

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 8-K

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

September 11, 2009
(Date of earliest event reported)

TELKONET, INC.
(Exact Name of Registrant as Specified in Its Charter)

Utah
(State or Other Jurisdiction of Incorporation)

000-31972
(Commission File No.)

87-0627421
(I.R.S. Employer Identification No.)

20374 Seneca Meadows Parkway, Germantown, Maryland 20876
(Address of Principal Executive Offices)

(240)-912-1800
(Registrant's Telephone Number)

Not Applicable
(Former Name or Former Address, if Changed Since Last Report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (see General Instruction A.2. below):

- Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425).
 - Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12).
 - Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b)).
 - Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c)).
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Item 1.01 Entry into a Material Definitive Agreement.

On September 11, 2009, Telkonet, Inc. (the “Company”) entered into a Loan Agreement in the aggregate principal amount of \$300,000 with the Wisconsin Department of Commerce (the “Department”). The outstanding principal balance bears interest at the annual rate of Two (2) percent. Payment of interest and principal is to be made in the following manner: (a) payment of any and all interest that accrues from the date of disbursement commences on January 1, 2010 and continues on the first day of each consecutive month thereafter through and including December 31, 2010; (b) commencing on January 1, 2011 and continuing on the first day of each consecutive month thereafter through and including November 1, 2016, the Company shall pay equal monthly installments of \$4,426 each; followed by a final installment on December 1, 2016 which shall include all remaining principal, accrued interest and other amounts owed by the Company to the Department under the Loan Agreement.

The Company is obligated under the Loan Agreement to create and fill Thirty-Five (35) new full-time positions with an average wage of \$18 per hour in Milwaukee, Wisconsin by December 31, 2012 and, thereafter maintain each such position until December 31, 2014. Failure to satisfy this covenant results in an incremental increase in the interest rate for each new full-time position not kept, created, or maintained; capped at four (4) percent.

If an event of default under the Loan Agreement occurs, and subject to an Intercreditor Agreement between the Company, the Department, Thermo Credit, LLC and YA Global Investments, L.P., the Department may, among other things, declare the principal amount of all obligations under the Loan Agreement immediately due and payable. Events of default under the Loan Agreement include failure to pay interest or principal on the borrowings thereunder, failure to comply with certain covenants or agreements contained therein, and other events of default customary for financings of this type, subject to, as the case may be, applicable cure periods. The Company may prepay amounts outstanding under the credit facility in whole or in part at any time without penalty. The credit facility is secured by the Company’s assets pursuant to a General Business Security Agreement, a copy of which is attached hereto as Exhibit 10.2. The proceeds from this loan will be used for the working capital requirements of the Company.

Item 9.01 Financial Statements and Exhibits.

(d) Exhibits

- 4.1 Promissory Note in favor of Wisconsin Department of Commerce
 - 10.1 Loan Agreement between the Wisconsin Department of Commerce and Telkonet, Inc.
 - 10.2 General Business Security Agreement
 - 10.3 Intercreditor Agreement
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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 hereunto duly authorized.

TELKONET, INC.

Date: September 17, 2009

By: /s/ Richard J. Leimbach
Richard J. Leimbach
Chief Financial Officer

PROMISSORY NOTE

Amount: \$300,000.00

FOR VALID CONSIDERATION, the receipt and sufficiency of which are hereby acknowledged, and in consideration for the terms and conditions set forth in the Gaming Economic Development Loan Agreement between the Wisconsin Department of Commerce (“Department”) and Telkonet, Inc. (“Borrower”) also identified as Contract #GEDL FY09-19444, the Borrower promises to pay the Department the principal sum of Three Hundred Thousand and 00/100 Dollars (\$300,000.00), or so much thereof as may be advanced by the Department, together with interest, in accordance with the terms and conditions hereinafter set forth.

1. **DEFINITIONS.** Terms used in this Promissory Note shall have the same meanings as in the Agreement.
2. **INTEREST RATE.** Except as otherwise provided herein, this Promissory Note shall bear interest on the unpaid principal balance at the annual rate of Two (2) percent, from the date of actual disbursement of the funds, or any portion thereof, to the Borrower until this Promissory Note is paid in full. Interest shall be computed based upon a 365-day year.
3. **TERM.** The term of this Note shall commence on the Effective Date with all principal, accrued interest and other amounts owed hereunder being due and payable not later than December 1, 2016.
4. **DEFERRAL PERIOD.** The Borrower’s payments of principal hereunder shall be deferred until December 31, 2010. All interest from the date of the Department’s first disbursement shall be paid in accordance with the terms of Paragraph 5.
5. **PAYMENT.** Payment of interest and principal shall be made in the following manner:
 - a) Payment of any and all interest that accrues from the date of disbursement shall commence on January 1, 2010 and continue on the first day of each consecutive month thereafter through and including December 31, 2010. The Borrower shall make payments in twelve equal monthly installments of \$500.00 each.
 - b) Commencing on January 1, 2011 and continuing on the first day of each consecutive month thereafter through and including November 1, 2016, the Borrower shall pay this Promissory Note in 71 equal monthly installments of \$4,426.00 each; followed by a final installment on December 1, 2016 which shall include all remaining principal, accrued interest and other amounts owed by the Borrower hereunder. Payments shall be applied first to interest accrued to date of receipt, and the balance, if any, to principal.
6. **TERMS OF PAYMENT.**
 - a) Time shall be of the essence as to the Borrower's payment of all principal, accrued interest, and other amounts owed hereunder, which shall be delivered to the Department at the following address, or such other place or places as the Department may designate, prior to the close of business on the due dates set forth above:

State of Wisconsin
Dept. of Commerce - Administrative
P.O. Box 78257
Milwaukee, WI 53293-0257
Attn: Contract GEDL FY09-19444

- b) If the Borrower fails to pay any amounts owed within ten (10) calendar days of the date when due, then, from the date of default until such delinquent payment is paid in full, the Borrower shall pay the Department interest on the delinquent payment at an annual rate of twelve (12) percent. The accrual and collection of such interest shall be in addition to and not in lieu of any other rights and remedies that the Department may have under the Agreement, the Promissory Note, other loan documents, and applicable federal and state laws.
 - c) The Borrower shall bear the entire risk of loss, theft, damage, destruction, or seizure of the Collateral. The Borrower shall be obligated to pay the principal, interest, and other amounts owed hereunder even if the Borrower is unable to use the Collateral or any portion thereof, because of loss, theft, damage, destruction, seizure, nonrepair, lack of maintenance, or any other reason.
 - d) All principal payments, interest and other amounts owed hereunder shall be paid by the Borrower regardless of any set off, counterclaim, recoupment, defense, or other rights which the Borrower may have against the Department, the sellers of the Collateral, the contractors and subcontractors involved in making improvements to the Collateral, or any other party.
7. **“EVENT OF DEFAULT” DEFINED.** The term “Event of Default” shall have the meaning set forth in the Agreement.
8. **REMEDIES IN EVENT OF DEFAULT.** Upon the occurrence of an Event of Default, the Department shall have the remedies set forth in the Agreement.
9. **NO PREPAYMENT PENALTY.** The Borrower shall have the right to prepay this Promissory Note, in whole or in part, at any time without penalty.
10. **CHOICE OF LAW. THIS PROMISSORY NOTE IS AND SHALL BE GOVERNED BY THE LAWS OF THE STATE OF WISCONSIN.** If any provisions of this Promissory Note shall be prohibited by or invalid under Wisconsin law, such provisions shall be ineffective only to the extent of such prohibition or invalidity, without affecting the validity or enforceability of the remaining provisions thereof.
11. **VENUE; JURISDICTION.** Any judicial action relating to the construction, interpretation, or enforcement of this Promissory Note, or the recovery of any principal, accrued interest, court costs, attorney’s fees and other amounts owed hereunder, shall be brought and venued in the U.S. District Court for the Western District of Wisconsin or the Dane County Circuit Court in Madison, Wisconsin. **THE BORROWER HEREBY CONSENTS TO PERSONAL JURISDICTION IN THOSE WISCONSIN COURTS, AND WAIVES ANY DEFENSES THAT MAKER OTHERWISE MIGHT HAVE RELATING THERETO.**
12. **CAPTIONS.** The captions in this Promissory Note are for convenience of reference only and shall not define or limit any of the terms and conditions set forth herein.

13. **WAIVER.** The Department's failure to declare this Promissory Note in default or to otherwise enforce any of their respective rights or remedies shall not be deemed a waiver of its right to declare this Promissory Note in default and enforce its rights and remedies upon the occurrence of a future Event of Default. Nor shall the Department's receipt and acceptance of any payment on this Promissory Note after the occurrence of an Event of Default constitute or be construed as a waiver of the default or the Department's rights and remedies as a result of that default. No covenant, condition, or provision of this Promissory Note may be waived except with the Department's express written consent.
14. **AGREEMENT INCORPORATED BY REFERENCE.** This Promissory Note is subject to all of the terms, conditions, covenants and promises set forth in the Agreement which is hereby incorporated by reference as if fully set forth herein.
15. **AUTHORITY TO SIGN DOCUMENT.** The person(s) signing this Promissory Note on behalf of the Borrower certifies and attests that the Borrower's respective Articles of Organization, Articles of Incorporation, By Laws, Member's Agreement, Charter, Partnership Agreement, Corporate or other Resolutions, and/or other related documents give full and complete authority to bind the Borrower, on whose behalf they are executing this document.

Borrower assumes full responsibility and holds the Department harmless for any and all payments made or any other actions taken by Department in reliance upon the above representation. Further, Borrower agrees to indemnify Department against any and all claims, demands, losses, costs, damages or expenses suffered or incurred by Department resulting from or arising out of any such payment or other action, including reasonable attorneys' fees and legal expenses.

IN WITNESS WHEREOF, the undersigned Borrower has executed and delivered this Promissory Note as of the dates set forth below.

TELKONET, INC.

By: /s/ Richard Leimbach
Richard Leimbach, CFO

9/11/2009
Date

**LOAN
AGREEMENT
BETWEEN THE
WISCONSIN DEPARTMENT OF COMMERCE
AND
TELKONET, INC.**

This Agreement is entered into by and between the Wisconsin Department of Commerce (“Department”) and Telkonet, Inc., (“Borrower”).

WITNESSETH

WHEREAS, the Department is authorized to award loan funds, for the purpose of economic development pursuant to Section 560.137 Wis. Stats.; and

WHEREAS, on May 18, 2009, the Department, relying upon representations in the Borrower's Application, agreed to lend up to Three Hundred Thousand and 00/100 Dollars (\$300,000.00) to the Borrower to be utilized in accordance with the terms and conditions of this Agreement.

NOW, THEREFORE, for valid consideration, the receipt of which is hereby acknowledged, and in consideration for the promises and covenants in this Agreement, the Department and Borrower agree as follows:

1. **DEFINITIONS.** For the purposes of this Agreement, the following terms shall have the meanings set forth below:
 - a) “Agreement” means this Agreement between the Department and the Borrower, together with any future amendments thereto.
 - b) “Application” means the Commerce application submitted by the Borrower.
 - c) “Borrower” means Telkonet, Inc., together with its lawful successors and assigns.
 - d) “Collateral” means the property described in Exhibit A.
 - e) “Department” means the Wisconsin Department of Commerce, together with its lawful successors and assigns.
 - f) “Effective Date” means the date this Agreement is executed by the Department.
 - g) “Eligible Project Costs” means the costs and expenditures incurred by the Borrower in connection with the Project as described in Exhibit A, over the time period described in Exhibit A.

- h) "Existing Full-Time Positions" means the currently existing Full-Time Positions that will be retained by the Borrower in Wisconsin in connection with the Project as described in Exhibit A.
 - i) "Full-Time Position" means any permanent position where an employee is required, as a condition of employment, to work at least 40 hours per week and 2,080 hours per year including paid leave and holidays.
 - j) "GEDL" and "Loan" each mean the Department's Gaming Economic Development Loan to the Borrower under this Agreement.
 - k) "Project" means the activities described in Exhibit A.
 - l) "Promissory Note" means the Promissory Note attached as Exhibit D
 - m) "Term of this Agreement" means until the Borrower's obligations hereunder are fully satisfied.
2. **DISBURSEMENT OF LOAN PROCEEDS.** Loan disbursements to the Borrower hereunder for Eligible Project Costs (defined in Exhibit A) shall be made on a periodic basis upon the Department's receipt and approval of a completed Request for Disbursement Form (attached as Exhibit C) and required supporting documentation.
- a) Prior to the disbursement of any Loan funds, the Borrower shall execute and deliver to the Department:
 - (i) A borrowing resolution.
 - (ii) A security agreement, granting the Department a subordinate security interest on all assets now owned or hereinafter acquired. Authentication of this agreement by the Borrower authorizes the Department to file a UCC financing statement for the stated Collateral.
 - (iii) An intercreditor agreement.
 - (iv) All other documents that reasonably may be required by the Department to effect the terms and conditions of this Agreement.
 - b) Disbursements by the Department to the Borrower shall be made after a nonrefundable origination fee of \$6,000.00, two (2.0) percent of the award amount, is paid to the Department.
3. **BORROWER'S LOAN PAYMENTS.** This Loan shall be repaid in accordance with the terms of the Promissory Note (Attached as Exhibit D).
4. **TAXES AND FEES.** Except as otherwise provided in this Agreement, the Borrower shall keep the Collateral free and clear of all judgements, levies, liens, security interests and encumbrances and shall pay all federal, state and local fees, assessments and taxes which may be assessed upon the ownership, possession or use of the Collateral.

5. **INSURANCE.** The Borrower covenants that it will maintain insurance in such amounts and against such liabilities and hazards as customarily is maintained by other companies operating similar businesses.
6. **“EVENT OF DEFAULT” DEFINED.** The occurrence of any one or more of the following events shall constitute an “Event of Default” for the purposes of this Agreement:
- a) The Borrower’s failure to pay, within ten (10) calendar days of the due date, any of the principal payments or interest due under the Promissory Note (Attached as Exhibit D);
 - b) The Borrower's failure to comply with or perform any of its material obligations under this Agreement; provided that the Borrower's failure to comply with the terms and conditions of Exhibit A, Section 3. a), b), and d) hereunder shall not be considered an “Event of Default”.
 - c) Any assignment for the benefit of the Borrower's creditors or commission of any other act amounting to a business failure;
 - d) The filing, by or against the Borrower, of a petition under any chapter of the U.S. Bankruptcy Code or for the appointment of a receiver;
 - e) Any uncured material default or breach of the Borrower’s obligations under the terms and conditions of its loan agreements, leases, or financing arrangements with other creditors;
 - f) Any material misrepresentation with respect to the Borrower's warranties and representations under this Agreement or the Application; or
 - g) Any other action or omission by the Borrower, which in the Department’s reasonable discretion, jeopardizes the Borrower's ability to fulfill its obligations under this Agreement or otherwise causes the Department to deem itself insecure.

7. **REMEDIES IN EVENT OF DEFAULT.**

- a) Upon the occurrence of any Event of Default, the Department shall send a written notice of default to the Borrower, and to the creditors, Thermo Credit, LLC and YA Global Investments, L.P., setting forth with reasonable specificity the nature of the default. If the Borrower fails to cure the default to the reasonable satisfaction of the Department within ten (10) calendar days, the Department may, without further written notice to the Borrower, declare the Borrower in default, terminate this Agreement effective immediately, and accelerate the principal balance, accrued interest, and other amounts owed by the Borrower hereunder.
- b) Upon the termination of this Agreement:
 - (i) The Borrower shall be liable for the full unpaid principal balance together with interest at the annual rate of twelve (12) percent from the date of the Event of Default to the date the Borrower's obligations hereunder are paid in full.

- (ii) Subject to the rights of other creditors, the Department shall be entitled to exercise any and all remedies available to the Department under this Agreement, related loan documents, and applicable laws.
 - c) In addition to the rights and remedies available to the Department at law, in equity, or in bankruptcy, the Department shall be entitled to recover from the Borrower an amount equal to the sum of:
 - (i) The unpaid principal balance, accrued interest, and other amounts owed by the Borrower hereunder;
 - (ii) All court costs and reasonable attorney's fees incurred by the Department in the enforcement of its rights and remedies under this Agreement, including all costs incurred in foreclosing upon, repossessing, storing, repairing, selling, leasing or otherwise disposing of the Collateral; and
 - (iii) Any other damages arising from the Borrower's default.
 - d) The Department's foreclosure upon, repossession of, and subsequent sale, lease, or disposition of the Collateral shall not affect the Department's right to recover from the Borrower any and all damages caused by the Borrower's breach of this Agreement. The Department's rights and remedies hereunder shall be cumulative, not exclusive, and shall be in addition to all other rights and remedies available at law, in equity or in bankruptcy.
8. **BORROWER'S WARRANTIES AND REPRESENTATIONS.** To induce the Department to enter into this Agreement, and for other good and valuable consideration, the receipt of which is hereby acknowledged, the Borrower hereby warrants and represents that:
- a) The Borrower is duly organized, validly existing, and authorized to engage in business in the State of Wisconsin.
 - b) To its knowledge, the Borrower is qualified to engage in business in every jurisdiction where the nature of its business makes such qualification necessary;
 - c) The Borrower is in compliance with all laws, regulations, ordinances and orders of public authorities applicable to it, the violation of which would have a material and adverse effect on the Borrower's financial ability to comply with this Agreement;
 - d) The Borrower is unaware of any conditions which could subject it to any damages, penalties or clean-up costs under any federal or state environmental laws which would have a material and adverse effect on the Borrower's financial ability to comply with this Agreement;
 - e) This Agreement is valid and enforceable in accordance with its terms against the Borrower, subject only to applicable bankruptcy, insolvency, reorganization or other similar laws affecting generally the enforceability of the rights of creditors;

- f) Except as set forth in Section 8(f) hereto, the Borrower is financially solvent and able to comply with all of the terms and conditions set forth in the Agreement and is not in default under the terms and conditions of any loan agreements, leases, or financing arrangements with the Borrower's other creditors. With respect to that certain Commercial Business Loan Agreement for Telkonet, Inc. Line of Credit September 9, 2008 by and between Thermo Credit, LLC and the Borrower, the Borrower is not in satisfaction of clauses D(10) (A) and (B) requiring that: (i) Borrower's minimum cash flow to debt service ratio not be less than 1 to 1 as of the end of each fiscal quarter and that (ii) Borrower maintain a tangible net worth of not less than \$14,400,000.00 as of the last day of each fiscal quarter. Thermo Credit, LLC has waived the foregoing requirements as of the quarter ended June 30, 2009 for a period of ninety (90) days thereafter.
- g) The financial statements and other information provided by the Borrower to the Department are complete and accurate in accordance with Generally Accepted Accounting Principles, and may be relied upon by the Department in deciding whether to enter into this Agreement with the Borrower;
- h) The Borrower has private Project funds as identified in Exhibit A to fund all other costs relating to the Project;
- i) In making these warranties and representations, the Borrower has not relied upon any information furnished by the Department.
- j) The Borrower's warranties and representations herein are true and accurate as of the date of this Agreement, and shall survive the execution thereof;

9. **BORROWER COVENANTS.**

- a) Deliverables. The Borrower shall comply with the terms and conditions set forth in Exhibit A Section 3. of this agreement. Should the Borrower fail to meet the terms and conditions set forth in Exhibit A it may be subject to penalties outlined in Exhibit A.
- b) Reporting. The Borrower shall provide the Department with reports, utilizing forms provided by the Department, as well as interim and/or fiscal year end financial statements in accordance with Exhibit B-1 and B-2.
- c) Inspection.
 - (i) The Department and its respective agents, shall, at any reasonable time and upon 48 hours notice, have the right to enter upon the Borrower's premises to inspect the Project.
 - (ii) The Borrower shall produce for the Department's inspection, examination, auditing and copying, upon reasonable advance notice, any and all records which relate to this Agreement.
- d) Nondiscrimination in Employment. During the Term of this Agreement, the Borrower shall not discriminate against any employee or applicant for employment because of age, race, religion, color, handicap, sex, physical condition, developmental disability as defined in sec. 51.01 (5) Stats., sexual orientation or national origin. This provision shall include, but not be limited to, the following: employment, upgrading, demotion or transfer; recruitment or recruitment advertising; layoff or termination; rates of pay or other forms of compensation; and selection for training, including apprenticeship. Except with respect to sexual orientation, the Borrower further agrees to take affirmative action to ensure equal employment opportunities. The Borrower agrees to post in conspicuous places, available for employees and applicants for employment, notices to be provided by the contracting officer setting forth the provisions of the nondiscrimination clause.

- e) Notification of Position Openings. In accordance with sec. 106.16, Stats., the Borrower shall, for a period of one year from the Effective Date, provide the Wisconsin Department of Workforce Development, local Job Service offices, and the area Workforce Development Board with prior written notice of any new or vacant Full-Time Positions that are related to the Project.
 - f) Consolidation or Merger. During the term of this Agreement, the Borrower shall not consolidate or merge with or into any other corporation or business entity without providing prior written consent of the Department.
 - g) Relocation of Operations. In accordance with §560.075(2), the Borrower shall not relocate the Project, or any Full-Time Positions related thereto, outside of Wisconsin for a minimum of five years from the date of the award.
10. **WISCONSIN OPEN RECORDS LAW.** Subject to the following terms, the Department shall safeguard all of the financial statements provided to them by the Borrower:
- a) Except as otherwise required or provided by court order, legal process or applicable Wisconsin law including, without limitation, the Wisconsin Open Records Law, sec. 19.31, Stats., et seq, the Department shall not reveal or disclose any financial information and documents provided by the Borrower to any non-government person or entity without the prior written consent of the Borrower.
 - b) If the Borrower believes or contends that any financial statements provided hereunder qualify as “trade secrets” exempt from disclosure under the Wisconsin Open Records Law, the Borrower shall:
 - (i) Fill out a standard trade secrets designation form to be provided by the Department, designating specific information or documents as “trade secrets” and agreeing to defend and indemnify the Department, and to hold them harmless in the event of any future open records request asking for copies of such documents; and
 - (ii) Provide the Department with two copies of such information -- a clean copy and a copy with the “trade secret” information redacted--for the Department’s files.
11. **ENTIRE AGREEMENT.** This Agreement and the accompanying loan documents, Promissory Note, and exhibits contain the entire Agreement of the parties concerning the Borrower's obligations under the terms and conditions of this Agreement. This Agreement may not be amended, modified or altered except in writing signed by the Borrower and the Department.
12. **CHOICE OF LAW. THIS AGREEMENT IS AND SHALL BE GOVERNED BY THE LAWS OF THE STATE OF WISCONSIN.** If any provisions of the Agreement shall be prohibited by or invalid under Wisconsin law, such provisions shall be ineffective only to the extent of such prohibition or invalidity, without affecting the validity or enforceability of the remaining provisions thereof.

13. **VENUE; JURISDICTION.** Any judicial action relating to the construction, interpretation, or enforcement of this Agreement, or the recovery of any principal, accrued interest, court costs, attorney's fees and other amounts owed hereunder, shall be brought and venued in the U.S. District Court for the Western District of Wisconsin or the Dane County Circuit Court in Madison, Wisconsin. **THE BORROWER HEREBY CONSENTS TO PERSONAL JURISDICTION IN THOSE WISCONSIN COURTS, AND WAIVES ANY DEFENSES THAT THE BORROWER OTHERWISE MIGHT HAVE RELATING THERETO.**
14. **WAIVER OF RIGHT TO JURY TRIAL. THE BORROWER HEREBY WAIVES ITS RIGHT TO A JURY TRIAL IN CONNECTION WITH ANY JUDICIAL ACTION OR PROCEEDING THAT MAY ARISE BY AND BETWEEN THE DEPARTMENT AND THE BORROWER CONCERNING THE CONSTRUCTION, INTERPRETATION OR ENFORCEMENT OF THIS AGREEMENT, OR THE RECOVERY OF ANY PRINCIPAL, ACCRUED INTEREST, COURT COSTS, ATTORNEY'S FEES AND OTHER AMOUNTS THAT MAY BE OWED BY THE BORROWER HEREUNDER.**
15. **MISCELLANEOUS.**
- a) Severability. The invalidity of any provision of this Agreement shall not affect the validity of the remaining provisions, which shall remain in full force and effect to govern the parties' relationship.
 - b) Department Not A Joint Venturer Or Partner. The Department shall not, under any circumstances, be considered or represented to be a partner or joint venturer of the Borrower or any beneficiary thereof.
 - c) Documents. All documents required to be delivered contemporaneously with the execution and delivery of this Agreement are expressly made a part of this Agreement as though completely herein, and all references to this Agreement herein shall be deemed to refer to and include all such documents.
 - d) Agreement Controlling. In the event of any conflict or inconsistency between the Agreement and the exhibits hereto, the terms of this Agreement shall control.
16. **CAPTIONS.** The captions in this Agreement are for convenience of reference only and shall not define or limit any of the terms and conditions set forth herein.
17. **AUTHORITY TO SIGN DOCUMENT.** The person(s) signing this Agreement on behalf of the Borrower certifies and attests that the Borrower's respective Articles of Organization, Articles of Incorporation, By Laws, Member's Agreement, Charter, Partnership Agreement, Corporate or other Resolutions, and/or other related documents give full and complete authority to bind the Borrower, on whose behalf they are executing this document.

Borrower assumes full responsibility and holds the Department harmless for any and all payments made or any other actions taken by Department in reliance upon the above representation. Further, Borrower agrees to indemnify Department against any and all claims, demands, losses, costs, damages or expenses suffered or incurred by Department resulting from or arising out of any such payment or other action, including reasonable attorneys' fees and legal expenses. The Borrower has read, fully understands, and agrees to all of the terms and conditions in this Agreement and the related loan documents;

IN WITNESS WHEREOF, the Department and the Borrower have executed and delivered this Agreement effective the date set forth next to the Department's signature below.

WISCONSIN DEPARTMENT OF COMMERCE

By: /s/ Mary Gage
Mary Gage, Bureau Director

9/11/2009
Date

TELKONET, INC.

By: /s/ Richard Leimbach
Richard Leimbach, CFO

9/11/2009
Date

Notices to the Borrower hereunder shall be effective upon mailing by first class mail, postage prepaid, and addressed as follows or such other person and address as may be designated in writing:

Notices to the Department hereunder shall be effective upon mailing by first class mail, postage prepaid, and addressed as follows:

Telkonet, Inc.
10200 Innovation Drive, Suite 300
Milwaukee, WI 53226
Attn: Jason Tienor, President/CEO

Wisconsin Department of Commerce
Bureau of Business Finance
201 West Washington Avenue
P.O. Box 7970
Madison, WI 53707
Attn: Contract #GEDL FY09-19444

With a copy to:

Telkonet, Inc.
20374 Seneca Meadows Parkway
Germantown, MD 20874
Attn: Howard Barr, General Counsel

GENERAL BUSINESS SECURITY AGREEMENT

Dated 9/11/2009

1. SECURITY INTEREST

In consideration of any financial accommodation at any time granted by Wisconsin Department of Commerce ("**Lender**") to Telkonet, Inc. ("**Borrower**"), each of the undersigned ("**Debtor**," whether one or more) grants Lender a security interest in all equipment, fixtures, inventory, documents, general intangibles, accounts, deposit accounts (unless a security interest would render a nontaxable account taxable), contract rights, chattel paper, patents, trademarks and copyrights (and the good will associated with and registrations and licenses of any of them), instruments, letter of credit rights and investment property, now owned or hereafter acquired by Debtor (or by Debtor with spouse), and all additions and accessions to, all spare and repair parts, special tools, equipment and replacements for, software used in, all returned or repossessed goods the sale of which gave rise to and all proceeds, supporting obligations and products of the foregoing ("**Collateral**"), wherever located, to secure all debts, obligations and liabilities to Lender arising out of credit previously granted, credit contemporaneously granted and credit granted in the future by Lender to any Debtor, or any Borrower, to any of them and another, or to another guaranteed or endorsed by any of them ("**Obligations**").

2. DEBTOR'S WARRANTIES

Debtor warrants and agrees that while any of the Obligations are unpaid:

(a) **Ownership and use.** Debtor owns (or with spouse owns) the Collateral free of all encumbrances and security interests (except Lender's security interest). Chattel paper constituting Collateral evidences a perfected security interest in the goods (including software used in the goods) covered by it, free from all other encumbrances and security interests, and no financing statement is on file or control agreement in existence (other than Lender's) covering the Collateral or any of it. Debtor, acting alone, may grant a security interest in the Collateral and agree to the terms of this Agreement. The Collateral is used or bought for use primarily for business purposes.

(b) **Sale of goods or services rendered.** Each account and chattel paper constituting Collateral as of this date arose from the performance of services by Debtor or from a bona fide sale or lease of goods, which have been delivered or shipped to the account debtor and for which Debtor has genuine invoices, shipping documents or receipts.

(c) **Enforceability.** Each account, contract right and chattel paper constituting Collateral as of this date is genuine and enforceable against the account debtor according to its terms. It and the transaction out of which it arose comply with all applicable laws and regulations. The amount represented by Debtor to Lender as owing by each account debtor is the amount actually owing and is not subject to setoff, credit, allowance or adjustment, except discount for prompt payment, nor has any account debtor returned the goods or disputed liability.

(d) **Due date.** There has been no default as of this date according to the terms of any chattel paper or account constituting Collateral and no step has been taken to foreclose the security interest it evidences or otherwise enforce its payment.

(e) **Financial condition of account debtor.** As of this date Debtor has no notice or knowledge of anything which might impair the credit standing of any account debtor and Debtor will advise Lender upon receipt of any such notice or knowledge affecting Collateral.

(f) **Valid organization.** If a corporation, limited liability company or general or limited partnership, Debtor is duly organized, validly existing and in good standing under the laws of the state of organization and is authorized to do business in Wisconsin.

(g) **Other agreements.** Debtor is not in default under any agreement for the payment of money.

(h) **Authority to contract.** The execution and delivery of this Agreement and any instruments evidencing Obligations will not violate or constitute a breach of Debtor's articles of incorporation or organization, by-laws, partnership agreement, operating agreement or any other agreement or restriction to which Debtor is a party or is subject.

(i) **Accuracy of information.** All information, certificates or statements given to Lender pursuant to this Agreement shall be true and complete when given.

(j) **Name and address.** Debtor's exact legal name is as set forth below Section 11. If Debtor is an individual, the address of Debtor's principal residence is as set forth below Section 11. If Debtor is an organization that has only one place of business, the address of Debtor's place of business, or if Debtor has more than one place of business, then the address of Debtor's chief executive office, is as set forth below Section 11.

(k) **Location.** The address where the Collateral will be kept, if different from that appearing below Section 11, is _____ . Such location shall not be changed without prior written consent of Lender, but the parties intend that the Collateral, wherever located, is covered by this Agreement.

(l) **Organization.** If Debtor is an organization, the type of organization and the state under whose law it is organized are as set forth below Section 11.

(m) **Environmental laws.** (i) No substance has been, is or will be present, used, stored, deposited, treated, recycled or disposed of on, under, in or about any real estate now or at any time owned or occupied by Debtor ("**Property**") during the period of Debtor's ownership or use of the Property in a form, quantity or manner which if known to be present on, under, in or about the Property would require clean-up, removal or some other remedial action ("**Hazardous Substance**") under any federal, state or local laws, regulations, ordinances, codes or rules ("**Environmental Laws**"). (ii) Debtor has no knowledge, after due inquiry, of any prior use or existence of any Hazardous Substance on the Property by any prior owner of or person using the Property, (iii) without limiting the generality of the foregoing, Debtor has no knowledge, after due inquiry, that the Property contains asbestos, polychlorinated biphenyl components (PCBs) or underground storage tanks, (iv) there are no conditions existing currently or likely to exist during the term of this Agreement which would subject Debtor to any damages, penalties, injunctive relief or clean-up costs in any governmental or regulatory action or third-party claim relating to any Hazardous Substance, (v) Debtor is not subject to any court or administrative proceeding, judgment, decree, order or citation relating to any Hazardous Substance, and (vi) Debtor in the past has been, at the present is, and in the future will remain in compliance with all Environmental Laws. Debtor shall indemnify and hold harmless Lender, its directors, officers, employees and agents from all loss, cost (including reasonable attorneys' fees and legal expenses), liability and damage whatsoever directly or indirectly resulting from, arising out of, or based upon (1) the presence, use, storage, deposit, treatment, recycling or disposal, at any time, of any Hazardous Substance on, under, in or about the Property, or the transportation of any Hazardous Substance to or from the Property, (2) the violation or alleged violation of any Environmental Law, permit, judgment or license relating to the presence, use, storage, deposit, treatment, recycling or disposal of any Hazardous Substance on, under, in or about the Property, or the transportation of any Hazardous Substance to or from Property, or (3) the imposition of any governmental lien for the recovery of environmental clean-up costs expended under any Environmental Law. Debtor shall immediately notify Lender in writing of any governmental or regulatory action or third-party claim instituted or threatened in connection with any Hazardous Substance described above on, in, under or about the Property.

(n) **Employees.** There are no unpaid wages due employees of Debtor and there are no outstanding liens against assets of Debtor for unpaid wages due employees of Debtor.

(o) **Fixtures.** If any of the Collateral is affixed to real estate, the legal description of the real estate set forth in each UCC Financing Statement signed or authorized by Debtor is true and correct.

3. SHIPPERS

Shippers authorized to draw drafts on Lender under section 6(c) are:

4. SALE AND COLLECTIONS

(a) **Sale of inventory.** So long as no default exists under any of the Obligations or this Agreement, Debtor may (a) sell inventory in the ordinary course of Debtor's business for cash or on terms customary in the trade, at prices not less than any minimum sale price shown on instruments evidencing

Obligations and describing inventory, or (b) lease or license inventory on terms customary in the trade.

(b) Verification and notification. Lender may verify Collateral in any manner, and Debtor shall assist Lender in so doing. Upon default Lender may at any time and Debtor shall, upon request of Lender, notify the account debtors or other persons obligated on the Collateral to make payment directly to Lender and Lender may enforce collection of, settle, compromise, extend or renew the indebtedness of such account debtors or other persons obligated on the Collateral. Until account debtors or other persons obligated on the Collateral are so notified, Debtor, as agent of Lender, shall make collections and receive payments on the Collateral.

(c) Deposit with Lender. At any time Lender may require that all proceeds of Collateral received by Debtor shall be held by Debtor upon an express trust for Lender, shall not be commingled with any other funds or property of Debtor and shall be turned over to Lender in precisely the form received (but endorsed by Debtor if necessary for collection) not later than the business day following the day of their receipt. Except as provided in Section 4(d) below, all proceeds of Collateral received by Lender directly or from Debtor shall be applied against the Obligations in such order and at such times as Lender shall determine.

(d) Accounting. If the extent to which Lender's security interest in the Collateral is a purchase money security interest depends on the application of a payment to a particular obligation of Debtor, the payment shall first be applied to obligations of Debtor for which Debtor did not create a security interest in the order in which those obligations were incurred and then to obligations of Debtor for which Debtor did create a security interest, including the Obligations secured by the Collateral, in the order in which those obligations were incurred; provided, however, that Lender shall retain its security interest in all Collateral regardless of the allocation of payments.

THIS AGREEMENT INCLUDES THE ADDITIONAL PROVISIONS ON PAGES 2 AND 3.

Page 1 of 3

ADDITIONAL PROVISIONS

5. DEBTOR'S COVENANTS

(a) Maintenance of Collateral. Debtor shall: maintain the Collateral in good condition and repair and not permit its value to be impaired; keep it free from all liens, encumbrances and security interests (other than Lender's security interest); defend it against all claims and legal proceedings by persons other than Lender; pay and discharge when due all taxes, license fees, levies and other charges upon it; not sell, lease, license or otherwise transfer or dispose of it or permit it to become a fixture or an accession to other goods, except for sales, leases or licenses of inventory as provided in this Agreement; not permit it to be used in violation of any applicable law, regulation or policy of insurance; and, as to Collateral consisting of instruments, chattel paper and letter of credit rights, preserve rights in it against prior parties. Loss of or damage to the Collateral shall not affect the liabilities of any Debtor or Borrower under this Agreement, the Obligations or other rights of Lender with respect to the Collateral.

(b) Insurance. Debtor shall keep the Collateral and Lender's interest in it insured under policies with such provisions, for such amounts and by such insurers as shall be satisfactory to Lender from time to time, and shall furnish evidence of such insurance satisfactory to Lender. Subject to Lender's satisfaction, Debtor is free to select the insurance agent or insurer through which the insurance is obtained. Debtor assigns (and directs any insurer to pay) to Lender the proceeds of all such insurance and any premium refund, and authorizes Lender to endorse in the name of Debtor any instruments for such proceeds or refunds and, at the option of Lender, to apply such proceeds and refunds to any unpaid balance of the Obligations, whether or not due, and/or to restoration of the Collateral, returning any excess to Debtor. Each insurance policy shall contain a standard lender's loss payable endorsement in favor of Lender, and shall provide that the policy shall not be cancelled, and the coverage shall not be reduced, without at least 10 days' prior written notice by the insurer to Lender. Lender is authorized, in the name of Debtor or otherwise, to make, adjust and/or settle claims under any credit insurance financed by Lender or any insurance on the Collateral, or cancel the same after the occurrence of an event of default. If Debtor fails to keep any required insurance on the Collateral, Lender may purchase such insurance for Debtor, such insurance may be acquired by Lender solely to protect the interest of Lender (and will not cover Debtor's equity in the Collateral), and Debtor's obligation to repay Lender shall be in accordance with Section 6(a).

(c) Maintenance of security interest. Debtor shall pay all expenses and upon request, take any action reasonably deemed advisable by Lender to preserve the Collateral or to establish, evidence, determine and maintain priority of, perfect, continue perfected, terminate and/or enforce Lender's interest in it or rights under this Agreement. Debtor authorizes Lender to file Uniform Commercial Code financing statements describing the Collateral (including describing the Collateral as "all assets," "all personal property" or with words of similar effect) and amendments and correction statements to such financing statements and ratifies any such financing statement or amendment filed prior to the date of this Agreement. Debtor will cooperate with Lender in obtaining control of Collateral or other security for the Obligations for which control may be required to perfect Lender's security interest under applicable law. If the Collateral is in possession of a third party, Debtor will join with Lender at its request in notifying the third party of Lender's security interest and obtaining an acknowledgment from the third party that it is holding the Collateral for the benefit of Lender.

(d) Taxes and other charges. Debtor shall pay and discharge all lawful taxes, assessments and government charges upon Debtor or against its properties prior to the date on which penalties attach, unless and to the extent only that such taxes, assessments and charges are contested in good faith and by appropriate proceedings by Debtor.

(e) Employees. Debtor shall pay all wages when due to employees of Debtor and shall not permit any lien to exist against the assets of Debtor for unpaid wages due employees of Debtor.

(f) Records and statements. Debtor shall furnish to Lender financial statements at least annually and such other financial information respecting Debtor at such times and in such form as Lender may request. Debtor shall keep accurate and complete records respecting the Collateral in such form as Lender may approve. At such times as Lender may require, Debtor shall furnish to Lender a statement certified by Debtor and in such form and containing such information as may be prescribed by Lender, showing the current status and value of the Collateral. Debtor shall furnish to Lender such reports regarding the payment of wages to employees of Debtor and the number of employees of Debtor as Lender may from time to time request, and without request shall furnish to Lender a written report immediately upon any material increase in the number of employees of Debtor, the failure of Debtor to pay any wages when due to employees of Debtor or the imposition of any lien against the assets of Debtor for unpaid wages due employees of Debtor.

(g) Inspection of Collateral. At reasonable times Lender may examine the Collateral and Debtor's records pertaining to it, wherever located, and make copies of records, and Debtor shall assist Lender in so doing.

(h) Service charge. In addition to the required payments under the Obligations and this Agreement, Debtor shall pay Lender's then current service charges for servicing and auditing in connection with this Agreement.

(i) Chattel paper. Lender may require that chattel paper constituting Collateral shall be on forms approved by Lender. Unless it consists of electronic chattel paper, Debtor shall promptly mark all chattel paper constituting Collateral, and all copies, to indicate conspicuously Lender's interest and, upon request, deliver them to Lender. If it consists of electronic chattel paper, Debtor shall promptly notify Lender of the existence of the electronic chattel paper and, at the request of Lender, shall take such actions as Lender may reasonably request to vest in Lender control of such electronic chattel paper under applicable law.

(j) United States contracts. If any Collateral arose out of contracts with the United States or any of its departments, agencies or instrumentalities, Debtor will notify Lender and execute writings required by Lender in order that all money due or to become due under such contracts shall be assigned to Lender and proper notice of the assignment given under the Federal Assignment of Claims Act.

(k) Modifications. Without the prior written consent of Lender, Debtor shall not alter, modify, extend, renew or cancel any accounts, letter of credit rights or chattel paper constituting Collateral or any Collateral constituting part of the Debtor's borrowing base.

(l) Returns and repossessions. Debtor shall promptly notify Lender of the return to or repossession by Debtor of goods underlying any Collateral and Debtor shall hold and dispose of them only as Lender directs.

(m) Promissory Notes, Chattel Paper and Investment Property. If Debtor shall at any time hold or acquire Collateral consisting of promissory notes, chattel paper or certificated securities, Debtor shall endorse, assign and deliver the same to Lender accompanied by such instruments of transfer or assignment duly executed in blank as Lender may from time to time request.

(n) Change of name, address or organization. Debtor shall not change Debtor's legal name or address without providing at least 30 days' prior written notice of the change to Lender. Debtor if it is an organization shall not change its type of organization or state under whose law it is organized and shall preserve its organizational existence, and Debtor whether or not Debtor is an organization shall not, in one transaction or in a series of related transactions, merge into or consolidate with any other organization, change Debtor's legal structure or sell or transfer all or substantially all of Debtor's assets.

6. RIGHTS OF LENDER

(a) Authority to perform for Debtor. Upon the occurrence of an event of default or if Debtor fails to perform any of Debtor's duties set forth in this Agreement or in any evidence of or document relating to the Obligations, Lender is authorized, in Debtor's name or otherwise, to take any such action including without limitation signing Debtor's name or paying any amount so required, and the cost shall be one of the Obligations secured by this Agreement and shall be payable by Debtor upon demand with interest from the date of payment by Lender at the highest rate stated in any evidence of any Obligation but not in excess of the maximum rate permitted by law.

(b) Charging Debtor's credit balance. Unless a lien would be prohibited by law or would render a nontaxable account taxable, Debtor grants Lender, as further security for the Obligations, a security interest and lien in any deposit account Debtor may at any time have with Lender and other money now or hereafter owed Debtor by Lender, and agrees that Lender may, at any time after the occurrence of an event of default, without prior notice or demand, set-off all or any part of the unpaid balance of the Obligations against any deposit balances or other money now or hereafter owed Debtor by Lender.

(c) Power of attorney. Debtor irrevocably appoints any officer of Lender as Debtor's attorney, with power after an event of default to receive, open and dispose of all mail addressed to Debtor (and Lender shall not be required as a condition to the exercise of this power to prove the occurrence of an event of default to the Post Office); to notify the Post Office authorities to change the address for delivery of all mail addressed to Debtor to such address as Lender may designate; to endorse the name of Debtor upon any instruments which may come into Lender's possession; and to sign and make draws under any letter of credit constituting Collateral on Debtor's behalf. Debtor agrees that Obligations may be created by drafts drawn on Lender by shippers of inventory named in Section 3. Debtor authorizes Lender to honor any such draft accompanied by invoices aggregating the amount of the draft and

describing inventory to be shipped to Debtor and to pay any such invoices not accompanied by drafts. Debtor appoints any employee of Lender as Debtor's attorney, with full power to sign Debtor's name on any instrument evidencing an Obligation, or any renewals or extensions, for the amount of such drafts honored by Lender and such instruments may be payable at fixed times or on demand, shall bear interest at the rate from time to time fixed by Lender and Debtor agrees, upon request of Lender, to execute any such instruments. This power of attorney to execute instruments may be revoked by Debtor only by written notice to Lender and no such revocation shall affect any instruments executed prior to the receipt by Lender of such notice. All acts of such attorney are ratified and approved and such attorney is not liable for any act or omission or for any error of judgment or mistake of fact or law. This power is a power coupled with an interest and is given as security for the Obligations, and the authority conferred by this power is and shall be irrevocable and shall remain in full force and effect until renounced by Lender except as otherwise expressly provided in this Section 6(c).

(d) Non-liability of Lender. Lender has no duty to determine the validity of any invoice, the authority of any shipper named in section 3 to ship goods to Debtor or compliance with any order of Debtor. Lender has no duty to protect, insure, collect or realize upon the Collateral or preserve rights in it against prior parties. Debtor releases Lender from any liability for any act or omission relating to the Obligations, the Collateral or this Agreement, except Lender's willful misconduct.

7. DEFAULT

Upon the occurrence of one or more of the following events of default:

(a) Nonperformance. Any of the Obligations are not paid when due, or Borrower or Debtor, as applicable, fails to perform, or rectify breach of, any warranty or covenant or other undertaking in this Agreement or in any evidence of or document relating to the Obligations or an event of default occurs under any evidence of or document relating to any other obligation secured by the Collateral;

(b) Inability to Perform. Borrower, Borrower's spouse, Debtor or a guarantor or surety of any of the Obligations dies, ceases to exist, becomes insolvent or the subject of bankruptcy or insolvency proceedings or any guaranty of the Obligations is revoked or becomes unenforceable for any reason;

(c) Misrepresentation. Any warranty or representation made to induce Lender to extend credit to Debtor or Borrower, under this Agreement or otherwise, is false in any material respect when made; or

(d) Insecurity. At any time Lender believes in good faith that the prospect of payment or performance of any of the Obligations or performance under any agreement securing the Obligations is impaired;

all of the Obligations shall, at the option of Lender and without notice or demand, become immediately payable; and Lender shall have all rights and remedies for default provided by the Wisconsin Uniform Commercial Code and this Agreement, as well as any other applicable law, and under any evidence of or document relating to any Obligation, and all such rights and remedies are cumulative and may be exercised from time to time. With respect to such rights and remedies:

(e) Repossession. Lender may take possession of Collateral without notice or hearing, which Debtor waives;

(f) Assembling collateral. Lender may require Debtor to assemble the Collateral and to make it available to Lender at any place reasonably designated by Lender;

(g) Notice of disposition. Written notice, when required by law, sent to any address of Debtor in this Agreement at least 10 calendar days (counting the day of sending) before the date of a proposed disposition of the Collateral is reasonable notice;

(h) Expenses and application of proceeds. Debtor shall reimburse Lender for any expense incurred by Lender in protecting or enforcing its rights under this Agreement, before and after judgment, including, without limitation, reasonable attorneys' fees and legal expenses (including those incurred in successful defense or settlement of any counterclaim brought by Debtor or incident to any action or proceeding involving Debtor brought pursuant to the United States Bankruptcy Code) and all expenses of taking possession, holding, preparing for disposition and disposing of Collateral (provided, however, Lender has no obligation to clean-up or otherwise prepare the Collateral for sale). After deduction of such expenses, Lender shall apply the proceeds of disposition to the extent actually received in cash to the Obligations in such order and amounts as it elects or as otherwise required by this Agreement. If Lender sells any Collateral on credit, Debtor will be credited only with payments that the purchaser actually makes and that Lender actually receives and applies to the unpaid balance of the purchase price of the Collateral; and

(i) Waiver. Lender may permit Debtor or Borrower to remedy any default without waiving the default so remedied, and Lender may waive any default without waiving any other subsequent or prior default by Borrower or Debtor. Lender shall continue to have all of its rights and remedies under this Agreement even if it does not fully and properly exercise them on all occasions.

8. WAIVER AND CONSENT

Each Debtor who is not also a Borrower expressly consents to and waives notice of the following by Lender without affecting the liability of any such Debtor: (a) the creation of any present or future Obligation, default under any Obligation, proceedings to collect from any Borrower or anyone else, (b) any surrender, release, impairment, sale or other disposition of any security or collateral for the Obligations, (c) any release or agreement not to sue any guarantor or surety of the Obligations, (d) any failure to perfect a security interest in or realize upon any security or collateral for the Obligations, (e) any failure to realize upon any of the Obligations or to proceed against any Borrower or any guarantor or surety, (f) any renewal or extension of the time of payment, (g) any allocation and application of payments and credits and acceptance of partial payments, (h) any application of the proceeds of disposition of any collateral for the Obligations to any obligation of any Debtor or Borrower secured by such collateral in such order and amounts as it elects, (i) any determination of what, if anything, may at any time be done with reference to any security or collateral, and (j) any settlement or compromise of the amount due or owing or claimed to be due or owing from any Borrower, guarantor or surety.

9. INTERPRETATION

The validity, construction and enforcement of this Agreement are governed by the internal laws of Wisconsin except to the extent such laws are preempted by federal law. All terms not otherwise defined have the meanings assigned to them by the Wisconsin Uniform Commercial Code, as amended from time to time, provided, however, that the term "instrument" shall be such term as defined in the Wisconsin Uniform Commercial Code-Secured Transactions Chapter 409. All references in this Agreement to sections of the Wisconsin Statutes are to those sections as they may be renumbered from time to time. Invalidity of any provision of this Agreement shall not affect the validity of any other provision. This Agreement is intended by Debtor and Lender as a final expression of this Agreement and as a complete and exclusive statement of its terms, there being no conditions to the enforceability of this Agreement. This Agreement may not be supplemented or modified except in writing.

10. PERSONS BOUND

Each person signing this Agreement is a Debtor. All Debtors are jointly and severally liable under this Agreement. This Agreement benefits Lender, its successors and assigns, and binds Debtor(s) and their respective heirs, personal representatives, successors and assigns and shall bind all persons and entities who become bound as a debtor to this Agreement. If checked here, this Agreement amends and replaces in their entirety the provisions of all existing General Business Security Agreements between Debtor and Lender; provided, however, that all security interests granted to Lender under those existing security agreements shall remain in full force and effect, subject to the provisions of this Agreement. Debtor acknowledges receipt of a completed copy of this Agreement.

11. OTHER PROVISIONS

Notwithstanding anything to the contrary herein, (a) the security interest granted herein shall be subordinate to any other security interest in the Collateral, including but not limited to security interests in the Collateral held by YA Global Investments, L.P. ("YA Global"), and Thermo Credit, LLC ("Thermo"), whether perfected or unperfected and without regard to the order of filing of UCC-1 Financing Statements by each of Thermo and YA Global, and (b) the rights and obligations set forth herein and in that certain Loan Agreement between the Lender and the Borrower of even date herewith are subject to that certain Intercreditor Agreement of even date herewith by and between the Lender, Borrower, YA Global, and Thermo.

Address: 10200 Innovation Drive, Suite 300, Milwaukee, WI 53226

/s/ Richard J. Leimbach, CFO

(SEAL)

SEE SECTIONS 2(j) AND (k)

C-Corporation

TYPE OF ORGANIZATION

Utah

STATE OF ORGANIZATION

(SEAL)

(SEAL)

(SEAL)

(SEAL)

Address: _____

(SEAL)

SEE SECTIONS 2(j) AND (k)

TYPE OF ORGANIZATION

STATE OF ORGANIZATION

(SEAL)

(SEAL)

(SEAL)

(SEAL)

Page 3 of 3
(General Business Security Agreement)

Intercreditor Agreement

September 11, 2009

Wisconsin Department of Commerce
Bureau of Business Finance
201 West Washington Avenue
P.O. Box 7970
Madison, Wisconsin 53707
Attn: Contract #GEDL FY09-19444

Re: Telkonet, Inc. ("Client")

Dear Sirs:

Thermo Credit, LLC ("Thermo Credit") and the above-referenced Client have entered into a Factoring Agreement dated as of January 28, 2008 (as amended and in effect, and together with all other documents, instruments and agreements executed in connection therewith, the "Factoring Agreement"). The Client's obligations under the Factoring Agreement (the "Factoring Obligations") are secured by a security interest (the "Factoring Lien") in all Receivables and Accounts of the Client, whether now owned or hereafter acquired, consisting of "Purchased Receivables" and "Records" (as defined in the Factoring Agreement) relating to the same, and proceeds and payments related to the same and all deposit accounts set up under or pursuant to the Factoring Agreement to receive such proceeds or payments (the "TCL Collateral").

YA Global Investments, L.P. ("YA Global") and the Client have entered into a Securities Purchase Agreement (the "Securities Purchase Agreement") pursuant to which YA Global has purchased certain secured convertible debentures in the original principal amount of \$3,500,000 (the "Debentures"). In connection with the Securities Purchase Agreement, YA Global has been granted a security interest (the "YA Global Liens") in all business assets of the Client (the "YA Global Collateral"), pursuant to and as set forth in that certain Security Agreement between YA Global and the Client dated May 30, 2008 (the "YA Global Security Agreement") and that such collateral includes Thermo Inventory Collateral (as defined below) and the TCL Collateral. As amended and in effect, the Securities Purchase Agreement, the Debentures, the Security Agreement, and all other documents, agreements, and instruments executed in connection therewith are collectively referred to herein as the "YA Global Documents" and all current and future obligations and liabilities of any kind of the Client to YA Global are referred to herein collectively as the "YA Global Obligations".

In connection with the foregoing, YA Global and Thermo Credit have entered into that certain Intercreditor Agreement dated May 30, 2008 (the "May 30 Agreement"), pursuant to which any lien or security interest that YA Global may have in the TCL Collateral shall be subordinate to Thermo Credit's lien and security interest in the TCL Collateral upon the terms set forth in the May 30 Agreement.

Thermo Credit and the Client have entered into a Line of Credit Agreement dated as of September 9, 2008 (the "Line of Credit Agreement") in an amount of up to ONE MILLION AND NO/100 Dollars (\$1,000,000.00) (the "Thermo Line of Credit"). The Client's obligations under the Line of Credit Agreement (the "LOC Obligations", and together with the Factoring Obligations, the "TCL Obligations") are secured by a security interest (the "LOC Lien", and together with the Factoring Lien, the "TCL Liens") in favor of Thermo Credit in inventory of the Client, as more fully defined in the Security Agreement between Thermo Credit and the Client dated as of September 9, 2008 (the "Thermo Security Agreement"). In connection with such Line of Credit Agreement, YA Global, Thermo Credit and the Client have entered into that certain Tri-Party Agreement dated as of September 9, 2008 (the "Tri-Party Agreement") pursuant to which the parties agreed that (i) Thermo Credit would have a first priority security interest in inventory of the Client with a value of Two Million Dollars (\$2,000,000), as reported in the books and records and financial statements of the Client maintained in conformity with generally accepted accounting principles (the "Thermo Inventory Collateral") and (ii) YA Global acknowledged that, to the extent set forth therein, its security interest in Thermo Inventory Collateral became, effective with the execution of the Tri-Party Agreement, junior to Thermo Credit's first priority security interest in Thermo Inventory Collateral.

Thermo Credit and YA Global have been advised by the Department of Commerce of the State of Wisconsin ("Wisconsin") that Wisconsin will be providing financing to the Client pursuant to a line of credit agreement of even date herewith (the "Wisconsin Financing") with the Client in the maximum principal amount of THREE HUNDRED THOUSAND AND NO/100 Dollars (\$300,000.00) (the "Wisconsin Line of Credit"), which is to be secured by a subordinate security interest in favor of Wisconsin on all of the Client's business assets (the "Wisconsin Lien") as more fully defined in the Security Agreement between Wisconsin and the Client of even date herewith and that such security interest includes the TCL Collateral, the Thermo Inventory Collateral, and the YA Global Collateral.

The parties hereby execute this Intercreditor Agreement ("Agreement") to set forth their respective rights and obligations and affirm the following:

1. YA Global hereby consents to the Wisconsin Financing, but only upon the terms and conditions set forth herein.
2. Thermo Credit waives any limitation under the Factoring Agreement, the Line of Credit Agreement or the Thermo Security Agreement on the incurrence of indebtedness by the Client to obtain additional financing under the Wisconsin Financing.
3. Wisconsin acknowledges the validity of (a) the YA Global Obligations, the YA Global Liens, the TCL Obligations, and the TCL Liens, and (b) the YA Global Documents, the TCL Documents, the May 30 Agreement and the Tri-Party Agreement (collectively the "Financing Agreements"). This acknowledgement is not intended to and shall not otherwise modify the rights and remedies of the parties hereto under this Agreement or any of the Financing Agreements.

4. In the event any goods are returned to the Client, if such goods are returned with respect to an account receivable or inventory of the Client that is part of Thermo Inventory Collateral, then such goods shall be a part of Thermo Inventory Collateral or the TCL Collateral, as applicable. In the event any such goods are returned with respect to the YA Global Collateral such goods shall be considered a part of YA Global Collateral.
5. So long as the Financing Agreements, or any of them, remain in full force and effect and so long as any amounts shall remain due and outstanding from the Client to YA Global or Thermo Credit, Wisconsin agrees not to (a) take any action to foreclose, repossess, marshal, control or exercise any remedies with respect to the Client or its assets, (b) not to join in any petition for bankruptcy or assignment for the benefit of creditors agreement affecting the Client or any of its assets, or (c) take any other action with respect to the Client or its assets.
6. Notwithstanding the order of filing of UCC-1 Financing Statements by each of Thermo Credit, YA Global and Wisconsin with respect to the Client, so long as the Financing Agreements, or any of them, remain in full force and effect and so long as any amounts shall remain due and outstanding from the Client to YA Global or Thermo Credit, Wisconsin agrees that any lien or security interest it may have in any of the TCL Collateral, YA Global Collateral or Thermo Inventory Collateral shall be subordinate to the liens and security interests therein held by either of Thermo Credit or YA Global.
7. Any proceeds of insurance on the assets of Client shall be allocated among the parties based upon the priorities set forth in Section 11(a) herein.
8. Unless Thermo Credit and YA Global have already been repaid in full, (a) Wisconsin agrees that in the event that it receives any of the TCL Collateral, Thermo Inventory Collateral, YA Global Collateral or the proceeds thereof, Wisconsin will immediately remit the same, with appropriate endorsements, to Thermo Credit and/or YA Global, as applicable, in accordance with the priorities set forth in Section 11(a) herein.
9. Each of Thermo Credit, YA Global and Wisconsin represent and warrant to the other that they have received no other instruction with respect to payment of sums due to the Client and are aware of no other assignment of such sums. Each of the parties acknowledge and agree that any such instruction other than from the other party shall be ineffective and shall be disregarded.
10. In the event of a default by the Client with respect to the any of the agreements reflected herein, the party becoming aware of such default shall provide the other parties with notice at the same time as sent to Client. From and after the occurrence of, and during the continuance of, any event of default under the Financing Agreements, Wisconsin agrees that it shall not accept, and the Client agrees that it will not make, any payments under the Wisconsin Line of Credit.

11. In the event of a liquidation of the assets of the Client by either Thermo Credit or YA Global, the parties hereto agree as follows:
- (a) The proceeds of any such liquidation shall be distributed as follows:
- (i) The proceeds of the liquidation of inventory shall be distributed as follows:
- (A) FIRST, to Thermo Credit up to the lesser of (x) the amount of the total outstanding LOC Obligations (not to exceed \$1,000,000.00 in principal), and (y) the amount of the proceeds generated from the liquidation of the Thermo Inventory Collateral (i.e., inventory with an aggregate value of Two Million Dollars (\$2,000,000), as reported in the books and records and financial statements of the Client maintained in conformity with generally accepted accounting principles);
- (B) SECOND, to YA Global to be applied in reduction of the YA Global Obligations until YA Global has been paid in full;
- (C) THIRD, to Thermo Credit to be applied in reduction of the TCL Obligations until paid in full; and
- (D) FOURTH, to Wisconsin to be applied in reduction of the amounts due under the Wisconsin Line of Credit until paid in full.
- (ii) The proceeds of the liquidation or collection of the TCL Collateral, shall be distributed as follows:
- (A) FIRST, to Thermo Credit up to the amount of the total outstanding Factoring Obligations (not to exceed \$2,500,000.00);
- (B) SECOND, to YA Global to be applied in reduction of the YA Global Obligations until YA Global has been paid in full;
- (C) THIRD, to Thermo Credit to be applied in reduction of the TCL Obligations until paid in full; and
- (D) FOURTH, to Wisconsin to be applied in reduction of the amounts due under the Wisconsin Line of Credit until paid in full.

(iii) The proceeds of the liquidation or collection of YA Global Collateral, other than Thermo Inventory Collateral or TCL Collateral, shall be distributed as follows:

(A) FIRST, to YA Global to be applied in reduction of the YA Global Obligations until YA Global has been paid in full;

(B) SECOND, to Thermo Credit to be applied in reduction of the TCL Obligations until paid in full; and

(C) THIRD, to Wisconsin to be applied in reduction of the amounts due under the Wisconsin Line of Credit until paid in full.

(b) Unless and until the repayment in full of the TCL Obligations, Thermo Credit shall have the right to control the liquidation of the Thermo Inventory Collateral and the TCL Collateral, including, without limitation, the determination of which inventory to liquidate first, the order of any such liquidation, and the method and manner of the same. From and after the repayment of the TCL Obligations, YA Global shall have the right to control such liquidation until the YA Global Obligations are repaid in full, at which point Wisconsin shall have the right to control such liquidation.

(c) Unless and until the repayment in full of the YA Global Obligations, YA Global shall have the right to control the liquidation of the YA Global Collateral (other than the Thermo Inventory Collateral and the TCL Collateral) including, without limitation, the determination of which assets to liquidate first, the order of any such liquidation, and the method and manner of the same. From and after the repayment of the YA Global Obligations, Thermo Credit shall have the right to control such liquidation until the TCL Obligations are repaid in full, at which point Wisconsin shall have the right to control such liquidation.

(d) Wisconsin hereby agrees that a party conducting a liquidation pursuant to Section 11(a) or otherwise exercising rights as a secured creditor seeking to collect or realize upon a security interest, mortgage, or lien granted by the Client to such party shall have the authority and permission of Wisconsin to release, discharge, or dissolve the Wisconsin Lien as follows:

(i) Thermo Credit shall have the right and ability to release, discharge, or dissolve the Wisconsin Lien on the Thermo Inventory Collateral and TCL Collateral.

(ii) YA Global shall have the right and ability to release, discharge, or dissolve the Wisconsin Lien on the YA Global Collateral.

12. Nothing herein shall affect the provisions of the Financing Agreements except as specifically set forth herein. Wisconsin shall be free to modify the provisions of its agreements with the Client provided that no such modifications shall (a) increase the maximum principal amount of the Wisconsin Line of Credit beyond \$300,000.00, (ii) accelerate the amortization, or the maturity date, of the Wisconsin Line of Credit, or (iii) limit or otherwise affect the obligations specifically set forth herein. Thermo Credit and YA Global shall be free to modify the provisions of their respective agreements with the Client (subject, however, as between Thermo Credit and YA Global, to the provisions of the May 30 Agreement or the Tri-Party Agreement) provided that no such modifications shall limit or otherwise affect the obligations specifically set forth herein.
13. The agreement set forth in this letter, and all transactions contemplated hereby, shall be governed by, construed and enforced in accordance with the laws of the State of Wisconsin. The parties herein waive trial by jury and agree that in the event that litigation results from or arises out of this agreement or the performance hereof, the parties agree that the prevailing party's reasonable attorney's fees, court costs and all other expenses resulting from or connected with such litigation, whether or not taxable by the court as costs, shall be paid by the non-prevailing party(ies) (provided, however, that nothing herein shall be construed to require a party not directly involved in such dispute to pay such fees and costs), in addition to any other relief to which the prevailing party may be entitled.
14. This Agreement is an irrevocable and continuing agreement and Thermo Credit, YA Global and Wisconsin may continue to rely upon the same in providing financing and other financial accommodations to or for the benefit of the Client. In connection therewith, Wisconsin may not increase its maximum commitment to the Client under the Wisconsin Line of Credit beyond the original maximum principal amount of \$300,000 without the prior written consent of both YA Global and Thermo Credit.
15. This Agreement shall terminate (a) upon full and final payment of all amounts owing to Wisconsin by the Client and (b) termination of the Wisconsin Line of Credit and of all obligations and commitments of Wisconsin to provide financing to the Client with subsequent release of all liens held thereto. The termination of this Agreement shall have no effect on the Financing Agreements, which Financing Agreements shall continue in full force and effect upon the terms set forth therein as if this Agreement had never been executed unless and until terminated in accordance with their own terms.

If the foregoing correctly sets forth our understanding, please indicate your assent below. This letter agreement is executed as a sealed instrument as of the date first set forth above. Thank you for your assistance in this regard.

YA GLOBAL INVESTMENTS, L.P.

By: /s/ Troy Rillo
Name: Troy Rillo
Title: Senior Managing Director

THERMO CREDIT, LLC

By: /s/ Jack V. Eumont
Name: Jack V. Eumont
Its: Executive Vice President

ACCEPTED AND AGREED:

TELKONET, INC.

By: /s/ Richard J. Leimbach
Name: Richard J. Leimbach
Its: Chief Financial Officer

WISCONSIN DEPARTMENT OF COMMERCE

By: /s/ Mary Gage
Name: Mary Gage
Its: Bureau Director

[Signature Page to Intercreditor Agreement]