Company does not expect the ongoing terms of the settlement agreement to have a material impact on the Company's operations or financial condition.

The Company is subject to legal proceedings and claims that arise in the normal course of business. The Company believes that the final disposition of such matters will not have a material adverse effect on the financial position, results of operations or cash flows of the Company.

In conjunction with the Company's purchase/lease of its Newark, New York facility in 1998, the Company entered into a payment-in-lieu of tax agreement, which provides the Company with real estate tax concessions upon meeting certain conditions. In connection with this agreement, a consulting firm performed a Phase I and II Environmental Site Assessment, which revealed the existence of contaminated soil and ground water around one of the buildings. The Company retained an engineering firm, which estimated that the cost of remediation should be in the range of \$230. Through April 1, 2006, total costs incurred have amounted to approximately \$100, none of which have been capitalized. In February 1998, the Company entered into an agreement with a third party which provides that the Company and this third party will retain an environmental consulting firm to conduct a supplemental Phase II investigation to verify the existence of the contaminants and further delineate the nature of the environmental concern. The third party agreed to reimburse the Company for fifty percent (50%) of the cost of correcting the environmental concern on the Newark property. The Company has fully reserved for its portion of the estimated liability. Test sampling was completed in the spring of 2001, and the engineering report was submitted to the New York State Department of Environmental Conservation (NYSDEC) for review. NYSDEC reviewed the report and, in January 2002, recommended additional testing. The Company responded by submitting a work plan to NYSDEC, which was approved in April 2002. The Company sought proposals from engineering firms to complete the remedial work contained in the work plan. A firm was selected to undertake the remediation and in December 2003 the remediation was completed, and was overseen by the NYSDEC. The report detailing the remediation project, which included the test results, was forwarded to NYSDEC and to the New York State Department of Health (NYSDOH). The NYSDEC, with input from the NYSDOH, requested that the Company perform additional sampling. A work plan for this portion of the project was written and delivered to the NYSDEC and approved. In November 2005, additional soil, sediment and surface water samples were taken from the area outlined in the work plan, as well as groundwater samples from the monitoring wells. The Company received the laboratory analysis and met with the NYSDEC in March 2006 to discuss the results. The Company's outside environmental consulting firm is preparing a final investigation report to be submitted to the NYSDEC by the end of May 2006. The environmental consulting firm previously estimated that the final cost to the Company to remediate the requested area would be approximately \$28, based on the submitted work plan. This further analysis will increase the estimated remediation costs modestly. At April 1, 2006 and December 31, 2005, the Company had \$45 and \$38, respectively, reserved for this matter.

The Company has had certain "exigent", non-bid contracts with the government, which have been subject to an audit and final price adjustment, which have resulted in decreased margins compared with the original terms of the contracts. As of April 1, 2006, there were no outstanding exigent contracts with the government. As part of its due diligence, the government has conducted post-

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audits of the completed exigent contracts to ensure that information used in supporting the pricing of exigent contracts did not differ materially from actual results. In September 2005, the Defense Contracting Audit Agency (DCAA) presented its findings related to the audits of three of the exigent contracts, suggesting a potential pricing adjustment of approximately \$1,400 related to reductions in the cost of materials that occurred prior to the final negotiation of these contracts. The Company has reviewed these audit reports, has submitted its response to these audits and believes, taken as a whole, the proposed audit adjustments can be offset with the consideration of other compensating cost increases that occurred prior to the final negotiation of the contracts. While the Company believes that potential exposure exists relating to any final negotiation of these proposed adjustments, it cannot reasonably estimate what, if any, adjustment may result when finalized. Such adjustments could reduce margins and have an adverse effect on the Company's business, financial condition and results of operations.

10. BUSINESS SEGMENT INFORMATION

The Company reports its results in three operating segments: Non-rechargeable Batteries, Rechargeable Batteries, and Technology Contracts. The Non-rechargeable Batteries segment includes 9-volt, cylindrical and various other non-rechargeable specialty batteries. The Rechargeable Batteries segment includes the Company's lithium polymer and lithium ion rechargeable batteries and battery chargers and accessories. The Technology Contracts segment includes revenues and related costs associated with various development contracts. The Company looks at its segment performance at the gross margin level, and does not allocate research and development or selling, general and administrative costs against the segments. All other items that do not specifically relate to these three segments and are not considered in the performance of the segments are considered to be Corporate charges.

Three-Month Period Ended April 1, 2006

	Non-rechargeable Batteries	Rechargeable Batteries	Technology Contracts	Corporate	Total
Revenues	\$ 15,645	\$ 2,565	\$ 109	\$ —	\$ 18,319
Segment contribution	3,322	696	(48)	(3,742)	228
Interest expense, net				(160)	(160)
Miscellaneous				156	156
Income taxes-current				(4)	(4)
Income taxes-deferred				(80)	(80)
Net income					\$ 140
Total assets	\$ 46,103	\$ 3,907	\$ 0	\$ 30,421	\$ 80,431

Three Month Period Ended April 2, 2005

	Non-rechargeable Batteries	Rechargeable Batteries	Technology Contracts	Corporate	Total
Revenues	\$ 12,808	\$ 2,128	\$ 427	\$ —	\$ 15,363
Segment contribution	1,940	51	32	(3,747)	(1,724)
Interest expense, net				(133)	(133)
Miscellaneous				(3)	(3)
Income taxes-current				17	17
Income taxes-deferred				293	293
Net loss					\$ (1,550)
Total assets	\$ 38,850	\$ 4,461	\$ 510	\$ 38,255	\$ 82,076

11. FIRES AT MANUFACTURING FACILITIES

In May 2004 and June 2004, the Company experienced two fires that damaged certain inventory and property at its facilities. The May 2004 fire occurred at the Company's U.S. facility and was caused by cells that shorted out when a forklift truck accidentally tipped the cells over in an oven in an enclosed area. Certain inventory, equipment and a small portion of the building where the fire was contained were damaged. The June 2004 fire happened at the Company's U.K. location and mainly caused damage to various inventory and the U.K. company's leased facility. The fire was contained mainly in a bunkered, non-manufacturing area designed to store various material, and there was additional smoke and water damage to the facility and its contents. It is unknown how the U.K. fire was started. The fires caused relatively minor disruptions to the production operations, and had no impact on the Company's ability to meet customer demand during that quarter.

The total amount of the two losses and related expenses associated with Company-owned assets was approximately \$2,000. Of this total, approximately \$450 was related to machinery and equipment, approximately \$750 was related to inventory and approximately \$800 was required to repair and clean up the facilities. The insurance claim related to the fire at the Company's U.S. facility was finalized in March 2005. As of April 1, 2006, the Company had received notice of a final claim settlement for the U.K. facility. Through April 1, 2006, the Company has received approximately \$1,900 in cash from the insurance companies to compensate it for its losses. As a result of the final settlement for the fire at the U.K. facility, the Company reflected a gain of \$148 in the first quarter of 2006 related to equipment and inventory damage. At April 1, 2006, the Company's current assets in its Condensed Consolidated Balance Sheet included a receivable from insurance companies for \$311, representing remaining proceeds to be received. In April 2006 the Company received payment in final settlement.

12. RECENT ACCOUNTING PRONOUNCEMENTS AND DEVELOPMENTS

In February 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 155, "Accounting for Certain Hybrid Financial Instruments." SFAS No. 155 amends SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" and SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS No. 155 also resolves issues addressed in SFAS No. 133 Implementation Issue No. D1, "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets." SFAS No. 155 eliminates the exemption from applying SFAS No. 133 to interests in securitized financial assets so that similar instruments are accounted for in the same manner regardless of the form of the instruments. SFAS No. 155 allows a preparer to elect fair value measurement at acquisition, at issuance, or when a previously recognized financial instrument is subject to a re-measurement (new basis) event, on an instrument-by-instrument basis. SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The fair value election provided for in paragraph 4(c) of SFAS No. 155 may also be applied upon adoption of SFAS No. 155 for hybrid financial instruments that had been bifurcated under paragraph 12 of SFAS No. 133 prior to the adoption of this Statement. Earlier adoption is permitted as of the beginning of an entity's fiscal year, provided the entity has not yet issued financial statements, including financial statements for any interim period for that fiscal year. Provisions of SFAS No. 155 may be applied to instruments that an entity holds at the date of adoption on an instrument-by-instrument basis. The Company is currently assessing any potential impact of adopting this pronouncement.

In March 2006, the FASB issued Statement of Financial Accounting Standards No. 156 ("SFAS" No. 156), "Accounting for Servicing of Financial Assets," an amendment of FASB Statement No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS No. 156 requires all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable, and permits for subsequent measurement using either

fair value measurement with changes in fair value reflected in earnings or the amortization and impairment requirements of Statement No. 140. The subsequent measurement of separately recognized servicing assets and servicing liabilities at fair value eliminates the necessity for entities that manage the risks inherent in servicing assets and servicing liabilities with derivatives to qualify for hedge accounting treatment and eliminates the characterization of declines in fair value as impairments or direct write-downs. SFAS 156 is effective for an entity's first fiscal year beginning after September 15, 2006. The Company is assessing any potential impact of adopting this pronouncement.

13. SUBSEQUENT EVENTS AND LIQUIDITY

At April 1, 2006, the Company was not in compliance with the EBIT (as defined) to interest covenant pertaining to its \$25,000 credit facility, as amended, with its primary lending banks. On May 3, 2006, however, the banks provided the Company with a waiver of the financial covenant violation as of the end of the first quarter of 2006.

As a result of the uncertainty of the Company's ability to comply with the financial covenants within the next year, the Company is continuing to classify all of the debt associated with this credit facility as a current liability on the Condensed Consolidated Balance Sheet as of April 1, 2006.

While the Company believes relations with its lenders are good and has received waivers as necessary in the past, there can be no assurance that such waivers can always be obtained. In such case, the Company believes it has, in the aggregate, sufficient cash, cash generation capabilities from operations, working capital, and financing alternatives at its disposal, including but not limited to alternative borrowing arrangements and other available lenders, to fund operations in the normal course.

The Company continues to be optimistic about its future prospects and growth potential. The improvement in the Company's financial position in recent years has enhanced the Company's ability to acquire additional financing. The Company continually explores various sources of capital, including leasing alternatives, issuing new or refinancing existing debt, and raising equity through private or public offerings. Although it stays abreast of such financing alternatives, the Company believes it has the ability over the next 12 months to finance its operations primarily through internally generated funds, or through the use of additional financing that currently is available to the Company.

As of April 1, 2006, cash and cash equivalents totaled \$3,491, an increase of \$277 from the beginning of the year.

Management's plan to achieve sustained operational profitability and reduce the negative cash flows from operations that it experienced during 2005 includes reducing the build-up of inventory related to the production of BA-5390s and executing certain cost cutting objectives that were begun in September 2005. Additionally, the Company believes it has adequate third party financing available to fund its operations or could obtain other financing, if needed.

If the Company is unable to achieve its plans or unforeseen events occur, the Company may need to implement alternative plans. While the Company believes it could complete its original plans or alternative plans, if necessary, there can be no assurance that such alternatives would be available on acceptable terms and conditions or that the Company would be successful in its implementation of such plans.

On May 1, 2006, the Company entered into a definitive agreement to acquire substantially all of the assets of McDowell Research, Limited (McDowell), a manufacturer of military communications accessories located in Waco, Texas, for a total value of approximately \$25,000. The acquisition is expected to close by the end of July 2006. Under the terms of the agreement, the purchase price of approximately \$25,000 will consist of \$5,000 cash and a \$20,000 non-transferable convertible note to be held by the

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sellers. The cash portion is expected to be financed by Ultralife's primary lending banks. The \$20,000 convertible note carries a five year term and is convertible at \$15 per share into 1.33 million shares of Ultralife common stock, with a forced conversion feature at \$17.50 per share. Ultralife anticipates that this acquisition will be accretive in 2006.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements. This report contains certain forward-looking statements and information that are based on the beliefs of management as well as assumptions made by and information currently available to management. The statements contained in this report relating to matters that are not historical facts are forward-looking statements that involve risks and uncertainties, including, but not limited to, future demand for the Company's products and services, addressing the process of U.S. military procurement of batteries, the successful commercialization of the Company's advanced rechargeable batteries, general economic conditions, government and environmental regulation, finalization of non-bid government contracts, competition and customer strategies, technological innovations in the non-rechargeable and rechargeable battery industries, changes in the Company's business strategy or development plans, capital deployment, business disruptions, including those caused by fires, raw materials supplies, environmental regulations, and other risks and uncertainties, certain of which are beyond the Company's control. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may differ materially from those described herein as anticipated, believed, estimated or expected.

This Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the accompanying consolidated financial statements and notes thereto contained herein and the Company's consolidated financial statements and notes thereto contained in the Company's Form 10-K for the year ended December 31, 2005.

The financial information in this Management's Discussion and Analysis of Financial Condition and Results of Operations is presented in thousands of dollars.

General

Ultralife Batteries, Inc. is a global provider of power solutions for diverse applications. The Company develops, manufactures and markets a wide range of non-rechargeable and rechargeable batteries, charging systems and accessories for use in military, industrial and consumer portable electronic products. Through its range of standard products and engineered solutions, Ultralife is at the forefront of providing the next generation of power systems. The Company believes that its technologies allow the Company to offer batteries that are flexibly configured, lightweight and generally achieve longer operating time than many competing batteries currently available.

The Company reports its results in three operating segments: Non-rechargeable Batteries, Rechargeable Batteries, and Technology Contracts. The Non-rechargeable Batteries segment includes 9-volt, cylindrical and various other non-rechargeable specialty batteries. The Rechargeable Batteries segment includes the Company's lithium polymer and lithium ion rechargeable batteries and battery chargers and accessories. The Technology Contracts segment includes revenues and related costs associated with various development contracts. The Company looks at its segment performance at the gross margin level, and does not allocate research and development or selling, general and administrative costs against the segments. All other items that do not specifically relate to these three segments and are not considered in the performance of the segments are considered to be Corporate charges.

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Results of Operations (dollars in thousands, except per share amounts)

Three-month periods ended April 1, 2006 and April 2, 2005

Impact of Adoption of FAS 123R. Effective January 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment" ("FAS 123R") requiring that compensation cost relating to share-based payment transactions be recognized in the financial statements. The Company adopted the modified prospective method of adoption, resulting in no restatement of the Company's prior period results. The total amount of non-cash, stock-based compensation expense for the first quarter of 2006 was \$258. Since the Company had not adopted this pronouncement in 2005, there was no expense for share-based compensation in the Company's 2005 reported results. (See Note 3 for additional information.)

In order for investors to be able to accurately assess the change in the Company's operating performance from year to year, a reconciliation from the Company's reported results to a non-GAAP measurement is being provided. The table below presents a reconciliation from the reported results to a non-GAAP measurement by adjusting out the stock-based compensation expense included in the first quarter 2006 results and comparing it to the comparable period results in 2005.

	Three-Month Period Ended April 1, 2006 (as reported)	FAS 123R Impact	Three-Month Period Ended April 1, 2006 (as adjusted)	Three-Month Period Ended April 2, 2005 (as reported)
Revenues	\$ 18,319	\$ —	\$ 18,319	\$ 15,363
Cost of Products Sold	14,349	(34)	14,315	13,340
Gross Margin	3,970	34	4,004	2,023
Operating Expenses	3,742	(224)	3,518	3,747
Operating Income/(Loss)	\$ 228	\$ 258	\$ 486	\$ (1,724)

The information provided in the table above provides the added information of showing the effect of the adoption of FAS123R on gross margin and operating expenses as they affect the Company's business model. The Company believes that this provides added information to investors who seek to utilize this information, which although not a GAAP measurement, is utilized in several recognized models of the value of a firm.

Revenues. Consolidated revenues for the three-month period ended April 1, 2006 amounted to \$18,319, an increase of \$2,956, or 19%, from the \$15,363 reported in the same quarter in the prior year. Non-rechargeable battery sales increased \$2,837, or 22%, from \$12,808 last year to \$15,645 this year. This increase is attributable to higher sales of batteries to commercial customers, particularly in the automotive telematics market, and modestly higher sales of a variety of batteries to military customers. These increases were offset in part by a decline in 9-volt sales. Rechargeable revenues increased \$437, or 21%, from \$2,128 to \$2,565, driven by increases in a broadening base of rechargeable products. Technology Contract revenues were \$109 in the first quarter of 2006, a decrease of \$318 from the \$427 reported in the first quarter of 2005 mainly attributable to the nearing of completion on the Company's development contract with General Dynamics.

Cost of Products Sold. Cost of products sold totaled \$14,349 for the quarter ended April 1, 2006, an increase of \$1,009, or 8%, over the same three-month period a year ago. The gross margin on consolidated revenues for the quarter was \$3,970, an increase of \$1,947 over the \$2,023 reported in the same quarter in the prior year due to the increase in revenues and a favorable product mix. As a percentage of revenues, gross margins amounted to 22% in the first quarter of 2006, an increase from 13% reported in the first quarter of 2005. Non-rechargeable battery margins were \$3,322, or 21% of revenues, for the first quarter of 2006 compared with \$1,940, or 15% of revenues, in the same period in 2005 primarily due to increased production efficiencies. In the Company's Rechargeable operations,

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gross margin amounted to \$696 in the first quarter of 2006, or 27% of revenues, compared to \$51, or 2% of revenues, in 2005, an improvement of \$645 related to the sales shift to higher margin batteries and chargers from digital camera batteries. Gross margins in the Technology Contract segment resulted in a loss of \$48, in the first quarter of 2006, compared to a profit of \$32, or 7%, in 2005, a decline of \$80 mainly due to varying margins realized under different technology contracts. The negative margin in the first quarter of 2006 resulted from an adjustment of the anticipated margin on the overall contract with General Dynamics.

Operating Expenses. Operating expenses for the three-month period ended April 1, 2006 totaled \$3,742, a \$5 decrease from the prior year's amount of \$3,747. Excluding the impact of expensing stock options of \$224 related to the adoption of FAS 123R in 2006, operating expenses decreased \$229. Research and development charges increased \$114 to \$960 in 2006 as the Company continued to increase its investment in new product development. Selling, general, and administrative expenses decreased \$119 to \$2,782. Excluding the impact of expensing stock options of \$217, selling, general, and administrative expenses decreased \$336 due mainly to lower consulting fees and professional services. Overall, operating expenses as a percentage of sales decreased to 20% in the first quarter of 2006 from 24% in 2005 due to the higher revenue base.

Other Income (Expense). Interest expense, net, for the first quarter of 2006 was \$160, an increase of \$27 from the comparable period in 2005, mainly related to lower interest income on lower invested cash as well as higher interest rates associated with the Company's outstanding debt. During the first quarter of 2006, the Company recorded a \$148 gain from insurance settlement related to the finalization of an insurance claim for the U.K. operation. (See Note 11 for additional information.)

Income Taxes. The Company reflected a tax provision of \$84 for the first quarter of 2006 compared with a benefit of \$310 in the first quarter of 2005. The effective tax rate for the first quarter of 2006 was 38% compared with 17% for the same period a year ago. The variation in the rates is due to the combination of income and losses in each of the Company's tax jurisdictions, which is particularly influenced by no tax provision or benefit being recorded for the Company's U.K. operation due to its history of losses. Since the Company has significant net operating loss carryforwards, the cash outlay for income taxes is expected to be nominal for quite some time into the future.

Net (Loss)/Income. Net income and income per share were \$140 and \$0.01, respectively, for the three months ended April 1, 2006, compared to net loss and loss per share of \$1,550 and \$0.11, respectively, for the same quarter last year, primarily as a result of the reasons described above. Average common shares outstanding used to compute basic earnings per share increased from 14,376,000 in the first quarter of 2005 to 14,756,000 in 2006 mainly due to stock option exercises.

Liquidity and Capital Resources (dollars in thousands)

As of April 1, 2006, cash and cash equivalents totaled \$3,491, an increase of \$277 from the beginning of the year. During the three-month period ended April 1, 2006, operating activities provided \$956 in cash as compared to a use of \$187 for the three-month period ended April 2, 2005. The generation of cash from operating activities in 2006 resulted mainly from an increase in net income and decreases in inventory, prepaids and other current assets, offset partially by increases in accounts receivable and a decrease in accounts payable and other liabilities. Decreases in inventory levels related to sales of BA-5390 batteries were partially offset by product line ramp ups to support the BA-5347 production and the rechargeable product line.

The Company used \$383 in cash for investing activities during the first three-month period of 2006 compared with \$475 in cash provided from investing activities in the same period in 2005. The Company used \$383 to purchase plant, property and equipment in 2006, down from \$533 for the same

period in 2005. In 2005, the Company sold certain investment securities that resulted in an increase in cash and cash equivalents of \$1,000.

During the three-month period ended April 1, 2006, the Company used \$276 in funds from financing activities compared to using \$129 in funds in the same period of 2005. The financing activities in 2006 included inflows from the issuance of stock, mainly as stock options were exercised during the period, offset by outflows for principal payments of term debt under the Company's primary credit facility. During the first three months of 2006, the Company issued 36,000 shares of common stock, primarily as a result of exercises of stock options, and the Company received approximately \$261 in cash proceeds as a result of these transactions.

Inventory turnover for the first three months of 2006 was an annualized rate of approximately 2.7 turns per year, down from the 3.4 turns for all of 2005. The Company's inventory levels are relatively high due a buildup of BA-5390 batteries during 2004 and 2005 in anticipation of orders from the military, a transition of certain European customers to newer, more cost-effective products, and the initial stocking of "Warstoppers" inventory for surge demand for the military. The Company's Days Sales Outstanding (DSOs) was an average of 47 days for the first three months of 2006, relatively consistent with the 45 days reflected for the full year of 2005.

At April 1, 2006, the Company had a capital lease obligation outstanding of \$48 for the Company's Newark, New York offices and manufacturing facilities.

As of April 1, 2006, the Company had open capital commitments to purchase approximately \$146 of production machinery and equipment.

On June 30, 2004, the Company closed on a new \$25,000 credit facility, comprised of a five-year \$10,000 term loan component and a three-year \$15,000 revolving credit component. The facility is collateralized by essentially all of the assets of the Company, including its subsidiary in the U.K. The term loan component is paid in equal monthly installments over 5 years. The rate of interest, in general, is based upon either a LIBOR rate or Prime, plus a Eurodollar spread (dependent upon a debt to earnings ratio within a predetermined grid). This facility replaced the Company's \$15,000 credit facility that expired on the same date. Availability under the revolving credit component is subject to meeting certain financial covenants, whereas availability under the previous facility was limited by various asset values. The lenders of the new credit facility are JP Morgan Chase Bank and Manufacturers and Traders Trust Company, with JP Morgan Chase Bank acting as the administrative agent. The Company is required to meet certain financial covenants, including a debt to earnings ratio, an EBIT (as defined) to interest expense ratio, and a current assets to total liabilities ratio.

On June 30, 2004, the Company drew down the full \$10,000 term loan. The proceeds of the term loan, to be repaid in equal monthly installments of \$167 over five years, were used for the retirement of outstanding debt and capital expenditures. From June 30, 2004 through August 1, 2004, the interest rate associated with the term loan was based on LIBOR plus a 1.25% Eurodollar spread. On July 1, 2004, the Company entered into an interest rate swap arrangement in the notional amount of \$10,000 to be effective on August 2, 2004, related to the \$10,000 term loan, in order to take advantage of historically low interest rates. The Company received a fixed rate of interest in exchange for a variable rate. The swap rate received was 3.98% for five years. The total rate of interest paid by the Company is equal to the swap rate of 3.98% plus the Eurodollar spread stipulated in the predetermined grid associated with the term loan. From August 2, 2004 to September 30, 2004, the total rate of interest associated with the outstanding portion of the \$10,000 term loan was 5.23%. On October 1, 2004, this adjusted rate increased to 5.33%, on January 1, 2005 the adjusted rate increased to 5.73%, and on April 1, 2005, the adjusted rate increased to 6.48%, the maximum amount under the current grid structure, and remains at that rate as of April 1, 2006. Derivative instruments are accounted for in accordance with SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" which requires that all derivative instruments be

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recognized in the financial statements at fair value. The fair value of this arrangement at April 1, 2006 resulted in an asset of \$123, all of which was reflected as short-term.

As of April 1, 2006, the Company had \$6,667 outstanding under the term loan component of its credit facility with its primary lending bank and nothing was outstanding under the revolver component. At April 1, 2006, the Company was not in compliance with the EBIT (as defined) to interest covenant, as amended. Subsequent to the end of the quarter, however, the banks provided the Company with a waiver of the financial covenant violation as of the end of the first quarter of 2006. (See Note 13 concerning a bank waiver for this financial covenant violation.) As a result of the uncertainty of the Company's ability to comply with the more restrictive financial covenants within the next year, the Company continued to classify all of the debt associated with this credit facility as a current liability on the Condensed Consolidated Balance Sheet as of April 1, 2006. While the revolver arrangement provides for up to \$15,000 of borrowing capacity, including outstanding letters of credit, the actual borrowing availability may be limited by the financial covenants. At April 1, 2006, the Company had \$2,200 of outstanding letters of credit related to this facility. In addition, the Company's additional borrowing capacity under the revolver component of the credit facility as of April 1, 2006 was approximately \$4,500.

While the Company believes relations with its lenders are good and has received waivers as necessary in the past, there can be no assurance that such waivers can always be obtained. In such case, the Company believes it has, in the aggregate, sufficient cash, cash generation capabilities from operations, working capital, and financing alternatives at its disposal, including but not limited to alternative borrowing arrangements and other available lenders, to fund operations in the normal course.

As of April 1, 2006, the Company's wholly-owned U.K. subsidiary, Ultralife Batteries (UK) Ltd., had approximately \$494 outstanding under its revolving credit facility with a commercial bank in the U.K. This credit facility provides the Company's U.K. operation with additional financing flexibility for its working capital needs. Any borrowings against this credit facility are collateralized with that company's outstanding accounts receivable balances. There was approximately \$280 in additional borrowing capacity under this credit facility as of April 1, 2006.

During the first three-month periods of 2006 and 2005, the Company issued 36,000 and 122,000 shares of common stock, respectively, as a result of exercises of stock options and warrants. The Company received approximately \$261 in 2006 and \$714 in 2005 in cash proceeds as a result of these transactions.

The Company continues to be optimistic about its future prospects and growth potential. The improvement in the Company's financial position in recent years has enhanced the Company's ability to acquire additional financing. The Company continually explores various sources of capital, including leasing alternatives, issuing new or refinancing existing debt, and raising equity through private or public offerings. Although it stays abreast of such financing alternatives, the Company believes it has the ability over the next 12 months to finance its operations primarily through internally generated funds, or through the use of additional financing that currently is available to the Company.

Management's plan to achieve operational profitability and reduce its negative cash flows from operations include reducing the build-up of inventory related to the production of BA-5390s and executing certain cost cutting objectives that were begun in September 2005. Additionally, the Company believes it has adequate third party financing available to fund its operations or could obtain other financing, if needed.

If the Company is unable to achieve its plans or unforeseen events occur, the Company may need to implement alternative plans. While the Company believes it could complete its original plans or alternative plans, if necessary, there can be no assurance that such alternatives would be available on acceptable terms and conditions or that the Company would be successful in its implementation of such plans.

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As described in Part II, Item 1, "Legal Proceedings", the Company is involved in certain environmental matters with respect to its facility in Newark, New York. Although the Company has reserved for expenses related to this, there can be no assurance that this will be the maximum amount. Management does not believe the ultimate resolution of this matter will have a significant adverse impact on the Company's financial condition and results of operations in the period in which it is resolved.

The Company typically offers warranties against any defects due to product malfunction or workmanship for a period up to one year from the date of purchase. The Company also offers a 10-year warranty on its 9-volt batteries that are used in ionization-type smoke detector applications. The Company provides for a reserve for this potential warranty expense, which is based on an analysis of historical warranty issues. There is no assurance that future warranty claims will be consistent with past history, and in the event the Company's experiences a significant increase in warranty claims, there is no assurance that the Company's reserves are sufficient. This could have a material adverse effect on the Company's business, financial condition and results of operations.

Outlook (in thousands of dollars)

Management expects revenues in the second quarter of 2006 to be approximately \$20,000, with upside dependent in part upon additional military orders. Management anticipates operating income will be in the range of \$500 in the second quarter, including \$300 of non-cash stock-based compensation expense.

Regarding revenue for the full year of 2006, the Company reiterates its outlook for at least \$90,000 on the base business of the Company, excluding acquisitions, with significant growth in the second half of the year related to growth in military sales, particularly BA-5390s. Growth above \$90,000 will continue to depend on a number of factors, including the pace at which the military transitions to lithium-manganese dioxide technology, and further expansion in commercial markets.

In January 2006, the Company entered into a definitive agreement to acquire all of the outstanding shares of Able New Energy Co., Ltd., an established, profitable manufacturer of lithium batteries located in Shenzhen, China, for a combination of cash, common stock and stock warrants for a total value of approximately \$4,200. In 2005, based on preliminary unaudited figures, which have been reviewed by management, Able generated approximately \$300 in operating profit on approximately \$2,300 in revenue. With more than 50 products, including a wide range of lithium-thionyl chloride and lithium-manganese dioxide batteries and coin cells, this acquisition will broaden the Company's expanding portfolio of high-energy power sources, enabling it to further penetrate large and emerging markets such as remote meter reading, RFID and other markets that will benefit from these chemistries. In addition, this acquisition will strengthen Ultralife's global presence, facilitate its entry into the rapidly growing Chinese market and improve the Company's access to lower cost raw materials. The cash portion of the purchase price is equal to \$2,500, with \$500 of the cash purchase price contingent on the achievement of certain performance milestones of the acquired business. The equity portion of the purchase price will consist of 80,000 shares of Ultralife common stock and 100,000 stock warrants, for a total equity consideration of approximately \$1,700. The Company anticipates that this acquisition will be accretive in 2006. The acquisition, which is subject to customary closing conditions and approval of the Chinese government, is currently expected to close in May 2006.

On May 1, 2006, the Company entered into a definitive agreement to acquire substantially all of the assets of McDowell Research, Limited (McDowell), a manufacturer of military communications accessories located in Waco, Texas, for a total value of approximately \$25,000. The acquisition is expected to close by the end of July 2006. In 2005, McDowell generated approximately \$3,200 in operating income, excluding non-recurring development costs of \$1,600, on approximately \$22,000 in revenue. Under the terms of the agreement, the purchase price of approximately \$25,000 will consist of

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\$5,000 in cash and a \$20,000 non-transferable convertible note to be held by the sellers. The cash portion is expected to be financed by Ultralife's primary lending banks. The \$20,000 convertible note carries a five year term and is convertible at \$15 per share into 1.33 million shares of Ultralife common stock, with a forced conversion feature at \$17.50 per share. Ultralife anticipates that this acquisition will be accretive in 2006.

As of April 1, 2006, the Company had \$6,667 outstanding under the term loan component of its credit facility with its primary lending banks and nothing was outstanding under the revolver component. On May 3, 2006, the Company's primary lending banks provided the Company with a waiver related to the violation of the EBIT (as defined) to interest financial covenant in the first quarter of 2006. As a result of the uncertainty of the Company's ability to comply with the financial covenants within the next year, the Company continues to classify all of the debt associated with this credit facility as a current liability on the Consolidated Balance Sheet as of April 1, 2006. In order to accommodate the acquisition of McDowell, the banks are working on an amendment to the credit facility that is necessary to be completed prior to the closing of this acquisition. While the Company believes relations with its lenders are good and has received waivers for non-compliance with financial covenants, as necessary in the past, there can be no assurance that such waivers can always be obtained. In such case, the Company believes it has, in the aggregate, sufficient cash, cash generation capabilities from operations, working capital, and financing alternatives at its disposal, including but not limited to alternative borrowing arrangements and other available lenders, to fund operations in the normal course.

Recent Accounting Pronouncements and Developments

In February 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 155, "Accounting for Certain Hybrid Financial Instruments." SFAS No. 155 amends SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" and SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS No. 155 also resolves issues addressed in SFAS No. 133 Implementation Issue No. D1, "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets." SFAS No. 155 eliminates the exemption from applying SFAS No. 133 to interests in securitized financial assets so that similar instruments are accounted for in the same manner regardless of the form of the instruments. SFAS No. 155 allows a preparer to elect fair value measurement at acquisition, at issuance, or when a previously recognized financial instrument is subject to a re-measurement (new basis) event, on an instrument-by-instrument basis. SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The fair value election provided for in paragraph 4(c) of SFAS No. 155 may also be applied upon adoption of SFAS No. 155 for hybrid financial instruments that had been bifurcated under paragraph 12 of SFAS No. 133 prior to the adoption of this Statement. Earlier adoption is permitted as of the beginning of an entity's fiscal year, provided the entity has not yet issued financial statements, including financial statements for any interim period for that fiscal year. Provisions of SFAS No. 155 may be applied to instruments that an entity holds at the date of adoption on an instrument-by-instrument basis. The Company is currently assessing any potential impact of adopting this pronouncement.

In March 2006, the FASB issued Statement of Financial Accounting Standards No. 156 ("SFAS" No. 156), "Accounting for Servicing of Financial Assets," an amendment of FASB Statement No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS No. 156 requires all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable, and permits for subsequent measurement using either fair value measurement with changes in fair value reflected in earnings or the amortization and impairment requirements of Statement No. 140. The subsequent measurement of separately recognized servicing assets and servicing liabilities at fair value eliminates the necessity for entities that manage the risks inherent in servicing assets and servicing liabilities with derivatives to qualify for hedge accounting treatment and eliminates the characterization of declines in fair value as impairments or direct write-

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downs. SFAS 156 is effective for an entity's first fiscal year beginning after September 15, 2006. The Company is assessing any potential impact of adopting this provision.

Critical Accounting Policies

Management exercises judgment in making important decisions pertaining to choosing and applying accounting policies and methodologies in many areas. Not only are these decisions necessary to comply with U.S. generally accepted accounting principles, but they also reflect management's view of the most appropriate manner in which to record and report the Company's overall financial performance. All accounting policies are important, and all policies described in Note 1 ("Summary of Operations and Significant Accounting Policies") in the Company's Annual Report on Form 10-K should be reviewed for a greater understanding of how the Company's financial performance is recorded and reported.

During the first three months of 2006, there were no significant changes in the manner in which the Company's significant accounting policies were applied or in which related assumptions and estimates were developed. Effective January 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment" ("FAS 123R") requiring that compensation cost relating to share-based payment transactions be recognized in the financial statements. The cost is measured at the grant date, based on the calculated fair value of the award, and is recognized as an expense over the employee's requisite service period (generally the vesting period of the equity award). The Company adopted FAS 123R using the modified prospective method and, accordingly, did not restate prior periods presented in this Form 10-Q to reflect the fair value method of recognizing compensation cost. Under the modified prospective approach, FAS 123R applies to new awards and to awards that were outstanding on January 1, 2006 that are subsequently modified, repurchased or cancelled. The Company calculates expected volatility for stock options by taking an average of historical volatility over the past 5 years and a computation of implied volatility. Prior to 2006, the computation of expected volatility was based solely on historical volatility. The computation of expected term was determined based on historical experience of similar awards, giving consideration to the contractual terms of the stock-based awards and vesting schedules. The interest rate for periods within the contractual life of the award is based on the U.S. Treasury yield in effect at the time of grant.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

(in whole dollars)

The Company is exposed to various market risks in the normal course of business, primarily interest rate risk and changes in market value of its investments and believes its exposure to these risks is minimal. The Company's investments are made in accordance with the Company's investment policy and primarily consist of commercial paper and U.S. corporate bonds. In July 2004, the Company entered into an interest rate swap arrangement in connection with the term loan component of its new credit facility. Under the swap arrangement, effective August 2, 2004, the Company received a fixed rate of interest in exchange for a variable rate. The swap rate received was 3.98% for five years and will be adjusted accordingly for a Eurodollar spread incorporated in the agreement. As of April 1, 2006, a one basis point move in the Eurodollar spread would have a \$1,000 value change. (See Note 7 in Notes to Condensed Consolidated Financial Statements for additional information.)

The Company is subject to foreign currency risk, due to fluctuations in currencies relative to the U.S. dollar. The Company monitors the relationship between the U.S. dollar and other currencies on a continuous basis and adjusts sales prices for products and services sold in these foreign currencies as appropriate to safeguard against the fluctuations in the currency effects relative to the U.S. dollar.

The Company maintains manufacturing operations in the U.S. and the U.K., and exports products to various countries. The Company purchases materials and sells its products in foreign currencies, and therefore currency fluctuations may impact the Company's pricing of products sold and materials purchased. In addition, the Company's foreign subsidiary maintains its books in local currency, which is translated into U.S. dollars for its consolidated financial statements.

Item 4. CONTROLS AND PROCEDURES

Evaluation Of Disclosure Controls And Procedures – The Company's president and chief executive officer (principal executive officer) and its vice president- finance and chief financial officer (principal financial officer) have evaluated the disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this quarterly report. Based on this evaluation, the president and chief executive officer and vice president - finance and chief financial officer concluded that the Company's disclosure controls and procedures were effective as of such date.

Changes In Internal Control Over Financial Reporting – There has been no change in the internal control over financial reporting that occurred during the fiscal quarter covered by this quarterly report that has materially affected, or is reasonably likely to materially affect, the internal control over financial reporting.

PART II OTHER INFORMATION

Item 1. Legal Proceedings (Dollars in thousands)

The Company is subject to legal proceedings and claims, which arise in the normal course of business. The Company believes that the final disposition of such matters will not have a material adverse effect on the financial position or results of operations of the Company.

In conjunction with the Company's purchase/lease of its Newark, New York facility in 1998, the Company entered into a payment-in-lieu of tax agreement, which provides the Company with real estate tax concessions upon meeting certain conditions. In connection with this agreement, a consulting firm performed a Phase I and II Environmental Site Assessment, which revealed the existence of contaminated soil and ground water around one of the buildings. The Company retained an engineering firm, which estimated that the cost of remediation should be in the range of \$230. Through April 1, 2006, total costs incurred have amounted to approximately \$100, none of which have been capitalized. In February 1998, the Company entered into an agreement with a third party which provides that the Company and this third party will retain an environmental consulting firm to conduct a supplemental Phase II investigation to verify the existence of the contaminants and further delineate the nature of the environmental concern. The third party agreed to reimburse the Company for fifty percent (50%) of the cost of correcting the environmental concern on the Newark property. The Company has fully reserved for its portion of the estimated liability. Test sampling was completed in the spring of 2001, and the engineering report was submitted to the New York State Department of Environmental Conservation (NYSDEC) for review. NYSDEC reviewed the report and, in January 2002, recommended additional testing. The Company responded by submitting a work plan to NYSDEC, which was approved in April 2002. The Company sought proposals from engineering firms to complete the remedial work contained in the work plan. A firm was selected to undertake the remediation and in December 2003 the remediation was completed, and was overseen by the NYSDEC. The report detailing the remediation project, which included the test results, was forwarded to NYSDEC and to the New York State Department of Health (NYSDOH). The NYSDEC, with input from the NYSDOH, requested that the Company perform additional sampling. A work plan for this portion of the project was written and delivered to the NYSDEC and approved. In November 2005, additional soil, sediment and surface water samples were taken from the area outlined in the work plan, as well as groundwater samples from the monitoring wells. The Company received the laboratory analysis and met with the NYSDEC in March 2006 to discuss the results. The Company's outside environmental consulting firm is preparing a final investigation report to be submitted to the NYSDEC by the end of May 2006. The environmental consulting firm previously estimated that the final cost to the Company to remediate the requested area would be approximately \$28, based on the submitted work plan. This further analysis will increase the estimated remediation costs modestly. At April 1, 2006 and December 31, 2005, the Company had \$45 and \$38, respectively, reserved for this matter.

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Item 6. Exhibits

- 10.1 Agreement on Transfer of Shares in Able New Energy Co., Limited By Ultralife Batteries, Inc. and Huang Deyong, Li Xiaochun, and Zhu Dehong dated January 25, 2006
- 10.2 First Amendment to Agreement on Transfer of Shares in Able New Energy Co., Limited By Able New Energy Co., Limited and Huang Deyong, Li Xiaochun, and Zhu Dehong
- 10.3 Agreement on Transfer of Equity Shares in Able New Energy Co., Ltd By Ultralife Batteries, Inc. and Huang Deyong, Li Xiaochun, and Zhu Dehong dated January 25, 2006
- 31.1 Section 302 Certification — CEO
- 31.2 Section 302 Certification – CFO
- 32 Section 906 Certifications

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.

ULTRALIFE BATTERIES, INC.

(Registrant)

Date: May 10, 2006

By: /s/ John D. Kavazanjian
John D. Kavazanjian
President and Chief Executive Officer

Date: May 10, 2006

By: /s/ Robert W. Fishback
Robert W. Fishback
Vice President — Finance and Chief
Financial Officer

Index to Exhibits

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- 32 Section 906 Certifications

AGREEMENT ON TRANSFER OF SHARES

IN

ABLE NEW ENERGY CO., LIMITED

BY

ULTRALIFE BATTERIES, INC.

AND

(HUANG DEYONG)

(LI XIAOCHUN)

(ZHU DEHONG)

Agreement on Transfer of Shares

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Schedule 2	The Company's Balance Sheet of December 31, 2005
Schedule 3	Escrow Agreement
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Agreement on Transfer of Shares

AGREEMENT ON TRANSFER OF SHARES

This Agreement on Transfer of Shares (this "Agreement") is made on this 25th day of January 2006 by and between:

Ultralife Batteries, Inc. (hereinafter referred to as the "PURCHASER"), a corporation organised and existing under the laws of the State of Delaware and having its principal office at 2000 Technology Parkway, Newark, New York 14513, US.

and

(Huang Deyong, hereinafter referred to as "MR.HUANG"), a Chinese citizen whose ID number is 230103670711321 and having domicile at B-7E, Huifangyuan, Xuefu Road, Nanshan District, Shenzhen, Guangdong, China;

(Li Xiaochun, hereinafter referred to as "MR.LI"), a Chinese citizen whose ID number is 110105197004075339 and having domicile at 8E, Building 2, Xiandaicheng Huating, Chuangye Road, Nanshan District, Shenzhen, Guangdong, China;

(Zhu Dehong, hereinafter referred to as "MR.ZHU"), a Chinese citizen whose ID number is 522101197204236013 and having domicile at B-7C, Qingchun Jiayuan, No. 205, Nanhai Road, Nanshan District, Shenzhen, Guangdong, China.

Mr. Huang, Mr. Li and Mr. Zhu hereinafter may be referred to collectively as the "SELLERS" or individually as the "SELLER". The Purchaser and the Sellers may be collectively referred to as the "PARTIES" or individually as a "PARTY".

PREAMBLE

WHEREAS Able HK is a private limited company incorporated in Hong Kong SAR on 9 May 2001 and has an authorised share capital of HK\$ 500,000 divided into 500,000 shares of HK\$ 1.00 each, all of which were fully paid up;

WHEREAS, the Sellers are the sole shareholders of Able HK, more specifically with Mr. Huang holding 250,000 ordinary shares of Able HK, Mr. Li holding 125,000 ordinary shares of Able HK and Mr. Zhu holding 125,000 ordinary shares of Able HK;

WHEREAS, the Sellers intend to sell and transfer the entire issued shares in Able HK and the Purchaser intends to buy and acquire such shares, and as a result of such share transfer, the Purchaser will hold all the issued shares of Able HK;

Agreement on Transfer of Shares

WHEREAS, the Company (hereinafter defined) is a PRC company active in the business of producing, marketing and selling various lithium batteries in both Chinese domestic market as well as export market and the Sellers are shareholders of the Company;

WHEREAS, on the date of this Agreement, Able HK will enter into the ETA (hereinafter defined) with the Sellers, whereby Able HK will acquire 100% equity shares of the Company, and as a result of such share transfer, Able HK will become the sole legal and beneficial owner of the entire equity shares of the Company;

NOW, THEREFORE, in consideration of the mutual covenants hereinafter set forth, the Parties hereto, intending to be legally bound hereunder, agree as follows:

ARTICLE 1

DEFINITIONS AND INTERPRETATIONS

1.1 Definitions

Unless the terms or context of this Agreement otherwise provide, the following terms shall have the meanings as set out below:

"Able HK" shall mean Able New Energy Co., Limited, a private limited company duly established and validly existing under the law of Hong Kong SAR with its registered address at 12/F, AT Tower, 180 Electric Road, North Point, Hong Kong SAR.

"Balance Sheet" shall mean the balance sheet of the Company dated December 31, 2005, a copy of which is attached as Schedule 2 hereto.

"China" and "PRC" mean the People's Republic of China, for purpose of this Agreement, excluding Hong Kong, Taiwan and Macau.

"Closing" shall mean the closing of the Transaction which shall take place on the date when the Conditions as described in Article 4.1 have been fulfilled, and the "Closing Date" or "Date of Closing" shall mean the date on which the Closing is effected as set out in Article 4.1 hereof.

"Company" shall mean the limited liability company named (Able New Energy Co., Ltd.), which is established under the PRC law with its legal address at ABLE Industrial Zone, Xintang Village, Guanlan Town, Baoan District, Shenzhen, Guangdong Province, China.

Agreement on Transfer of Shares

"Conditions" shall mean collectively all the conditions set out in Article 4.1 hereof.

"Condition Fulfilment Deadline" shall mean April 30, 2006 or such later date as the Purchaser may designate at its sole discretion.

"Employment Contract" shall mean the Employment Contract to be entered into by the Company and each of the Sellers a copy of which is attached to the ETA as Schedule 1 thereof and which will become effective as of the Closing Date.

"Encumbrance" shall mean a mortgage, charge, pledge, lien, option, restriction, right of first refusal, right of pre-emption, third-party right or interest, other encumbrance or security interest of any kind, or another type of preferential arrangement (including, without limitation, a title transfer or retention arrangement) having similar effect and any agreement or obligation to create or grant any of the aforesaid.

"Escrow Agreement" shall mean the Escrow Agreement to be entered into between the Purchaser, Mr. Huang and Arculli Fong & Ng (the "Escrow Agent") on the date of this Agreement a copy of which is attached hereto as Schedule 3.

"ETA" shall mean the Agreement on Transfer of Shares which is executed by Able HK and the Sellers on the date hereof. A copy of the ETA is attached hereto as Schedule 1.

"Execution Date" shall mean the date on which this Agreement is signed by duly authorized representatives of all the Parties. Unless otherwise agreed by the Parties, the Execution Date shall not be later than January 28, 2006.

"Hong Kong" shall mean Hong Kong Special Administrative Region.

"Net Sales" shall mean the net revenue of the Company generated from sales of the Company's products, net of any discount, rebate, commission, VAT or other sales tax.

"Purchase Price" shall mean the purchase price for the Transferred Shares that is payable by the Purchaser to the Sellers according to Article 3 hereof.

"Transaction" shall mean the transaction defined in Article 2.1 hereof.

Agreement on Transfer of Shares

"Transferred Shares" shall mean all the issued shares of Able HK, which will be transferred from the Sellers to the Purchaser under the Transaction according to the terms and conditions hereunder.

"U.S." shall mean the United States of America.

"Warranties" shall mean means collectively all the representations, warranties and undertakings set out in Article 6.1 hereof.

1.2 Interpretation

Articles and headings are inserted for the purpose of convenience and reference only and shall not affect the interpretation or construction of this Agreement. Words denoting the singular shall, where applicable, include plural and vice versa. Reference to the masculine gender shall, where applicable, include the feminine gender and vice versa.

ARTICLE 2

TRANSFER OF SHARES

2.1 Subject to the Conditions set forth in Article 4 hereof and with effect as of the Date of Closing, the Sellers hereby sell and transfer to the Purchaser and the Purchaser hereby buys and acquires from the Sellers, all of the rights, title and interests to and under the Transferred Shares as follows (the "TRANSACTION"):

- (i) Mr. Huang sells and transfers to the Purchaser 250,000 ordinary shares of Able HK;
- (ii) Mr. Li sells and transfers to the Purchaser 125,000 ordinary shares of Able HK; and
- (iii) Mr. Zhu sells and transfers to the Purchaser 125,000 ordinary shares of Able HK.

Upon the completion of the Transaction, the Purchaser will hold all issued shares of Able HK.

2.2 The Sellers represent and warrant to, and covenant with, the Purchaser that at the Sellers' own cost and expense, they will execute and do or procure to be executed and done by any other necessary party all deeds, documents, acts and things necessary and appropriate to vest the ownership of the Transferred Shares to the Purchaser as may be necessary to give full effect to this Agreement.

Agreement on Transfer of Shares

ARTICLE 3

PURCHASE PRICE AND PAYMENT

3.1 The total Purchase Price to be paid by the Purchaser for the Transferred Shares shall be the sum of USD \$1,500,000 in cash and 80,000 common stocks and 100,000 stock warrants of Ultralife. The stock warrants shall immediately vest upon the grant, have a term of five (5) years and have a strike price equal to the Purchaser's stock price at closing on the Execution Date. Of the Purchase Price, the following cash, stocks and stock warrants shall be paid and granted to each of the Sellers:

- (i) USD \$750,000 shall be paid to Mr. Huang and 40,000 common stocks and 50,000 stock warrants of Ultralife shall be granted to Mr. Huang;
- (ii) USD \$375,000 shall be paid to Mr. Li and 20,000 common stocks and 25,000 stock warrants of Ultralife shall be granted to Mr. Li; and
- (iii) USD \$375,000 shall be paid to Mr. Zhu and 20,000 common stocks and 25,000 stock warrants of Ultralife shall be granted to Mr. Zhu.

If the market price of Ultralife's common stock is below USD \$12.50 on the Closing Date, the number of common stocks granted to the Sellers shall be increased from 80,000 to a number that ensures that the total value of the common stocks is equal to USD \$1,000,000. Such increased number of common stock of Ultralife shall be granted to each of the Sellers pro rata to their shareholding ratio in Able HK at the Closing Date, and the number of common stocks granted to each of the Sellers set forth in 3.1(i), (ii) and (iii) will be changed accordingly.

3.2 The Purchaser shall pay the Purchase Price in the form of stocks and stock warrants as set out in Article 3.1 to each of the Sellers within one (1) month from the Date of Closing.

3.3 The Purchase Price in the form of USD \$1,500,000 of cash shall be deferred in accordance with the following schedule:

- (i) USD \$1,000,000 shall be payable to the Sellers pro rata to their shareholding ratio at the Closing within thirty (30) days of the Closing Date;

Agreement on Transfer of Shares

(ii) USD \$250,000 shall be payable to the Sellers pro rata to their shareholding ratio at the Closing within thirty (30) days of the date that the Net Sales of the Company exceeds USD \$5,000,000 after the Date of Closing; and

(iii) USD \$250,000 shall be payable to the Sellers pro rata to their shareholding ratio at the Closing within thirty (30) days of the date that the Net Sales of the Company exceeds USD \$10,000,000 after the Date of Closing.

3.4 Any and all sums which are payable to each of the Sellers hereunder shall be paid by the Purchaser to a bank account respectively maintained by each of the Sellers, as shall have been notified by such Seller in writing at least fourteen (14) days prior to the date of payment.

3.5 Each Seller shall be solely liable and responsible for any taxes, fees and public levies including, without limitation, profits tax, enterprise income tax, capital gains tax, value added taxes (VAT), business tax, and turnover tax, which may be levied or imposed by any tax, revenue or other government authorities in any part of the world, in connection with the sale and transfer of the corresponding portion of the Transferred Shares, or on the profit derived by such Seller from such sale and transfer. If the Purchaser is required under any applicable law or regulation to deduct or withhold tax with respect to the Purchaser Price or any part thereof payable to the Seller, the Purchaser shall be entitled to deduct the relevant amounts from the Purchase Price and to pay over the amounts deducted to the relevant tax, revenue or other government authorities, provided that the Purchaser shall deliver to the Seller official receipts or other documentary evidence showing that the amounts withheld have been paid to the relevant tax revenue or other governmental authorities, within 30 days of payment.

3.6 In the event that the Purchaser has any claim against any of the Sellers under this Agreement, and/or Able HK has any unsatisfied claim against the Sellers under the ETA, the Purchaser shall be entitled to deduct and set-off the relevant amount of any such claim from and against the portion of the Purchaser Price payable to any Seller. The Purchaser shall inform the Sellers about the grounds and amounts of the claim promptly.

ARTICLE 4

CLOSING

4.1 The Closing shall take place on the day when all the following conditions have been fulfilled:

Agreement on Transfer of Shares

- (i) All the conditions set out in Article 4.1 of the ETA have been fulfilled;
- (ii) The Purchaser has received instrument(s) of transfer in respect of the Transferred Shares duly executed respectively by or on behalf of each of the Sellers as shareholders in favour of the Purchaser;
- (iii) The Purchaser has received sold note(s) in respect of the Transferred Shares duly executed by the Sellers in a form complying with the requirements of the Stamp Duty Ordinance, Cap. 117, and a cheque payable to Hong Kong Government in respect of the stamp duty payable on such sold notes;
- (iv) The Purchaser has received the share certificates in respect of the Transferred Shares;
- (v) The Purchaser has received the board resolutions of Able HK approving the transfer of the Transferred Shares, approving the transactions contemplated under this Agreement and authorising the entering into and the execution of this Agreement and any other ancillary documents so as to give effect to the transactions contemplated hereunder, the appointment of directors nominated by the Purchaser to the board of directors of Able HK and the resignation of the directors which were nominated and/or appointed by the Sellers;
- (vi) The Purchaser has received all records, papers, documents and data (in whatever form they may exist), all Company's seal and chop(s) in the possession, custody or control of, or kept or made by or on behalf of the Sellers relating to the business and affairs of Able HK;
- (vii) All other things and such other documents as may be required in the reasonable opinion of the Purchaser in order to deliver good and marketable title of the Transferred Shares to the Purchaser, free and clear of any Encumbrance have been done and/or delivered; and
- (viii) The Sellers have signed all necessary documents and caused such board resolution(s) to be passed and taken such steps as shall be necessary to cause Able HK to:
 - (a) enter the Purchaser upon the books and shareholder register of Able HK as the holders of the Transferred Shares; and
 - (b) issue share certificates to the Purchaser.

Agreement on Transfer of Shares

- 4.2 The Sellers shall use their best endeavors to procure the fulfillment of all the Conditions specified in Article 4.1, and shall deliver to the Purchaser the originals or certified true copies of those letters, certificates, documents and other documentary evidence proving the fulfillment of the Conditions. If at any time the Seller becomes aware of a fact or circumstance that might prevent a Condition from being satisfied, it will immediately inform the Purchaser.
- 4.3 The date on which all the Conditions are or are deemed to be fulfilled shall be confirmed in writing by the Purchaser to the Sellers within seven (7) days after the date on which the originals or certified true copies of all the letters, certificates and documents provided for in Article 4.2 have actually been received by the Purchaser. The Purchaser may, to such extent as it deems fit and is legally entitled to do so, at any time waive in writing any of the Conditions set out in Article 4.1 on such terms as it may decide.
- 4.4 If any of the Conditions (which have not previously been waived by the Purchaser) have not been satisfied on or before the Condition Fulfilment Deadline, then the Purchaser may on that date, at its option (but without prejudice to any other right or remedy it may have), by notice to the Sellers:
- (i) waive the Conditions which have not been satisfied; or
 - (ii) postpone the Condition Fulfilment Deadline to a date not later than June 30, 2006; or
 - (iii) terminate this Agreement in which event the provisions of Article 9 will apply.

ARTICLE 5

NON-COMPETITION

- 5.1 After the execution of this Agreement and for a period of three (3) years following the expiry or the termination of the Employment Contract, the Sellers shall not jointly or separately, assist or have an interest in (other than a passive investment of no more than 5% of the equity of the company in which the investment is made), or enter the employment of or act as an agent, advisor or consultant for, any person, in, or enter the employment of or act as an agent, advisor or consultant for, any person, entity or joint venture which is engaged in, or will be engaged in, any activity or business which will (a) engages in production and sales of products that are same as or similar to those of the Company; (b) contract, solicit or enters in contract or agreement with the Company's employees, customers, suppliers and other business contacts; (c)

Agreement on Transfer of Shares

compete directly or indirectly with the business of the Company in any other manner.

- 5.2 Each of the Sellers acknowledges that the consideration for the above non-competition covenants has been included in the Purchase Price and upon his receipt of the portion of the Purchase Price pursuant to Article 3.3 (i) of this Agreement he shall have also received the consideration for the non-competition covenants and shall not be entitled to claim for any compensation from the Purchaser.
- 5.3 If any of the Sellers violates any of the obligations set out in this Article 5, any profits or remunerations gained by the Seller from the competition activities in violation to this Article should be forfeited to the Purchaser. In addition, for each case of violation the Seller shall be obligated to pay a penalty in the amount of USD \$10,000 to the Purchaser. If a violation is continued for more than four weeks, each four weeks of the continuation of the violation shall be deemed to constitute an independent violation.

ARTICLE 6

REPRESENTATIONS AND WARRANTIES OF THE SELLERS

- 6.1 Each of the Sellers represents and warrants that, as of the Execution Date as well as the Closing Date:
- (i) Each of the representations and warranties set out in Article 7.1 of the ETA is true, accurate and not misleading in any way;
 - (ii) Able HK is duly organised, validly existing and in good standing under the laws of Hong Kong. The Sellers have paid in the capital of Able HK of HK \$500,000 (five hundred thousand Hong Kong dollars).
 - (iii) The Sellers are the sole legal and beneficial owners of the Transferred Shares, and are entitled to sell and transfer the full legal and beneficial ownership of the Transferred Shares to the Purchaser free from all Encumbrances and with all legal and beneficial rights now and hereafter relating to the Transferred Shares.
 - (iv) There are no Encumbrances on, over or affecting any of the Transferred Shares and the assets of Able HK. There is no agreement or commitment to give or create any such Encumbrance. No claim has been made by any person to be entitled to any such Encumbrance which has not been waived in its entirety or satisfied in full.

Agreement on Transfer of Shares

- (v) Each of the Sellers has obtained all necessary consents, approvals or authorisation to execute and perform this Agreement required from any department in charge, or governmental authorities pursuant to any laws and regulations which he is subject to. Execution of this Agreement does not and will not constitute any breach or violation of any contract, agreement, corporate or regulatory documents, laws and regulations by which the Seller is bound.
- (vi) The payment of the Purchaser Price in the form of cash, stocks and stock warrants are not in breach of any Hong Kong or PRC laws. If the receipt of such payment by the Sellers is subject to any approval by any governmental authorities, each of the Sellers shall obtain all such necessary approvals. If any Seller fails to comply with all such laws that he is subject to, the Sellers agree to indemnify the Purchaser, Able HK and the Company for any resulted damages and losses.
- (vii) All information and documents in relation to Able HK that have been provided to the Purchaser for purpose of or in connection with this Agreement, including without limitation to those listed in Schedule 4, are true and accurate in all respects and are not misleading because of any omission or ambiguity or for any other reason.
- (viii) All the accounts, books, ledgers and financial and other records of Able HK are complete and accurate in all material respects and have been properly kept in accordance with the legal requirements and normal business practice, and are in the possession of Able HK or under its control, and all transactions relating to the business of Able HK have been duly and correctly recorded therein and there are no inaccuracies or discrepancies of any kind contained or reflected in such accounts, books, ledgers and financial and other records and they are sufficient to give a true and accurate view of the state of Able HK's affairs and to explain its transactions.
- (ix) The Balance Sheet as of December 31, 2005 and for the twelve-month period then ended which is attached as Schedule 2 hereto is complete and accurate in all material respects and does not contain any material misstatements or omissions, it fairly represents the financial position of the Company as of such date and the results of operations for such period, and they have been prepared in accordance with the PRC Enterprise Accounting System, and to the extent the PRC Enterprise Accounting System permits alternative applications, such system is applied on a basis consistent with past practice. There are no liabilities

Agreement on Transfer of Shares

or obligations of Company vis-a-vis any person, entity or governmental entity, whether accrued, contingent, determined or otherwise, other than those reflected in the Balance Sheet.

- (x) The assets included in the books and accounts of Able HK are the absolute property of Able HK free from any mortgage, charge, lien, bill of sale or other encumbrance and are not the subject of any leasing, hiring or hire purchase agreement or agreement for payment on deferred terms or assignment or factoring or other similar agreement and all such assets are in the possession or under the control of Able HK.
- (xi) There has been no breach by the Seller or Able HK or by any of their respective officers or employees (in their capacity as such) of any legislation or regulations affecting Able HK or its business.
- (xii) Able HK has since December 31, 2005 carried on business in the ordinary and usual course and has not entered into any contract which is onerous in nature and may affect the Purchaser's decision to purchase the Transferred Shares.
- (xiii) There has been no breach by the Seller or Able HK of any contract, agreement or covenant to which the Seller or Able HK is a party; if any dispute arises under or in connection with such contract, agreement or covenant for matters that have taken place up to the Closing Date, the Sellers agree to indemnify the Purchaser and Able HK, without delay, for all reasonable costs of settling such disputes.
- (xiv) Able HK is not engaged (whether as plaintiff, defendant or otherwise) in any litigation or arbitration, administrative or criminal or other proceeding, and no litigation or arbitration, administrative or criminal or other proceedings against Able HK is pending, threatened or expected, and there is no fact or circumstance likely to give rise to any such litigation or arbitration, administrative or criminal or other proceedings, or to any proceedings against any director, officer or employee (past or present) of Able HK in respect of any act or default for which Able HK might be vicariously liable.
- (xv) Able HK has not issued or granted, or made any commitment capable of being realised after the Execution Date to issue or grant, any guarantee, commercial paper, Encumbrance or other security to secure any current, contingent or future liability or obligation of the Seller or any third party.

Agreement on Transfer of Shares

- 6.2 Each of the Sellers acknowledges and accepts that the Purchaser is entering into this Agreement in reliance upon each of the Warranties notwithstanding any investigations which the Purchaser, its agents or advisors may have made, and jointly and severally undertake to indemnify the Purchaser and Able HK against any loss, damages, costs (including all legal costs on a solicitor and own client basis), expenses or other liabilities which the Purchaser may incur in connection with:
- (i) any of the Warranties being untrue or misleading or breached;
 - (ii) the settlement of any claim that any of the Warranties are untrue or misleading or have been breached and in which the Seller acknowledges or confirms (on a with or without liability basis) that there has been a breach of Warranties;
 - (iii) any arbitration or legal proceedings in which the Purchaser or Able HK claims that any of the Warranties are untrue or misleading or have been breached, and in which settlement is reached under which the Seller (on a with or without liability basis) acknowledges that a Warranty is untrue or misleading or has been breached, or arbitration award or judgment is given for the Purchaser or Able HK provided that if the arbitrator or court makes a ruling as to the payment of costs by the parties, then that ruling shall apply in lieu of the provisions of this Article; and
 - (iv) the enforcement and amount of any such settlement or arbitration award or judgment.
- 6.3 Each of the Warranties shall be construed as a separate Warranty and (save as expressly provided to the contrary) shall not be limited or restricted by reference to, or inference from, the terms of any other Warranty or any other terms of this Agreement.
- 6.4 Any rights to which the Purchaser may be or become entitled to by reason of any of the Warranties, and all remedies which may be available to the Purchaser in consequence of any of the Warranties being untrue or misleading or breached, shall ensure for the benefit of any subsidiary or parent or holding company of the Purchaser and, accordingly, any loss which is sustained by the Purchaser in consequence of any of the Warranties being untrue, misleading or breached, shall be deemed also to be a loss of such subsidiary or parent or holding company, and such subsidiary or parent or holding company may bring proceedings and exercise any other remedy on the footing that it has been the legal and beneficial owner of the Transferred Shares at all times since Closing.
- 6.5 Each of the Sellers hereby undertakes that he will, periodically and whenever requested, whether before or after Closing, forthwith disclose in writing to the

Agreement on Transfer of Shares

Purchaser any event, fact or circumstance which may become known to him after the date hereof and which is materially inconsistent with any of the Warranties, or which could reasonably be expected to materially affect a purchaser's valuation of the Transferred Shares or which may entitle the Purchaser to make any claim under this Agreement.

- 6.6 Any breach of any of the Warranties or indemnities made or given by the Seller hereunder occurring before Closing shall, in addition and without prejudice to any other rights or remedies available to the Purchaser, entitle the Purchaser to rescind this Agreement forthwith (provided, in the case of rescission only, that such breach is material) and/or to sue for any breach thereof on the basis set out in this Article 6.
- 6.7 The Warranties shall be deemed repeated on each day up to the Closing Date and again on Closing (by reference to the facts then subsisting).
- 6.8 No claim shall be brought by the Purchaser for breach of any of the Warranties unless (i) the breach occurs during the period of 3 years following the Closing Date, and (ii) notice of such claim specifying in reasonable detail the breach to which the claim relates, the nature of the breach and the amount claimed (where ascertainable) has been received by the relevant Sellers not later than the expiry of the period of 38 months following the Closing Date.
- 6.9 The Sellers shall only be liable with respect to any claim under the Warranties if:
- (i) the amount finally adjudicated or agreed as being payable with respect to such individual claim is in excess of USD \$1,000 or the equivalent amount thereof in any other currencies; and
 - (ii) the aggregate amount finally adjudicated or agreed as being payable with respect to all such claims referred to in paragraph (a) above is in excess of USD \$10,000 or the equivalent amount thereof in any other currencies, in which event the Seller shall be liable for the whole amount and not merely for the excess.
- 6.10 If the Sellers shall pay to the Purchaser or Able HK any amount by way of compensation or damages under a claim for breach of Warranties, and the Purchaser or Able HK subsequently recovers from a third party any amount relating to such breach or claim, the Purchaser or Able HK (as the case may be) shall repay to the Sellers such amount previously paid by them or so much thereof as does not exceed the amount recovered from the third party.
- 6.11 The provisions of Articles 6.8 to 6.10 shall not apply in the event of fraud or dishonesty on the part of any of the Sellers prior to the Closing Date.

Agreement on Transfer of Shares

- 6.12 If in respect of or in connection with any breach of any of the Warranties, any amount payable to the Purchaser or Able HK by the Sellers is subject to taxation, the Sellers shall pay such additional amounts to the Purchaser or Able HK so as to ensure that the net amount actually received by the Purchaser or Able HK is equal to the full amount payable to the Purchaser or Able HK under this Agreement.
- 6.13 If there is any breach of any of the Warranties or any provision of this Agreement, or any breach of any provision of the ETA happens before the full payment of the Purchase Price, the Purchaser may, to the fullest extent afforded by Hong Kong laws, without prejudice to any other rights that it may have, set off any loss or damage found to be suffered or incurred by it or Able HK (or otherwise agreed) in connection with any such breach or set off any claim, against the Purchase Price.

ARTICLE 7

REPRESENTATIONS AND WARRANTIES OF THE PURCHASER

- 7.1 The Purchaser represents and warrants that, as of the Execution Date as well as the Closing Date:
- (i) It is duly organised, validly existing and in good standing under the laws of the State of Delaware;
 - (ii) It has obtained the consents, approvals or authorisation to enter into this Agreement and any other ancillary documents so as to give effect to the transactions contemplated hereunder required from its shareholders and/or board of directors pursuant to its articles of association, or required by law. Conclusion of this Agreement does not constitute a breach of any agreement or law by which the Purchaser is bound.

ARTICLE 8

CONFIDENTIALITY

- 8.1 For purpose of this Article, Confidential Information shall mean all information not in the public domain (and whether or not recorded in documentary form or on computer disc) including but not limited to:
- (i) the business methods, corporate plans, management systems, finances, maturing new business opportunities or research and development projects of Able HK and/or the Company;

Agreement on Transfer of Shares

- (ii) the marketing or sales of any products or services of Able HK and/or the Company, including, without limitation, sales targets and statistics, market surveys and plans, sales techniques, price lists, contact details of customers or potential customers or any suppliers and potential suppliers to Able HK and/or the Company, the nature of their business operations, their preferences, ability to pay and all confidential aspects of their business relationship with Able HK and/or the Company; and
- (iii) any trade secrets, secret formulae, processes, inventions, designs, know-how, discoveries, technical specifications and other technical information relating to any product or service of Able HK and/or the Company.

8.2 (i) Before and after Closing, the Sellers:

- (a) may not use or disclose to any person any Confidential Information belonging to Able HK and/or the Company or otherwise relating to their business which they have obtained during their operation; and
- (b) will make every effort to prevent the use or disclosure of Confidential Information.

(ii) Article 8.2(i) does not apply to:-

- (a) disclosure of Confidential Information to a director or employee of the Purchaser or Able HK whose function requires him to have the Confidential Information;
- (b) disclosure of Confidential Information to a professional adviser for the purpose of advising the Sellers but only on terms that the provisions of Article 8 apply to the use or disclosure by such professional adviser of such Confidential Information;
- (c) Confidential Information which has become public knowledge otherwise than, directly or indirectly, through the Sellers' breach of this Article 8; or
- (d) disclosure of Confidential Information required by law or regulation (and then if and to the extent practicable only after consulting and taking into account the reasonable requirements of the Purchaser).

8.3 Each of the undertakings in this Article 8 is a separate and independent undertaking. If one or more of those undertakings is held to be void or unenforceable, the validity of the remaining undertakings will not be affected.

8.4 The Sellers agree that:-

Agreement on Transfer of Shares

- (i) the restrictions and undertakings contained in Article 8 are reasonable and necessary for the protection of the Purchaser's legitimate interests in the goodwill of Able HK and/or the Company; and
- (ii) if any such restrictions or undertakings are found to be void or voidable, but would be valid and enforceable if some part or parts of the restriction or undertaking were deleted, such restriction or undertaking will apply with such modifications as may be necessary to make it valid and enforceable.

8.5 The Parties acknowledge that since damages or an account of profits will not be an adequate remedy for a breach of the obligations in this Article 8, the Purchaser is entitled to an injunction to prevent a breach or continued breach.

ARTICLE 9

TERMINATION

9.1 In the event that Able HK is entitled to terminate the ETA pursuant to the provisions thereof, the Purchaser shall be entitled to terminate this Agreement forthwith.

9.2 If this Agreement is terminated pursuant to Articles 4.4, 6.6 and 9.1 hereof, then:

- (a) all rights and obligations of the Parties will cease immediately upon termination except that termination will not affect the then accrued rights and obligations of the Parties (including the right to damages for the breach, if any, giving rise to the termination) and any other pre-termination breach by any of the Parties;
- (b) the Parties shall, to their best efforts, coordinate to reverse the Transaction to the effect that this Agreement has never been executed by the Parties.

ARTICLE 10

BREACH OF CONTRACT

10.1 In the event of any failure by any Party to perform any of its or his material obligations hereunder, or any representations and warranties set forth herein are inaccurate, untrue, or misleading, it shall constitute a breach of this Agreement ("Breach"). Any breach of the ETA by any of the Sellers shall be deemed as a Breach to this Agreement as well. The Party in breach of this Agreement shall fully indemnify the non-breaching Party for any and all damages and losses suffered by the non-breaching Party as a result of the Breach.

Agreement on Transfer of Shares

- 10.2 The Party in breach shall have thirty (30) days within which to cure any Breach upon written notice of the non-breaching Party indicating the Breach. If a cure is not effected within the above time period, then the non-breaching Party shall be entitled to be compensated for all damages and losses related to and/or resulting from such breach, provided however that the non-breaching Party shall not be entitled to receive punitive or non-consequential damages.
- 10.3 In case of any breach of this Agreement by any of the Sellers, and/or any breach of the ETA by any of the Sellers of which damages and losses suffered by Able HK has not been compensated pursuant to the provisions thereof, the Purchaser shall be entitled to deduct and set-off its damages and losses and/or those of Able HK from and against the Purchaser Price. If the unpaid part of Purchase Price is not enough to cover such damages and losses, the Seller shall further compensate the Purchaser for the remaining amount of damages and losses.

ARTICLE 11

REIMBURSEMENT OF APPROVED EXPENSES

- 11.1 The Purchaser agrees to reimburse the Sellers for certain out-of-pocket expenses incurred by the Sellers in connection with the Transaction under the ETA and the Transaction under this Agreement provided that such expenses have been approved by the Purchaser in writing and in advance ("Approved Expenses"). For purpose of reimbursing the Sellers of the Approved Expenses, the Purchaser, Mr. Huang and the Escrow Agent shall enter into the Escrow Agreement on the date of this Agreement under which the Purchaser shall deposit cash with an amount of USD \$105,000 (the "Escrow Moneys") into a trust account opened in the name of the Escrow Agent (the "Escrow Account").
- 11.2 In each case where the Purchaser approves the said expenses incurred by the Sellers, the Purchaser and Mr. Huang shall issue a joint instruction to the Escrow Agent instructing the Escrow Agent to release a sum of money equal to the amount of the Approved Expenses to Mr. Huang. The Sellers hereby acknowledge and agree that upon receipt of the money by Mr. Huang, the Sellers shall be deemed to have been reimbursed for the Approved Expenses.
- 11.3 In the event that the Escrow Moneys are insufficient to cover the Approved Expenses, the Purchaser shall inject more funds to the Escrow Account to the extent necessary to reimburse the Sellers for the Approved Expenses.

Agreement on Transfer of Shares

- 11.4 In the event that the Purchaser breaches this Agreement, the Purchaser and Mr. Huang shall issue a joint instruction to the Escrow Agent instructing the Escrow Agent to release the remainder of the Escrow Money to Mr. Huang.
- 11.5 In the Event that the Sellers breaches this Agreement: (i) Mr. Huang and the Purchaser shall issue a joint instruction to the Escrow Agent instructing the Escrow Agent to release the remainder of the Escrow Moneys to the Purchaser; and (ii) the Sellers shall refund the Purchaser for any reimbursement for the Approved Expenses that Mr. Huang has received from the Escrow Agent pursuant to this Article.
- 11.6 In the event that the Closing does not take place before the Condition Fulfilment Deadline without the fault of any Party: (i) Mr. Huang and the Purchaser shall issue a joint instruction to the Escrow Agent instructing the Escrow Agent to release the remainder of the Escrow Moneys to the Purchaser; (ii) Mr. Huang shall be entitled to keep the reimbursement for the Approved Expenses that Mr. Huang has received from the Escrow Agent pursuant to this Article by the Condition Fulfilment Deadline.
- 11.7 On May 1, 2006, if there is any money in the Escrow Account, the Parties agree that the Escrow Agent shall be entitled to transfer the remainder of the Escrow Moneys back to the Purchaser.

ARTICLE 12

SETTLEMENT OF DISPUTES

- 12.1 Any dispute, controversy or claim arising out of or relating to this Agreement, or the breach, termination or invalidity of this Agreement, shall be settled by arbitration in accordance with the UNCITRAL Arbitration Rules which are in force at the relevant time (and as the same may be amended by the remainder of this provision). The place of arbitration shall be in Hong Kong at the Hong Kong International Arbitration Centre. The Purchaser shall be entitled to appoint one arbitrator, the Sellers shall be jointly entitled to appoint one arbitrator, and the third arbitrator shall be appointed by Hong Kong International Arbitration Centre and serve as the chairman of the arbitration panel. The language to be used in such arbitration proceedings shall be English.
- 12.2 The arbitral award shall be final and binding on all the Parties (regardless of whether they are parties to the arbitration proceedings or not), and may be enforced by any court or judicial authority having competent jurisdiction over the party or its assets against whom the arbitral award is to be enforced.

Agreement on Transfer of Shares

12.3 Upon and after the submission of any dispute to arbitration, the Parties shall continue to exercise their remaining respective rights, and fulfil their remaining respective obligations under this Agreement, except insofar as the same may relate directly to the matters in dispute.

ARTICLE 13

MISCELLANEOUS

13.1 This Agreement shall become effective when it has been signed by authorised representatives of all the Parties.

13.2 This Agreement and the rights of the Parties hereunder shall be construed and interpreted in accordance with the laws of Hong Kong. If there are no relevant Hong Kong laws, then standard international commercial practice shall apply.

13.3 Each of the Sellers shall be jointly and severally liable for any duties and responsibilities of the Sellers hereunder, including the representations and warranties made by the Sellers. In case of breach of any provisions of the Agreement, or any of the Sellers' representations and warranties is found to be mistake or inaccurate, the Purchaser may claim against any and all of the Sellers at its sole discretion.

13.4 Except as otherwise provided for in Article 11 of this Agreement, each Party shall be responsible for the costs incurred by itself during or in connection with the drafting, negotiating and execution of this Agreement including costs for its legal and financial advisors, the costs and expenses incurred for conducting asset valuation, obtaining approvals, permits that it is required to obtain.

13.5 This Agreement supersedes all and any previous agreements or arrangements between the Parties relating to the sale and purchase of the Transferred Shares, and no future variation shall be effective unless made in writing and signed by each of the Parties.

13.6 If at any time any provision of this Agreement is or become illegal, invalid or unenforceable in any respect, the remaining provision hereof shall in no way be affected or impaired thereby.

13.7 The attached schedules shall form an integral part of this Agreement. This Agreement constitutes the entire agreement between the Parties. There are not and shall be deemed not to be any verbal statements or undertakings between the Parties.

Agreement on Transfer of Shares

13.8 Except for any agreement made by the Parties in writing to the contrary, no failure or delay to exercise any right, power, priority or remedy under this Agreement will be deemed as waiver of such right, power, priority or remedy. Nor will any single or partial exercise of any right, power, priority or remedy preclude any other or further exercise of that or any other right, power, priority or remedy.

13.9 This Agreement is signed in six (6) originals and each Party shall hold at least one (1) original. This Agreement is written in English and Chinese language and both language versions shall be equally valid.

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Agreement on Transfer of Shares

IN WITNESS WHEREOF, each Party hereto has caused this Agreement to be executed by its authorised representatives:

Shenzhen, Guangdong Province, January 25, 2006

By: ULTRALIFE BATTERIES, INC.

/s/ John D. Kavazanjian

Authorized Representative:

By: (HUANG DEYONG)

/s/ Huang Deyong

By: (LI XIAOCHUN)

/s/ Li Xiaochun

By: (ZHU DEHONG)

/s/ Zhu Dehong

FIRST AMENDMENT TO
AGREEMENT ON TRANSFER OF SHARES
IN
ABLE NEW ENERGY CO., LIMITED
BY
ULTRALIFE BATTERIES, INC.
AND
(HUANG DEYONG)
(LI XIAOCHUN)
(ZHU DEHONG)

First Amendment to the Agreement on Transfer of Shares

FIRST AMENDMENT TO THE AGREEMENT ON TRANSFER OF SHARES

This First Amendment to the Agreement on Transfer of Shares (this "Amendment") is made on this ____ day of _____ 2006 by and between:

ULTRALIFE BATTERIES, INC. (hereinafter referred to as the "PURCHASER"), a corporation organised and existing under the laws of the State of Delaware and having its principal office at 2000 Technology Parkway, Newark, New York 14513, US.

and

(Huang Deyong, hereinafter referred to as "MR.HUANG"), a Chinese citizen whose ID number is 230103670711321 and having domicile at B-7E, Huifangyuan, Xuefu Road, Nanshan District, Shenzhen, Guangdong, China;

(Li Xiaochun, hereinafter referred to as "MR.LI"), a Chinese citizen whose ID number is 110105197004075339 and having domicile at 8E, Building 2, Xiandaicheng Huating, Chuangye Road, Nanshan District, Shenzhen, Guangdong, China;

(Zhu Dehong, hereinafter referred to as "MR.ZHU"), a Chinese citizen whose ID number is 522101197204236013 and having domicile at B-7C, Qingchun Jiayuan, No. 205, Nanhai Road, Nanshan District, Shenzhen, Guangdong, China.

Mr. Huang, Mr. Li and Mr. Zhu hereinafter may be referred to collectively as the "SELLERS" or individually as the "SELLER". The Purchaser and the Sellers may be collectively referred to as the "PARTIES" or individually as a "PARTY".

PREAMBLE

WHEREAS on January 25th 2006, the Parties entered into the Agreement on Transfer of Shares (hereinafter referred to as the "STA") for the transfer of the entire issued shares in Able New Energy Co., Limited;

WHEREAS the Parties agree that certain provisions of the STA requires for clarification and amendment and intend to amend the STA pursuant to the terms and conditions of this Amendment;

ACCORDINGLY the Parties hereby agree to this Amendment which shall become effective as of the date hereof. Subject to the amendments expressly set out herein, all terms and conditions of the STA shall continue to be valid and effective.

First Amendment to the Agreement on Transfer of Shares

ARTICLE 1

Unless the terms or context of this Amendment otherwise provide, the terms herein shall bear the same meaning as defined in the STA.

ARTICLE 2

The following article shall be inserted after Article 11.6 of the STA and become Article 11.7 thereof, with the original Article 11.7 accordingly numbered as Article 11.8.

"11.7 In the event that the Closing takes place pursuant to Article 4.1 hereof by the Condition Fulfilment Deadline, except for the reimbursement for the Approved Expenses that have been waived in writing by the Purchaser for the reason that such Approved Expenses are for its benefit and convenience, the total amount of the reimbursement for the Approved Expenses that the Sellers have received from the Escrow Agent pursuant to this Article by the Date of Closing shall be credited to the part of Purchase Price payable to the Sellers pursuant to Article 3.3(i) hereof. Accordingly, such reduced sum of Purchase Price shall be payable to the Sellers pro rata to their shareholding ratio at the Closing within thirty (30) days of the Closing Date."

IN WITNESS WHEREOF, each Party hereto has caused this First Amendment to the Agreement on Transfer of Shares to be executed by its authorised representatives:

Shenzhen, Guangdong Province, [date], 2006

By: ULTRALIFE BATTERIES, INC.

/s/ Philip M. Meek

Authorized Representative:

By: (HUANG DEYONG)

/s/ Huang Deyong

First Amendment to the Agreement on Transfer of Shares

By: (LI XIAOCHUN)

/s/ Li Xiaochun

By: (ZHU DEHONG)

/s/ Zhu Dehong

AGREEMENT ON TRANSFER OF EQUITY SHARES

IN

(ABLE NEW ENERGY CO., LTD.)

BY

(ABLE NEW ENERGY CO., LIMITED)

AND

(HUANG DEYONG)

(LI XIAOCHUN)

(ZHU DEHONG)

Agreement on Transfer of Equity Shares

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Agreement on Transfer of Equity Shares

AGREEMENT ON TRANSFER OF EQUITY SHARES

This Agreement on Transfer of Equity Shares (this "Agreement") is made in Shenzhen, Guangdong Province, People's Republic of China ("China") on this 25th day of January 2006 by and between:

(Able New Energy Co., Limited, hereinafter referred to as "PURCHASER"), a company duly established and validly existing under the law of Hong Kong SAR with its registered address at 12/F, AT Tower, 180 Electric Road, North Point, Hong Kong SAR.

and

(Huang Deyong, hereinafter referred to as "MR.HUANG"), a Chinese citizen whose ID number is 230103670711321 and having domicile at B-7E, Huifangyuan, Xuefu Road, Nanshan District, Shenzhen, Guangdong, China;

(Li Xiaochun, hereinafter referred to as "MR.LI"), a Chinese citizen whose ID number is 110105197004075339 and having domicile at 8E, Building 2, Xiandaicheng Huating, Chuangye Road, Nanshan District, Shenzhen, Guangdong, China;

(Zhu Dehong, hereinafter referred to as "MR.ZHU"), a Chinese citizen whose ID number is 522101197204236013 and having domicile at B-7C, Qingchun Jiayuan, No. 205, Nanhai Road, Nanshan District, Shenzhen, Guangdong, China.

Mr. Huang, Mr. Li and Mr. Zhu hereinafter may be referred to collectively as the "SELLERS" or individually as the "SELLER". The Purchaser and the Sellers may be collectively referred to as the "PARTIES" or individually as a "PARTY".

PREAMBLE

WHEREAS, the Sellers are the sole shareholders of the Company (hereinafter defined), more specifically with Mr. Huang holding 50% equity shares of the Company, Mr. Li holding 25% equity shares of the Company and Mr. Zhu holding the remaining 25% equity shares of the Company;

WHEREAS, the Company is active in the business of producing, marketing and selling various lithium batteries in both Chinese domestic market as well as export market;

WHEREAS, the Sellers intend to sell and transfer the entire equity interests in the Company and the Purchaser intends to buy and acquire such interests.

Agreement on Transfer of Equity Shares

NOW, THEREFORE, in consideration of the mutual covenants hereinafter set forth, the Parties hereto, intending to be legally bound hereunder, agree as follows:

ARTICLE 1

DEFINITIONS AND INTERPRETATIONS

1.1 Definitions

Unless the terms or context of this Agreement otherwise provide, the following terms shall have the meanings as set out below:

"Able GmbH" shall mean a company established under the law of Germany with its legal address at Hannenstieg 22, 22175, Hamburg, Germany which is wholly owned by Mr. Li.

"Amended Articles of Association" shall mean the amended articles of association of the Company, which will become effective as of the Effectiveness Date.

"Business" shall mean the current business of manufacturing and sales of lithium batteries by the Company.

"Business License" shall mean the revised business license of the Company which will be issued by the SZAIC following the Effectiveness Date and meeting the requirements set out in Article 4.1 (ii).

"China" and "PRC" mean the People's Republic of China, for purpose of this Agreement, excluding Hong Kong, Taiwan and Macau.

"Closing" shall mean the closing of the Transaction contemplated hereunder as described in Article 4.1, and the "Closing Date" or "Date of Closing" shall mean the date on which the Closing is effected as set out in Article 4.1 hereof.

"Company" shall mean the limited liability company named (Able New Energy Co., Ltd.), with its legal address at ABLE Industrial Zone, Xintang Village, Guanlan Town, Baoan District, Shenzhen, Guangdong Province, China.

"Conditions" shall mean collectively all the conditions set out in Article 4.1.

"Condition Fulfilment Deadline" shall mean April 30, 2006 or such later date as the Purchaser may designate at its sole discretion.

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"Effectiveness Date" shall mean the date on which this Agreement becomes legally effective pursuant to Article 9.1 hereof.

"Employment Contract" shall mean the Employment Contract to be entered into by the Company and each of the Key Employees a copy of which is attached hereto as Schedule 1 and which will become effective as of the Closing Date.

"Encumbrance" shall mean a mortgage, charge, pledge, lien, option, restriction, right of first refusal, right of pre-emption, third-party right or interest, other encumbrance or security interest of any kind, or another type of preferential arrangement (including, without limitation, a title transfer or retention arrangement) having similar effect and any agreement or obligation to create or grant any of the aforesaid.

"Examination and Approval Authority" shall mean the Bureau of Trade and Industry of Shenzhen Municipality or any other Chinese governmental authority which is competent to approve this Agreement, the Transaction contemplated hereunder and the Amended Articles of Association according to PRC laws and regulations.

"Execution Date" shall mean the date on which this Agreement is signed by duly authorized representatives of all the Parties. Unless otherwise agreed by the Parties, the Execution Date shall not be later than January 28, 2006.

"Key Employees" shall mean Mr. Huang, Mr. Li and Mr. Zhu.

"Landlord" shall mean the owner of the Current Premises or the Previous Premises, as the case may be.

"Net Sales" shall mean the net revenue of the Company generated from sales of its products, net of any discount, rebate, commission, VAT or other sales tax.

"New Premises" shall mean the premises located at Shanjiankeng, Xintang Town, Dashuikeng, Guanlan County, Bao'an District, Shenzhen, where the Company will relocate or has relocated from the Previous Premises for operation of the Business.

"Previous Premises" shall mean the premises located at Block 4, Foreign Trade Industrial Zone, Guan Lan Town, Bao'An District, Shenzhen, which was previously occupied and used by the Company for the Business.

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"Purchase Price" shall mean the purchase price for the Transferred Shares that is payable by the Purchaser to the Sellers according to Article 3 hereof.

"SAB" shall mean (Shenzhen Able Battery Co., Ltd.(pound)(C), a limited liability company established and existing under the law of PRC of which Mr. Huang is a majority shareholder.

"SZAIC" shall mean the Shenzhen Administration for Industry and Commerce and/or a local branch thereof, as appropriate to the context.

"Trademark" shall mean the trademark (ABLE' LOGO) which is registered under the name of SAB and will be legally transferred to the Company pursuant to a trademark transfer agreement to be entered into by SAB and the Company.

"Transferred Shares" shall mean the 100% equity shares in the Company, which will be transferred from the Sellers to the Purchaser under the Transaction according to the terms and conditions hereunder.

"Transaction" shall mean the transaction defined in Article 2.1 hereof.

"U.S." shall mean the United States of America.

"Warranties" shall mean collectively all the representations, warranties and undertakings set out in Article 7.1 hereof.

1.2 Interpretation

Articles and headings are inserted for the purpose of convenience and reference only and shall not affect the interpretation or construction of this Agreement. Words denoting the singular shall, where applicable, include plural and vice versa. Reference to the masculine gender shall, where applicable, include the feminine gender and vice versa.

ARTICLE 2

TRANSFER OF SHARES

2.1 Subject to the Conditions set forth in Article 4 hereof and with effect as of the Date of Closing, the Sellers hereby sell and transfer to the Purchaser and the Purchaser hereby buys and acquires from the Sellers, all of the rights, title and interests to and under the Transferred Shares as follows (the "TRANSACTION"):

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- (i) Mr. Huang sells and transfers to the Purchaser 50% equity interests of the Company;
- (ii) Mr. Li sells and transfers to the Purchaser 25% equity interests of the Company; and
- (iii) Mr. Zhu sells and transfers to the Purchaser 25% equity interests of the Company.

Upon the completion of the Transaction, the Company will become 100% owned by the Purchaser and will be converted into a wholly foreign owned enterprise (WFOE).

- 2.2 The Sellers represent and warrant to, and covenant with, the Purchaser that at the Sellers' own cost and expense, they will execute and do or procure to be executed and done by any other necessary party all deeds, documents, acts and things necessary and appropriate to vest the ownership of the Transferred Shares to the Purchaser as may be necessary to give full effect to this Agreement.

ARTICLE 3

PURCHASE PRICE AND PAYMENT

- 3.1 The total Purchase Price to be paid by the Purchaser for the Transferred Shares shall be the sum of USD \$1,000,000. Of the Purchase Price, the following sum shall be paid to each of the Sellers:
- (i) USD \$500,000 shall be paid to Mr. Huang;
 - (ii) USD \$250,000 shall be paid to Mr. Li; and
 - (iii) USD \$250,000 shall be paid to Mr. Zhu.
- 3.2 The Purchaser shall make payment of the Purchase Price to each of the Sellers as set out in Article 3.1 within one (1) month from the Date of Closing.
- 3.3 Any and all sums which are payable to each of the Sellers hereunder shall be paid by the Purchaser to a RMB bank account maintained by the Seller respectively in China, as shall have been notified by such Seller in writing at least fourteen (14) days prior to the date of payment.
- 3.4 Each Seller shall be solely liable and responsible for any taxes, fees and public levies including, without limitation, profits tax, enterprise income tax, capital gains tax, value added taxes (VAT), business tax, and turnover tax, which may be levied or imposed by any tax, revenue or other government authorities in any part of the world, in connection with the sale and transfer of the corresponding portion of the Transferred Shares, or on the profit derived by such Seller from such sale

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and transfer. If the Purchaser is required under any applicable law or regulation to deduct or withhold tax with respect to the Purchaser Price or any part thereof payable to the Seller, the Purchaser shall be entitled to deduct the relevant amounts from the Purchase Price and to pay over the amounts deducted to the relevant tax, revenue or other government authorities, provided that the Purchaser shall deliver to the Seller official receipts or other documentary evidence showing that the amounts withheld have been paid to the relevant tax revenue or other governmental authorities, within 30 days of payment.

- 3.5 In the event that the Purchaser has any claim against any of the Sellers under this Agreement, it shall be entitled to deduct and set-off the relevant amount of any such claim from and against the portion of the Purchaser Price payable to any Seller. The Purchaser shall inform the Sellers about the grounds and amounts of the claim promptly.

ARTICLE 4

CLOSING

- 4.1 The Closing shall take place on the day when all the following conditions have been fulfilled:

- (i) All necessary governmental approvals on the Transaction have been properly issued, including but not limited to the following:
 - (a) Written approval of this Agreement and the Transaction contemplated hereunder by the Examination and Approval Authority;
 - (b) Written approval of the Amended Articles of Association by the Examination and Approval Authority.
- (ii) The Business License of the Company has been issued meeting the following requirements:
 - (a) The legal form of Company has been changed to a wholly foreign owned enterprise (WFOE) with the Purchaser being the 100% owner of the Company;
 - (b) The legal representative of the Company has been changed to a nominee of the Purchaser.

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- (c) The operation term of the Company shall be not less than thirty (30) years commencing from the date of the issuance of the Business License.
- (iii) The Company's Board of Directors including the Chairman, Executive Director and Directors, the Supervisory Committee, and the General Manager which were nominated and/or appointed by the Sellers have resigned or been removed; and the new Board of Directors and new General Manager have been appointed by the Purchaser, such appointment having been approved by the Examination and Approval Authority and registered with the SZAIC accordingly;
- (iv) The Company has received all consents and approvals from third parties as may be necessary or as required by the relevant agreement or contracts to which the Company is a party in connection with the proposed change in the shareholding structure of the Company so as to ensure that the Company maintains on the same terms all its existing contractual and other rights after the Closing;
- (v) Authorized representatives of the Purchaser have taken over from the Sellers and the Company all the originals of the Company's business license, other certificates, licenses, permits, legal and financial documents as well as all the company stamps and chops.
- (vi) No material change has occurred in the Business which would or might, in the reasonable opinion of the Purchaser, materially and adversely affect the carrying out of the post-transaction Business by the Purchaser and/or the Company after the Closing;
- (vii) Any lease agreement between the Company or its shareholder on the one hand and the Landlord on the other hand for the Previous Premises has been properly terminated, and a written termination agreement has been entered to the satisfaction of the Purchaser;
- (viii) A new lease agreement for the New Premises has been entered into between the Company and the Landlord with terms and conditions satisfactory to the Purchaser, and properly registered with competent real property authority in the PRC;
- (ix) The following agreements have been properly terminated by the parties thereto and a written termination agreement has been entered into for each of the said agreements to the satisfaction of the Purchaser:
 - (a) The Exclusive Distributorship Agreement between the Company and ProBatt GmbH, a German company, on February 21, 2005;

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- (b) The Partnership Contract between the Company and Europa, a French company, on May 24, 2005;
- (c) The Sales Representative Agreement between the Company and Electronic Technology Sales, a US Company, on July 7, 2005.

- (x) Each of the Key Employees has entered into the Employment Contract with the Company.
- (xi) Able GmbH has changed its company name by removing the word "Able" without replacing it by any similar word and expression; a non-compete covenant shall have been duly executed by all the Sellers and Able GmbH in the form approved by the Purchaser, whereby they undertake to refrain from using the trade name "Able" in its business and from competing directly or indirectly with the Business;
- (xii) The Company has obtained all necessary approvals and permits with respect to environmental protection and safety production which are required for operation of the Business on the New Premises from the competent Chinese governmental authorities according to the national and local laws, rules and regulations;
- (x) A trademark transfer agreement has been executed by SAB to transfer the Trademark to the Company and an exclusive license is granted to the Company for the use of the Trademark before such transfer is legally effective.

4.2 The Sellers shall use their best endeavors to procure the fulfillment of all the Conditions specified in Article 4.1, and shall deliver to the Purchaser the originals or certified true copies of those letters, certificates, documents and other documentary evidence proving the fulfillment of the Conditions. If at any time either the Seller becomes aware of a fact or circumstance that might prevent a Condition from being satisfied, it will immediately inform the Purchaser.

4.3 The date on which all the Conditions are or are deemed to be fulfilled shall be confirmed in writing by the Purchaser to the Sellers within seven (7) days after the date on which the originals or certified true copies of all the letters, certificates and documents provided for in Article 4.2 have actually been received by the Purchaser. The Purchaser may, to such extent as it deems fit and is legally entitled to do so, at any time waive in writing any of the Conditions set out in Article 4.1 on such terms as it may decide.

4.4 If any of the Conditions (which have not previously been waived by the Purchaser) have not been satisfied on or before the Condition Fulfillment

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Deadline, then the Purchaser may on that date, at its option (but without prejudice to any other right or remedy it may have), by notice to the Sellers:

- (i) waive the Conditions which have not been satisfied; or
- (ii) postpone the Condition Fulfilment Deadline to a date not later than June 30, 2006; or
- (iii) terminate this Agreement in which event the provisions of Article 11 will apply.

ARTICLE 5

NON-COMPETITION

- 5.1 After the execution of this Agreement and for a period of three (3) years following the expiry or the termination of the Employment Contract, the Sellers shall not jointly or separately, assist or have an interest in (other than a passive investment of no more than 5% of the equity of the company in which the investment is made), or enter the employment of or act as an agent, advisor or consultant for, any person, in, or enter the employment of or act as an agent, advisor or consultant for, any person, entity or joint venture which is engaged in, or will be engaged in, any activity or business which will (a) engages in production and sales of products that are same as or similar to those of the Company; (b) contract, solicit or enters in contract or agreement with the Company's employees, customers, suppliers and other business contacts; (c) compete directly or indirectly with the business of the Company in any other manner.
- 5.2 Each of the Sellers acknowledges that the consideration for the above non-competition covenants has been included in the Purchase Price and upon his receipt of the Purchase Price pursuant to this Agreement he shall have also received the consideration for the non-competition covenants and shall not be entitled to claim for any compensation from the Purchaser. Nevertheless, the Parties agree that, in the event that the Employment Contract with any of the Sellers is early terminated by the Company prior to its expiry without the fault of such Seller, the Purchaser shall pay to such Seller extra compensation in the amount of the monthly salary of such Seller multiply by nine.
- 5.3 If any of the Sellers violates any of the obligations set out in this Article 5, any profits or remunerations gained by the Seller from the competition activities in violation to this Article should be forfeited to the Purchaser. In addition, for each case of violation the Seller shall be obligated to pay a penalty in the amount of US\$ 10,000 to the Purchaser. If a violation is continued for more than four

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weeks, each four weeks of the continuation of the violation shall be deemed to constitute an independent violation.

ARTICLE 6

CONDUCT OF BUSINESS AFTER SIGNING

- 6.1 During the period between the Execution Date and the Closing Date ("Transitional Period"), the Purchaser shall have the right to send its representative ("Purchaser's Representative") to work on secondment at the Company and to direct the management and operations of the Company. The Purchaser's Representative shall have full access to financial, operation and other information of the Company. All salary and benefit costs of the Purchaser's Representative will be borne by the Purchaser.
- 6.2 The Sellers undertake that during the Transitional Period:
- (i) The Purchaser shall be provided with unlimited access to the financial documents and information of the Company;
 - (ii) The Company shall conduct their activities in the ordinary and usual course of business and consistent with their past customs and practices. Without the Purchaser's prior written consent they shall refrain from actions falling outside of their ordinary course of business.
 - (iii) The Company shall refrain from obtaining any loan, credit or incurring liabilities of any sort which is higher than RMB 100,000 (One Hundred thousand Renminbi) without prior written consent of the Purchaser;
 - (iv) The Company shall refrain from the disposal of its assets and properties or create any pledge, mortgage or encumbrance over such assets and properties;
 - (v) The Company shall refrain from allotting or issuing any shares or any loan capital or securities or other rights convertible into shares or loan capital or distributing any profits or dividends.
- 6.3 In the event that any Seller or the Company failed to comply with the provisions under above (i) ~ (v), the Purchaser is entitled to: i) immediately terminate this Agreement without notice; in such case the Purchaser is under no obligation to make any payment; or ii) the Purchaser may deduct the losses or damages that is suffered by the Company or the Purchaser due to the breach from the Purchase Price provided herein.

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- 6.4 The Sellers undertake to immediately take actions to liquidate, dissolve and deregister SAB after the signing of this Agreement. The legal procedures for dissolution of SAB shall be completed latest in six (6) months after the Execution Date.
- 6.5 The Sellers undertake to go through relevant PRC regulatory procedure to obtain the licenses and permits required for the use of any special equipment currently used by the Company such as the X-ray equipment immediately after the signing of this Agreement. Such license and permits shall be obtained within one month after the Date of Closing.

ARTICLE 7

REPRESENTATIONS AND WARRANTIES OF THE SELLER

- 7.1 Each of the Sellers represents and warrants that, as of the Effectiveness Date as well as the Closing Date:
- (i) The Company is duly organised, validly existing and in good standing under the laws of China. The Sellers have paid in the registered capital of the Company of RMB 1,000,000 (one million Renminbi).
 - (ii) The Sellers are the sole legal and beneficial owners of the Transferred Shares, and are entitled to sell and transfer the full legal and beneficial ownership of the Transferred Shares to the Purchaser free from all Encumbrances and with all legal and beneficial rights now and hereafter relating to the Transferred Shares.
 - (iii) There are no Encumbrances on, over or affecting any of the Transferred Shares and the assets of the Company. There is no agreement or commitment to give or create any such Encumbrance. No claim has been made by any person to be entitled to any such Encumbrance which has not been waived in its entirety or satisfied in full.
 - (iv) Each of the Sellers has obtained all necessary consents, approvals or authorisation to execute and perform this Agreement required from any department in charge, or governmental authorities pursuant to any laws and regulations which he is subject to. Execution of this Agreement does not and will not constitute any breach or violation of any contract, agreement, corporate or regulatory documents, laws and regulations by which the Seller is bound.

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- (v) All licences, consents and other permissions and approvals required for carrying out the Business of the Company have been properly granted and are valid and in full force and effect; and the Company is not in default and has not received notice that it is in default with respect to the terms of any such licence, consent, permission or approval, or that any such licence, consent, permission or approval is likely to be revoked or which constitutes grounds for such revocation.
- (vi) All information and documents in relation to the Company that have been provided to the Purchaser for purpose of or in connection with this Agreement, including without limitation to those listed in Schedule 2, are true and accurate in all respects and are not misleading because of any omission or ambiguity or for any other reason.
- (vii) All the accounts, books, ledgers and financial and other records of the Company are complete and accurate in all material aspects and have been properly kept in accordance with the legal requirements and normal business practice, and are in the possession of the Company or under its control, and all transactions relating to the Business have been duly and correctly recorded therein and there are no inaccuracies or discrepancies of any kind contained or reflected in such accounts, books, ledgers and financial and other records and they are sufficient to give a true and accurate view of the state of the Company's affairs and to explain its transactions.
- (viii) The assets included in the books and accounts of the Company are the absolute property of the Company free from any mortgage, charge, lien, bill of sale or other encumbrance and are not the subject of any leasing, hiring or hire purchase agreement or agreement for payment on deferred terms or assignment or factoring or other similar agreement and all such assets are in the possession or under the control of the Company.
- (ix) As of the Date of Closing, total current assets of the Company minus total liabilities (including but not limited to payables and outstanding loans) are equal to at least RMB500,000.
- (x) There has been no breach by the Seller or the Company or by any of their respective officers or employees (in their capacity as such) of any legislation or regulations affecting the Company or its business.
- (xi) There has been no breach by the Seller or the Company of any contract, agreement or covenant to which the Seller or the Company is a party; if any dispute arises under or in connection with such contract, agreement or

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covenant for matters that have taken place up to the Closing Date, the Sellers agree to indemnify the Purchaser and the Company, without delay, for all reasonable costs of settling such disputes.

- (xii) The Company has since December 31, 2005 carried on business in the ordinary and usual course and has not entered into any contract which is onerous in nature and may affect the Purchaser's decision to purchase the Transferred Shares.
- (xiii) Unless otherwise disclosed to the Purchaser in writing, the Company is not engaged (whether as plaintiff, defendant or otherwise) in any litigation or arbitration, administrative or criminal or other proceeding, and no litigation or arbitration, administrative or criminal or other proceedings against the Company is pending, threatened or expected, and there is no fact or circumstance likely to give rise to any such litigation or arbitration, administrative or criminal or other proceedings, or to any proceedings against any director, officer or employee (past or present) of the Company in respect of any act or default for which the Company might be vicariously liable.
- (xiv) The Company have not issued or granted, or made any commitment capable of being realised after the Execution Date to issue or grant, any guarantee, commercial paper, Encumbrance or other security to secure any current, contingent or future liability or obligation of the Seller or any third party.
- (xv) The Company has been in strict compliance with all the requirements under Chinese law with respect to environmental protection, public health, production safety and labor matters. No notices, complaints, demands or proceedings have been received, by the Company or the Seller, in relation to any of such issues. There is no condition requiring decontamination or other remedial action. If any dispute arises with the relevant authorities charged with the application of environmental protection, public health, production safety, labor matters and other relevant laws and regulations for matters that have taken place up to the Closing Date, the Seller agrees to indemnify the Purchaser, without delay, for all reasonable costs of settling such disputes, including any interests charged or penalty imposed.
- (xvi) Before the Closing Date, the land on which the Company has been located, including the relative surface water, does not have any toxic or noxious residues which violate the regulations of China as the Company has not carried out such operations as to cause contamination in the above places and in all events have carried out all necessary clean-up operations

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of the same land as a result of the activities of third parties and/or the previous owners of the land.

(xvii) The Company has fully and in a timely manner met their obligations resulting from tax, labor and social insurance legislation with respect to the filing of returns and the payment of taxes; adequate provisions have been made for taxes, public levies and social security contributions anticipated and/or not yet paid. If any dispute arises with the tax authorities or other authorities charged with the application of tax, labor social security and other relevant laws and regulations for matters that have taken place up to the Closing Date, the Sellers agree to indemnify the Purchaser, without delay, for all reasonable costs of settling such disputes, including any interests charged or penalty imposed.

(xviii) No claims have been asserted by any person or entity against the Company over the use of intellectual property rights including patents, trademarks, trade names, copyrights, technology, know-how or processes or challenging or questioning the validity or effectiveness of any such license or agreement. In case of any such claim, there is no legally valid basis to it. The use of any intellectual property rights by the Company does not infringe on the rights of any third party.

7.2 Each of the Sellers acknowledges and accepts that the Purchaser is entering into this Agreement in reliance upon each of the Warranties notwithstanding any investigations which the Purchaser, its agents or advisors may have made, and jointly and severally undertake to indemnify the Purchaser and the Company against any loss, damages, costs (including all legal costs on a solicitor and own client basis), expenses or other liabilities which the Purchaser may incur in connection with:

- (i) any of the Warranties being untrue or misleading or breached;
- (ii) the settlement of any claim that any of the Warranties are untrue or misleading or have been breached and in which the Seller acknowledges or confirms (on a with or without liability basis) that there has been a breach of Warranties;
- (iii) any arbitration or legal proceedings in which the Purchaser or the Company claims that any of the Warranties are untrue or misleading or have been breached, and in which settlement is reached under which the Seller (on a with or without liability basis) acknowledges that a Warranty is untrue or misleading or has been breached, or arbitration award or judgment is given for the Purchaser or the Company provided that if the arbitrator or court makes a ruling as to the payment of costs by the parties, then that ruling shall apply in lieu of the provisions of this Article; and

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(iv) the enforcement and amount of any such settlement or arbitration award or judgment.

- 7.3 Each of the Warranties shall be construed as a separate Warranty and (save as expressly provided to the contrary) shall not be limited or restricted by reference to, or inference from, the terms of any other Warranty or any other terms of this Agreement.
- 7.4 Any rights to which the Purchaser may be or become entitled to by reason of any of the Warranties, and all remedies which may be available to the Purchaser in consequence of any of the Warranties being untrue or misleading or breached, shall ensure for the benefit of any subsidiary or parent or holding company of the Purchaser and, accordingly, any loss which is sustained by the Purchaser in consequence of any of the Warranties being untrue, misleading or breached, shall be deemed also to be a loss of such subsidiary or parent or holding company, and such subsidiary or parent or holding company may bring proceedings and exercise any other remedy on the footing that it has been the beneficial owner of the Transferred Shares at all times since Closing.
- 7.5 Each of the Sellers hereby undertakes that he will, periodically and whenever requested, whether before or after Closing, forthwith disclose in writing to the Purchaser any event, fact or circumstance which may become known to him after the date hereof and which is materially inconsistent with any of the Warranties, or which could reasonably be expected to materially affect a purchaser's valuation of the Transferred Shares or which may entitle the Purchaser to make any claim under this Agreement.
- 7.6 Any breach of any of the Warranties or indemnities made or given by the Seller hereunder occurring before Closing shall, in addition and without prejudice to any other rights or remedies available to the Purchaser, entitle the Purchaser to rescind this Agreement forthwith (provided, in the case of rescission only, that such breach is material) and/or to sue for any breach thereof on the basis set out in this Article 7.
- 7.7 The Warranties shall be deemed repeated on each day up to the Closing Date and again on Closing (by reference to the facts then subsisting).
- 7.8 No claim shall be brought by the Purchaser for breach of any of the Warranties unless (i) the breach occurs during the period of 3 years following the Closing Date, and (ii) notice of such claim specifying in reasonable detail the breach to which the claim relates, the nature of the breach and the amount claimed (where ascertainable) has been received by the relevant Sellers not later than the expiry of the period of 38 months following the Closing Date.

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- 7.9 The Sellers shall only be liable with respect to any claim under the Warranties if:
- (i) the amount finally adjudicated or agreed as being payable with respect to such individual claim is in excess of US\$ 1,000 or the equivalent amount thereof in any other currencies; and
 - (ii) the aggregate amount finally adjudicated or agreed as being payable with respect to all such claims referred to in paragraph (i) above is in excess of US\$ 10,000 or the equivalent amount thereof in any other currencies, in which event the Seller shall be liable for the whole amount and not merely for the excess.
- 7.10 If the Sellers shall pay to the Purchaser or the Company any amount by way of compensation or damages under a claim for breach of Warranties, and the Purchaser or the Company subsequently recovers from a third party any amount relating to such breach or claim, the Purchaser or the Company (as the case may be) shall repay to the Sellers such amount previously paid by them or so much thereof as does not exceed the amount recovered from the third party.
- 7.11 The provisions of Articles 7.8 to 7.10 shall not apply in the event of fraud or dishonesty on the part of any of the Sellers prior to the Closing Date.
- 7.12 If in respect of or in connection with any breach of any of the Warranties, any amount payable to the Purchaser or the Company by the Sellers is subject to taxation, the Sellers shall pay such additional amounts to the Purchaser or the Company so as to ensure that the net amount actually received by the Purchaser or the Company is equal to the full amount payable to the Purchaser or the Company under this Agreement.
- 7.13 If there is any breach of any of the Warranties or any provision of this Agreement by the Seller before the full payment of the Purchase Price, the Purchaser may, to the fullest extent afforded by PRC laws, without prejudice to any other rights that it may have, set off any loss or damage found to be suffered or incurred by it or the Company (or otherwise agreed) in connection with any such breach or set off any claim, against the Purchase Price.

ARTICLE 8

REPRESENTATIONS AND WARRANTIES OF THE PURCHASER

- 8.1 The Purchaser represents and warrants that, as of the Effectiveness Date as well as the Closing Date:

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- (i) It is duly organised, validly existing and in good standing under the laws of Hong Kong SAR;
- (ii) It has obtained the consents, approvals or authorisation to enter into this Agreement required from its shareholders and/or board of directors pursuant to its articles of association, or required by law. Conclusion of this Agreement does not constitute a breach of any agreement or law by which the Purchaser is bound.

ARTICLE 9

EFFECTIVENESS

- 9.1 This Agreement shall become effective when it has been 1) signed by authorised representatives of all the Parties; and 2) duly approved by the Examination and Approval Authority in writing.

ARTICLE 10

CONFIDENTIALITY

- 10.1 For purpose of this Article, Confidential Information shall mean all information not in the public domain (and whether or not recorded in documentary form or on computer disc) including but not limited to:

- (i) the business methods, corporate plans, management systems, finances, maturing new business opportunities or research and development projects of the Company;
- (ii) the marketing or sales of any products or services of the Company, including, without limitation, sales targets and statistics, market surveys and plans, sales techniques, price lists, contact details of customers or potential customers or any suppliers and potential suppliers to the Company, the nature of their business operations, their preferences, ability to pay and all confidential aspects of their business relationship with the Company; and
- (iii) any trade secrets, secret formulae, processes, inventions, designs, know-how, discoveries, technical specifications and other technical information relating to any product or service of the Company.

- 10.2 (i) Before and after Closing, the Sellers:

- (a) may not use or disclose to any person any Confidential Information belonging to the Company or otherwise relating to the Business which they have obtained during their operation; and

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(b) will make every effort to prevent the use or disclosure of Confidential Information.

(ii) Article 10.2(i) does not apply to:-

- (a) disclosure of Confidential Information to a director or employee of the Purchaser or the Company whose function requires him to have the Confidential Information;
- (b) disclosure of Confidential Information to a professional adviser for the purpose of advising the Sellers but only on terms that the provisions of Article 10 apply to the use or disclosure by such professional adviser of such Confidential Information;
- (c) Confidential Information which has become public knowledge otherwise than, directly or indirectly, through the Sellers' breach of this Article 10; or
- (d) disclosure of Confidential Information required by law or regulation (and then if and to the extent practicable only after consulting and taking into account the reasonable requirements of the Purchaser).

10.3 Each of the undertakings in this Article 10 is a separate and independent undertaking. If one or more of those undertakings is held to be void or unenforceable, the validity of the remaining undertakings will not be affected.

10.4 The Sellers agree that:-

- (i) the restrictions and undertakings contained in Article 10 are reasonable and necessary for the protection of the Purchaser's legitimate interests in the goodwill of the Company; and
- (ii) if any such restrictions or undertakings are found to be void or voidable, but would be valid and enforceable if some part or parts of the restriction or undertaking were deleted, such restriction or undertaking will apply with such modifications as may be necessary to make it valid and enforceable.

10.5 The Parties acknowledge that since damages or an account of profits will not be an adequate remedy for a breach of the obligations in this Article 10, the Purchaser is entitled to an injunction to prevent a breach or continued breach.

ARTICLE 11

TERMINATION

11.1 If this Agreement is terminated pursuant to Article 4.4, 6.3 and 7.6, then:

Agreement on Transfer of Equity Shares

- (a) all rights and obligations of the Parties will cease immediately upon termination except that termination will not affect the then accrued rights and obligations of the Parties (including the right to damages for the breach, if any, giving rise to the termination) and any other pre-termination breach by any of the Parties;
- (b) the Parties shall, to their best efforts, coordinate to reverse the Transaction to the effect that this Agreement has never been executed by the Parties.

ARTICLE 12

BREACH OF CONTRACT

- 12.1 In the event of any failure by any Party to perform any of its or his material obligations hereunder, or any representations and warranties set forth herein are inaccurate, untrue, or misleading, it shall constitute a breach of this Agreement ("Breach"). The Party in breach of this Agreement shall fully indemnify the non-breaching Party for any and all damages and losses suffered by the non-breaching Party as a result of the Breach.
- 12.2 The Party in breach shall have thirty (30) days within which to cure any Breach upon written notice of the non-breaching Party indicating the Breach. If a cure is not effected within the above time period, then the non-breaching Party shall be entitled to be compensated for all damages and losses related to and/or resulting from such breach, provided however that the non-breaching Party shall not be entitled to receive punitive or non-consequential damages.
- 12.3 In case of any breach of this Agreement by any of the Sellers, the Purchaser shall be entitled to deduct and set-off its damages and losses from and against the Purchaser Price. If the unpaid part of Purchase Price is not enough to cover such damages and losses, the Seller shall further compensate the Purchaser for the remaining amount of damages and losses.

ARTICLE 13

SETTLEMENT OF DISPUTES

- 13.1 Any dispute, controversy or claim arising out of or relating to this Agreement, or the breach, termination or invalidity of this Agreement, shall be settled by arbitration in accordance with the UNCITRAL Arbitration Rules which are in force at the relevant time (and as the same may be amended by the remainder of this provision). The place of arbitration shall be in Hong Kong at the Hong Kong International Arbitration Centre. The Purchaser shall be entitled to appoint one arbitrator, the Sellers shall be jointly entitled to appoint one

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arbitrator, and the third arbitrator shall be appointed by Hong Kong International Arbitration Centre and serve as the chairman of the arbitration panel. The language to be used in such arbitration proceedings shall be English.

- 13.2 The arbitral award shall be final and binding on all the Parties (regardless of whether they are parties to the arbitration proceedings or not), and may be enforced by any court or judicial authority having competent jurisdiction over the party or its assets against whom the arbitral award is to be enforced.
- 13.3 Upon and after the submission of any dispute to arbitration, the Parties shall continue to exercise their remaining respective rights, and fulfil their remaining respective obligations under this Agreement, except insofar as the same may relate directly to the matters in dispute.

ARTICLE 14

MISCELLANEOUS

- 14.1 This Agreement and the rights of the Parties hereunder shall be construed and interpreted in accordance with the laws of the People's Republic of China. If there are no relevant Chinese laws, then standard international commercial practice shall apply.
- 14.2 Each of the Sellers shall be jointly and severally liable for any duties and responsibilities of the Sellers hereunder, including the representations and warranties made by the Sellers. In case of breach of any provisions of the Agreement, or any of the Sellers' representations and warranties is found to be mistaken or inaccurate, the Purchaser may claim against any and all of the Sellers at its sole discretion.
- 14.3 Each Party shall be responsible for the costs incurred by itself during or in connection with the drafting, negotiating and execution of this Agreement including costs for its legal and financial advisors, the costs and expenses incurred for conducting asset valuation, obtaining approvals, permits that it is required to obtain.
- 14.4 This Agreement supersedes all and any previous agreements or arrangements between the Parties relating to the sale and purchase of the Transferred Shares, and no future variation shall be effective unless made in writing, signed by each of the Parties and approved by the Examination and Approval Authority.

Agreement on Transfer of Equity Shares

- 14.5 If at any time any provision of this Agreement is or become illegal, invalid or unenforceable in any respect, the remaining provision hereof shall in no way be affected or impaired thereby.
- 14.6 The attached schedules shall form an integral part of this Agreement. This Agreement constitutes the entire agreement between the Parties. There are not and shall be deemed not to be any verbal statements or undertakings between the Parties.
- 14.7 Except for any agreement made by the Parties in writing to the contrary, no failure or delay to exercise any right, power, priority or remedy under this Agreement will be deemed as waiver of such right, power, priority or remedy. Nor will any single or partial exercise of any right, power, priority or remedy preclude any other or further exercise of that or any other right, power, priority or remedy.
- 14.8 This Agreement is signed in eight (8) originals and each Party shall hold one (1) original and four (4) originals may be submitted to the Examination and Approval Authority. This Agreement is written in English and Chinese language and both language versions shall be equally valid.

(The rest of this page is intentionally left blank)

Agreement on Transfer of Equity Shares

IN WITNESS WHEREOF, each Party hereto has caused this Agreement to be executed by its authorised representatives:

Shenzhen, Guangdong Province, January 25, 2006

By: (ABLE NEW ENERGY CO., LIMITED)

/s/ John D. Kavazanjian

Authorized Representative:

By: (HUANG DEYONG)

/s/ Huang Deyong

By: (LI XIAOCHUN)

/s/ Li Xiaochun

By: (ZHU DEHONG)

/s/ Zhu Dehong

I, John D. Kavazanjian, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Ultralife Batteries, Inc.;
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: May 10, 2006

/s/ John D. Kavazanjian

John D. Kavazanjian
President and Chief Executive Officer

I, Robert W. Fishback, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Ultralife Batteries, Inc.;
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: May 10, 2006

/s/ Robert W. Fishback

Robert W. Fishback
Vice President – Finance and
Chief Financial Officer

Section 1350 Certification

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 ("Section 906"), John D. Kavazanjian and Robert W. Fishback, the President and Chief Executive Officer and Vice President — Finance and Chief Financial Officer, respectively, of Ultralife Batteries, Inc., certify that (i) the Quarterly Report on Form 10-Q for the quarter ended April 1, 2006 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and (ii) the information contained in such report fairly presents, in all material respects, the financial condition and results of operations of Ultralife Batteries, Inc.

A signed original of this written statement required by Section 906 has been provided to Ultralife Batteries, Inc. and will be retained by Ultralife Batteries, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

Date: May 10, 2006

/s/ John D. Kavazanjian

John D. Kavazanjian
President and Chief Executive Officer

Date: May 10, 2006

/s/ Robert W. Fishback

Robert W. Fishback
Vice President – Finance and
Chief Financial Officer