



2016 ANNUAL REPORT

Record-Breaking Year
Future Opportunities



NAPCO Security Technologies, Inc.

Total Security Solution for Wireless Locking, Access Control & Alarms



ALARM LOCK®
Wireless Locking &
Standalone Access & Egress



Continental Access®
Complete Platform: Access, Wireless
Locking & Security Management



MARKS USA®
Architectural Door Hardware,
Locks, Lifesafety & Exit Trim



NAPCO
Security & Fire Systems plus
Cell/IP Alarm Reporting

NAPCO Security Technologies, Inc. provides commercial and residential security through a professional dealer network of more than 10,000 security dealers, integrators, locksmiths and contractors worldwide. Its innovative, synergistic products and technologies, provide solutions in three main categories: alarms and connectivity, locking and access control and surveillance.

One of NAPCO's strong growth drivers is recurring revenue services from its cellular communicator - and connected home-brands. Among the fastest growing brands in its class, NAPCO StarLink™ Alarm Communicators report alarm signals universally from any brand of security system, in lieu of telephone landlines and 2G cell networks, both rapidly disappearing. StarLink is a proven go-to solution, ideal for millions of installed and new alarm systems, now available for residential, as well as commercial fire alarm reporting. It checks all the boxes, as it is easy to install, economical and dependably uses today's leading nationwide cellular networks, both AT&T® and Verizon Network Certified®, protecting security consumers and dealers' account bases and valuation.

On-trend for households seeking to bridge their home with increasingly mobile lifestyles, iBridge® Connected Home Services, accessible from any smart phone/tablet via an app, provides security, video and smart home automation and newly features complementary iBridge Messenger™ SMS/MMS text and video notifications. iBridge offers dealers a value-add to their NAPCO Gemini security system, for old and new accounts, providing incremental Recurring Monthly Revenue for both the installer and the Company.

Faced with escalating school violence, as a long-time trusted source in some of the largest school districts and leading colleges and universities across the country, NAPCO's divisions, Alarm Lock®, ContinentalAccess®, and Marks USA®, continue to evolve and expand their LocDown™ security solutions, to fit any classroom, campus and budget. From enterprise access control systems with integrated access control, locks, alarms, video and visitor-/threat-management to wireless networked access locks with built-in ID readers and keyfob-control; or LocDown™ mechanical locks that lock from inside the classroom, the Company makes the scalable solutions needed to

safeguard schools, students and staffers. In this same vertical, NAPCO Commercial™ security systems have gained considerable traction providing intrusion and lifesafety protection in new addressable and wireless systems and upgrade applications.

Based on the continued popularity and strengths of Alarm Lock's Trilogy Network™ Access Lock Platform, teamed with Marks' wide array of architectural hardware, the Company created the new décor-friendly ArchiTech™ Series Designer Wireless Access Control line, designed with the proven functionality for traditional corporate, healthcare and educational campuses, plus new customizable aesthetics to satisfy even the most discriminating multi-dwelling residential buildings. These locks will also offer an all new smartphone app paired with Bluetooth LE technology, for ultimate keyless user convenience and compromise-free security. Additionally, ArchiTech Locks are seamlessly integrated on Continental's enterprise class CA3000 system providing interoperable global control, real-time access, video and visitor management and a host of robust server-based advantages.

CEO Letter to Shareholders



Richard L. Soloway
Chairman, President, and CEO

Dear NAPCO Investor,

In Fiscal 2016 NAPCO set all-time records for sales, net income, and operating cash flows: a direct result of successful strategies that effectively position NAPCO to address major paradigm shifts affecting our entire society. These shifts include the growth of cellular radio communications, Internet of Things (IoT), and growing concern over school safety and security.

As a company singularly focused on the security market, NAPCO is staying ahead of a fast-changing world with scalable, end-to-end solutions that seamlessly integrate access control, electronic door locking systems, fire and burglary alarm systems, cellular alarm communicators and IoT-enabled 'smart home' solutions.

Our Company's year-over-year improvement can be measured by many financial metrics, including the following:

- Annual net revenues increased 6% to a record \$82.5 million.
- Income before taxes increased 21% to \$6.1 million.
- Net income increased 19% to \$5.8 million.
- Adjusted EBITDA* increased 13% to \$7.8 million or \$0.42 per diluted share.

*See table on inside back cover (page 51)

- Earnings per share (diluted) increased 24% to \$0.31.
- Cash flow from operating activities increased 136% to a record \$9.2 million.

Additionally, our operating leverage continues to improve as we add incremental sales while maintaining a relatively stable fixed cost structure. For example, selling, general, and administrative (SGA) expenses rose just 2% to \$21.3 million in Fiscal 2016, resulting in our operating margin improving to 15.6% during Q4 of Fiscal 2016 and 7.7% for the entire fiscal year.

Our balance sheet remains strong, as we generated more than \$9 million in operating cash flow during Fiscal 2016. The bulk of the cash was used to pay down long-term debt. As of June 30, 2016, debt, net of cash, was reduced to \$1 million from \$8.4 million in the prior year, down from a high of \$35.9 million following the acquisition of Marks USA in August of 2008. Cash flow was also used to repurchase 193,000 shares of common stock.

The rapid emergence of the IoT has heightened demand for alarms, locks, and access control devices that can be accessed via smart devices. With the largest

offering of 'smart' devices serving both consumer and commercial security markets, NAPCO's robust portfolio of innovative products and services offer compelling advantages to end-customers, allowing easy-to-install upgrades to currently installed systems made by competitors and dynamic end-market sales opportunities that deliver recurring revenue to NAPCO and its authorized dealers.

In 2016 we introduced StarLink fire and commercial communicators, available in AT&T 3G/4G and Verizon CDMA versions. StarLink communicators serve both the residential and small business market, as well as the lucrative commercial fire alarm market: offering a cost-effective way to replace outdated hard-wired phone lines along with aging 2G communicators, which will be phased out by the end of 2016.

This Fall we will be introducing the StarLink Connect controller: a universal cellular radio solution that interfaces with NAPCO brand alarm systems along with tens of millions of previously installed alarm systems made by other providers. Starlink Connect works with NAPCO's proprietary iBridge 'Connected Home' services to provide remote control of security systems, lighting, HVAC, door locks, and security camera video, from any smart device.

By offering a compelling value proposition to customers, products such as StarLink and iBridge generate recurring revenue for NAPCO and its channel partners.

Recurring revenue increased by 63% for the entire fiscal year. While still a relatively small percentage of annual revenues, recurring revenue serves a vital function of 'leveling' seasonal revenue swings, thus permitting sales forecasting to become more consistent and predictable.

As reported, violence on school and college campuses has increased. As a leading provider of comprehensive security and safety solutions for colleges, universities, and K-12 schools, NAPCO provides an unrivaled combination of in-depth product solutions, in-house manufacturing, and seamless integration capabilities. These advantages position us to win competitive bids for multi-million dollar projects aimed at enhancing school security: a market expected to reach \$4.9 billion by 2017.**

We recently introduced the School Access-control Vulnerability Index, or SAVI, a propriety audit system that rates the security preparedness of K-12 schools. The SAVI index provides a metricable benchmark for crafting customized solutions that deliver identifiably improved preparedness against the threat of

a mass incident. The SAVI index further leverages the breadth of our comprehensive product solutions for the educational marketplace, such as Alarm Lock™ and LocDown™ locking and access control solutions, Marks commercial grade lock hardware, Continental access control systems, and NAPCO burglary, intrusion, and fire alarm systems.

To enhance and focus our efforts in the school security field, we recently created a new School & Campus Safety Division, led by Byron Thurmond, who previously managed the nationally renowned security systems deployed by the Houston Independent School District, the nation's 7th largest district. The School & Campus Safety Division will concentrate its sales efforts on more than 100,000 K-12 schools and 10,000 higher-education institutions across the US, promoting comprehensive end-to-end solutions that are modular and scalable, whereas competing solutions are more difficult to integrate and maintain.

Looking to the future, I see NAPCO as primed for vibrant and sustainable growth, evidenced by strong initial demand for our latest product innovations, along with an active pipeline of new products and services that protect people and property in an increasingly dangerous world. In order to grow, we need to maintain our innovative

edge by re-investing approximately 7% of revenues to fund ongoing R&D efforts that lead to game-changing products that build brand loyalty. We also need to attract and retain top talent.

In Fiscal 2017, we expect to see continued improvement in our operating leverage, as incremental sales will contribute marginally to manufacturing-related labor costs with virtually no material impact on SG&A expenses. Assuming that business conditions remain healthy, bottom line growth could be roughly twice the rate of top line growth, creating added shareholder value.

While the major paradigm shifts discussed herein are still in their infancy, NAPCO must think ahead by assembling all the talent, resources, and IP-protected technology needed to successfully grow and defend a sizable market share. Moreover, our long-term

success demands comprehensive solutions that satisfy the demands of tech-savvy consumers.

In today's turbulent and unstable world, innovative security solutions will always be in demand. As the industry's only 'pure play' public company with an ISO-9001 certified, low-cost manufacturing center in the Dominican Republic, NAPCO has the flexibility to quickly adapt to fast-changing markets with a relatively fixed cost manufacturing infrastructure that maximizes capacity utilization and overhead absorption.

With an experienced management team, a motivated workforce, and an exceptionally loyal sales and distribution network consisting of more than 10,000 alarm dealers and 2,000 security system integrators, NAPCO is poised for long-term sustainable growth. Armed with all of these resources, as well as a growing portfolio of proprietary,

patent-protected technologies, we seek to continuously raise the bar with innovative 'breakthrough' products and services that set industry standards for innovation and excellence. This gives us a sustainable advantage in attracting and retaining channel partners.

Based on last year's financial performance, and our dynamic outlook for the future, it is evident that our long-term vision and strategies are mutually benefiting NAPCO's shareholders. We intend to accelerate this progress in FY 2017.

Once again, I would like to thank our customers, employees, channel partners, and investors for their continued confidence and support.



Richard L. Soloway
Chairman, President and CEO

* Non-GAAP Information. Certain non-GAAP measures are included in this document, including EBITDA, non-GAAP operating income and Adjusted EBITDA. We define EBITDA as GAAP net income plus income tax expense (benefit), net interest expense and depreciation and amortization expense. Non-GAAP operating income does not include impairment of goodwill, amortization of intangibles, restructuring charges, stock-based compensation expense and other infrequent or unusual charges. These non-GAAP measures are provided to enhance the user's overall understanding of our financial performance. By excluding these charges our non-GAAP results provide information to management and investors that is useful in assessing NAPCO's core operating performance and in comparing our results of operations on a consistent basis from period to period. The presentation of this information is not meant to be a substitute for the corresponding financial measures prepared in accordance with generally accepted accounting principles. Investors are encouraged to review the reconciliation of GAAP to non-GAAP financial measures included on page 51.

** Source: IHS, Inc., an Englewood, Colorado-based research company.

This letter contains statements relating to future results of the Company (including certain projections and business trends) that are "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those projected as a result of certain risks and uncertainties, including but not limited to, changes in political and economic conditions, demand for and market acceptance of new and existing products, as well as other risks and uncertainties detailed from time to time in the filings of the Company with the Securities and Exchange Commission.

Trademarks of NAPCO: NAPCO, StarLink iBridge, iBridge Messenger, iSee Video, LocDown, Lifesaver, Alarm Lock, Continental Access, Marks USA, NAPCO Commercial, Trilogy, Trilogy Networx, ArchiTech.

Trademarks of their respective companies: AT&T, Verizon Network Certified, Control4, NASDAQ

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended June 30, 2016

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 0-10004

NAPCO SECURITY TECHNOLOGIES, INC.

(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

11-2277818
(I.R.S. Employer I.D. Number)

333 Bayview Avenue, Amityville, New York
(Address of principal executive offices)

11701
(Zip Code)

Registrant's telephone number, including area code: (631) 842-9400

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

Common Stock, par value \$.01 per share
(Title of Each Class)

The NASDAQ Stock Market LLC
(Name of each exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. Yes No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "Large accelerated filer", "Accelerated filer" and "Smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

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

As of December 31, 2015, the aggregate market value of the common stock of Registrant held by non-affiliates based upon the last sale price of the stock on such date was \$69,768,521.

As of September 06, 2016, 18,786,893 shares of common stock of Registrant were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Part III incorporates information by reference from the Registrant's definitive proxy statement to be filed with the Securities and Exchange Commission in connection with the solicitation of proxies for the Registrant's 2016 Annual Meeting of Stockholders.

PART I

ITEM 1: BUSINESS.

NAPCO Security Technologies, Inc. ("NAPCO" or the "Company") was incorporated in December 1971 in the State of Delaware. Its executive offices are located at 333 Bayview Ave, Amityville NY 11701. Its telephone number is (631) 842-9400.

The Company is a diversified manufacturer of security products, encompassing access control systems, door-locking products, intrusion and fire alarm systems and video surveillance products for commercial and residential use. These products are used for commercial, residential, institutional, industrial and governmental applications, and are sold worldwide principally to independent distributors, dealers and installers of security equipment.

Website Access to Company Reports

Copies of our filings under the Securities Exchange Act of 1934 (including annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to these reports) are available free of charge on our website (www.napcosecurity.com) on the same day they are electronically filed with the Securities and Exchange Commission.

Products

The Company's products ("Products") are comprised of the following:

Access Control Systems. Access control systems consist of one or more of the following: various types of identification readers (e.g. card readers, hand scanners), a control panel, a PC-based computer and electronically activated door-locking devices. When an identification card or other identifying information is entered into the reader, the information is transmitted to the control panel/PC which then validates the data and determines whether or not to grant access by electronically deactivating the door locking device. An electronic log is kept which records various types of data regarding access activity.

The Company designs, engineers, manufactures and markets the software and control panels discussed above. It also buys and resells various identification readers, PC-based computers and various peripheral equipment for access control systems.

Door Security Products. The Company manufactures a variety of door locking devices including microprocessor-based electronic door locks with push button, card reader and bio-metric operation, door alarms, mechanical door locks and simple dead bolt locks. These devices may control a single door or, in the case of some of the Company's microprocessor-based door locks, may be networked with the Company's access control systems and controlled remotely.

Intrusion and Fire Alarm Systems. Alarm systems usually consist of various detectors, a control panel, a digital keypad and signaling equipment. When a break-in occurs, an intrusion detector senses the intrusion and activates a control panel via hard-wired or wireless transmission that sets off the signaling equipment and, in most cases, causes a bell or siren to sound. Communication equipment such as a digital communicator may be used to transmit the alarm signal to a central station or another person selected by a customer.

The Company manufactures and markets the following products for alarm systems:

Automatic Communicators. When a control panel is activated by a signal from an intrusion detector, it activates a communicator that can automatically dial one or more pre-designated telephone numbers utilizing wired ("landline") or cellular communications systems. If programmed to do so, a digital communicator dials the telephone number of a central monitoring station and communicates in computer language to a digital communicator receiver, which signals an alarm message.

Control Panels. A control panel is the "brain" of an alarm system. When activated by any one of the various types of intrusion detectors, it can activate an audible alarm and/or various types of communication devices.

Combination Control Panels/Digital Communicators and Digital Keypad Systems. A combination control panel, digital communicator and a digital keypad has continued to be the leading configuration in terms of dealer and consumer preference. Benefits of the combination format include the cost efficiency resulting from a single microcomputer function, as well as the reliability and ease of installation gained from the simplicity and sophistication of micro-computer technology.

Fire Alarm Control Panel. Multi-zone fire alarm control panels, which accommodate an optional digital communicator for reporting to a central station, are also manufactured by the Company.

Area Detectors. The Company's area detectors are both passive infrared heat detectors and combination microwave/passive infrared detectors that are linked to alarm control panels. Passive infrared heat detectors respond to the change in heat patterns caused by an intruder moving within a protected area. Combination units respond to both changes in heat patterns and changes in microwave patterns occurring at the same time.

Video Surveillance Systems. Video surveillance systems typically consist of one or more video cameras, a control panel and a video monitor or PC. More advanced systems can also include a recording device and some type of remote communication device such as an internet connection to a PC or browser-enabled cell phone. The system allows the user to monitor various locations at once while recorders save the video images for future use. Remote communication devices can allow the user to view and control the system from a remote location.

The Company designs, engineers, and markets the software and control panels discussed above. It also buys and resells various video cameras, PC-based computers and peripheral equipment for video surveillance systems.

Peripheral Equipment

The Company also markets peripheral and related equipment manufactured by other companies. Revenues from peripheral equipment have not been significant.

Research and Development

The Company's business involves a high technology element. Research and development costs incurred by the Company are charged to expense as incurred and are included in "Cost of Sales" in the consolidated statements of operations. During the fiscal years ended June 30, 2016 and 2015, the Company expended approximately \$6,169,000 and \$5,382,000, respectively, on Company-sponsored research and development activities conducted primarily by its engineering department to develop and improve the Products. The Company intends to continue to conduct a significant portion of its future research and development activities internally.

Employees

As of June 30, 2016, the Company had 984 full-time employees.

Marketing

The Company's staff of 53 sales and marketing support employees located at the Company's Amityville offices sells and markets the Products primarily to independent distributors and wholesalers of security alarm and security hardware equipment. Management estimates that these channels of distribution represented approximately 51% and 53% of the Company's total sales for the fiscal years ended June 30, 2016 and 2015, respectively. The remaining revenues are primarily from installers and governmental institutions. The Company's sales representatives periodically contact existing and potential customers to introduce new products and create demand for those as well as other Company products. These sales representatives, together with the Company's technical personnel, provide training and other services to wholesalers and distributors so that they can better service the needs of their customers. In addition to direct sales efforts, the Company advertises in technical trade publications and participates in trade shows in major United States and European cities.

In the ordinary course of the Company's business the Company grants extended payment terms to certain customers. The Company had one customer with an accounts receivable balance that comprised 22% of the Company's accounts receivable at both June 30, 2016 and 2015. Sales to this customer comprised 13% of net sales in each of the fiscal years ended June 30, 2016 and 2015. For further discussion on Concentration of Credit Risk see disclosures included in Item 1A and Item 7.

Competition

The security products industry is highly competitive. The Company's primary competitors are comprised of approximately 20 other companies that manufacture and market security equipment to distributors, dealers, central stations and original equipment manufacturers. The Company believes that no one of these competitors is dominant in the industry. Most of these companies have substantially greater financial and other resources than the Company.

The Company competes primarily on the basis of the features, quality, reliability and pricing of, and the incorporation of the latest innovative and technological advances into, its Products. The Company also competes by offering technical support services to its customers. In addition, the Company competes on the basis of its expertise, its proven products, its reputation and its ability to provide Products to customers on a timely basis. The inability of the Company to compete with respect to any one or more of the aforementioned factors could have an adverse impact on the Company's business.

Relatively low-priced "do-it-yourself" alarm system products are available to the public at retail stores. The Company believes that these products compete with the Company only to a limited extent because they appeal primarily to the "do-it-yourself" segment of the market. Purchasers of such systems do not receive professional consultation, installation, service or the sophistication that the Company's Products provide.

Seasonality

The Company's fiscal year begins on July 1 and ends on June 30. Historically, the end users of NAPCO's products want to install its products prior to the summer; therefore sales of its products historically peak in the period April 1 through June 30, the Company's fiscal fourth quarter, and are reduced in the period July 1 through September 30, the Company's fiscal first quarter. In addition, demand is affected by the housing and construction markets. Deterioration of the current economic conditions may also affect this trend.

Raw Materials

The Company prepares specifications for component parts used in the Products and purchases the components from outside sources or fabricates the components itself. These components, if standard, are generally readily available; if specially designed for the Company, there is usually more than one alternative source of supply available to the Company on a competitive basis. The Company generally maintains inventories of all critical components. The Company for the most part is not dependent on any one source for its raw materials. The Company believes that any vendor that is currently the sole source of a component can be replaced without a material impact on the Company.

Sales Backlog

In general, orders for the Products are processed by the Company from inventory. A sales backlog of approximately \$1,592,000 and \$2,044,000 existed as of June 30, 2016 and 2015, respectively. The Company expects to fill the entire backlog that existed as of June 30, 2016 during fiscal 2017.

Government Regulation

The Company's telephone dialers, microwave transmitting devices utilized in its motion detectors and any new communication equipment that may be introduced from time to time by the Company must comply with standards promulgated by the Federal Communications Commission ("FCC") in the United States and similar agencies in other countries where the Company offers such products, specifying permitted frequency bands of operation, permitted power output and periods of operation, as well as compatibility with telephone lines. Each new Product

that is subject to such regulation must be tested for compliance with FCC standards or the standards of such similar governmental agencies. Test reports are submitted to the FCC or such similar agencies for approval. Cost of compliance with these regulations has not been material.

Patents and Trademarks

The Company has been granted several patents and trademarks relating to the Products. While the Company obtains patents and trademarks as it deems appropriate, the Company does not believe that its current or future success is dependent on its patents or trademarks.

Foreign Sales

The revenues and identifiable assets attributable to the Company's domestic and foreign operations for its last two fiscal years are summarized in the following table:

<u>Financial Information Relating to Domestic and Foreign Operations</u>		
	<u>2016</u>	<u>2015</u>
	(in thousands)	
Sales to external customers(1):		
Domestic	\$79,931	\$74,736
Foreign	<u>2,582</u>	<u>3,026</u>
Total Net Sales	<u>\$82,513</u>	<u>\$77,762</u>
Identifiable assets:		
United States	\$51,272	\$50,998
Dominican Republic (2)	<u>13,497</u>	<u>14,039</u>
Total Identifiable Assets	<u>\$64,769</u>	<u>\$65,037</u>

(1) All of the Company's sales originate in the United States and are shipped primarily from the Company's facilities in the United States. There were no sales into any one foreign country in excess of 10% of total Net Sales.

(2) Consists primarily of inventories (2016 = \$10,076; 2015 = \$10,546) and fixed assets (2016 = \$3,311; 2015 = \$3,347) located at the Company's principal manufacturing facility in the Dominican Republic.

ITEM 1A: RISK FACTORS

The risks described below are among those that could materially and adversely affect the Company's business, financial condition or results of operations. These risks could cause actual results to differ materially from historical results and from any results predicted by any forward-looking statements related to conditions or events that may occur in the future.

Our Business Could Be Materially Adversely Affected as a Result of General Economic and Market Conditions

We are subject to the effects of general economic and market conditions. In the event that the U.S. or international economic conditions deteriorate, our revenue, profit and cash-flow levels could be materially adversely affected in future periods. In the event of such deterioration, many of our current or potential future customers may experience serious cash flow problems and as a result may, modify, delay or cancel purchases of our products. Additionally, customers may not be able to pay, or may delay payment of, accounts receivable that are owed to us. If such events do occur, they may result in our expenses being too high in relation to our revenues and cash flows.

We Are Dependent Upon the Efforts of Richard L. Soloway, Our Chief Executive Officer and There is No Succession Plan in Place

The success of the Company is largely dependent on the efforts of Richard L. Soloway, Chief Executive Officer. The loss of his services could have a material adverse effect on the Company's business and prospects. There is currently no succession plan to address the loss of Mr. Soloway's services.

Competitors May Develop New Technologies or Products in Advance of Us

Our business may be materially adversely affected by the announcement or introduction of new products and services by our competitors, and the implementation of effective marketing or sales strategies by our competitors. The industry in which the Company operates is characterized by constantly improved products. There can be no assurance that competitors will not develop products that are superior to the Company's products. The Company has historically invested approximately 6% to 8% of annual revenues on Research and Development to mitigate this risk. Future success will depend, in part, on our ability to continue to develop and market products and product enhancements cost-effectively. The Company's research and development expenditures are principally targeted at enhancing existing products, and to a lesser extent at developing new ones. Further, there can be no assurance that the Company will not experience additional price competition, and that such competition may not adversely affect the Company's revenues and results of operations.

Our Business Could Be Materially Adversely Affected by the Inability to Maintain Expense Levels Proportionate to Sales Volume

While expense levels relative to current sales levels result in positive net income and cash flows, if sales levels decrease significantly and we are unable to decrease expenses proportionately, our business may be adversely affected.

Our Business Could Be Materially Adversely Affected as a Result of Housing and Commercial Building Market Conditions

We are subject to the effects of housing and commercial building market conditions. If these conditions deteriorate, resulting in declines in new housing or commercial building starts, existing home or commercial building sales or renovations, our business, results of operations or financial condition could be materially adversely affected, particularly in our intrusion and door locking product lines.

Our Business Could Be Materially Adversely Affected as a Result of Lessening Demand in the Security Market

Our revenue and profitability depend on the overall demand for our products. Delays or reductions in spending, domestically or internationally, for electronic security systems could materially adversely affect demand for our products, which could result in decreased revenues or earnings.

The Markets We Serve Are Highly Competitive and We May Be Unable to Compete Effectively

We compete with approximately 20 other companies that manufacture and market security equipment to distributors, dealers, control stations and original equipment manufacturers. Some of these companies may have substantially greater financial and other resources than the Company. The Company competes primarily on the basis of the features, quality, reliability and pricing of, and the incorporation of the latest innovative and technological advances into, its products. The Company also competes by offering technical support services to its customers. In addition, the Company competes on the basis of its expertise, its proven products, its reputation and its ability to provide products to customers on a timely basis. The inability of the Company to compete with respect to any one or more of the aforementioned factors could have an adverse impact on the Company's business.

Our Business Could be Materially Adversely Affected as a Result of Offering Extended Payment Terms to Customers

We regularly grant credit terms beyond 30 days to certain customers. These terms are offered in an effort to keep a full line of our products in-stock at our customers' locations. The longer the terms that are granted, the more risk is inherent in collection of those receivables. We believe that our Bad Debt reserves are adequate to account for this inherent risk.

We Rely On Distributors To Sell Our Products And Any Adverse Change In Our Relationship With Our Distributors Could Result In A Loss Of Revenue And Harm Our Business.

We distribute our products primarily through independent distributors and wholesalers of security alarm and security hardware equipment. Our distributors and wholesalers also sell our competitors' products, and if they favor our competitors' products for any reason, they may fail to market our products as effectively or to devote resources necessary to provide effective sales, which would cause our results to suffer. In addition, the financial health of these distributors and wholesalers and our continuing relationships with them are important to our success. Some of these distributors and wholesalers may be unable to withstand adverse changes in business conditions. Our business could be seriously harmed if the financial condition of some of these distributors and wholesalers substantially weakens.

Members of Management and Certain Directors Beneficially Own a Substantial Portion of the Company's Common Stock and May Be in a Position to Determine the Outcome of Corporate Elections

Richard L. Soloway, our Chief Executive Officer, members of management and the Board of Directors beneficially own approximately 37% of the currently outstanding shares of Common Stock. By virtue of such ownership and their positions with NAPCO, they may have the practical ability to determine the election of all directors and control the outcome of substantially all matters submitted to NAPCO's stockholders.

In addition, NAPCO has a staggered Board of Directors. Such concentration of ownership and the staggered Board could have the effect of making it more difficult for a third party to acquire, or discourage a third party from seeking to acquire, control of NAPCO.

Our Business Could be Materially Adversely Affected by Adverse Tax Consequences of Offshore Operations

We operate on a global basis, with a portion of our operating income generated outside the United States.

We intend to reinvest these earnings in our foreign operations indefinitely, except where we are able to repatriate these earnings to the United States without material incremental tax provision. A significant portion of our assets that result from these earnings remain outside the United States. If these indefinitely reinvested earnings were repatriated into the United States as dividends, we would be subject to additional taxes.

Our Business Could Be Materially Adversely Affected as a Result of the Inability to Maintain Adequate Financing

Our business is dependent on maintaining adequate levels of financing used to fund operations and capital expenditures. The current debt facilities provide for quarterly principal debt repayments of approximately \$75,000 plus interest as well as certain financial covenants relating to ratios affected by profit, asset and debt levels. If the Company's profits, asset or cash-flow levels decline below the minimums required to meet these covenants or to make the minimum debt payments, the Company may be materially adversely affected. Effects on the Company could include higher interest costs, reduction in borrowing availability or revocation of these credit facilities.

Our Business Could Be Materially Adversely Affected by a weakening of the US Dollar against the Dominican Peso

We are exposed to foreign currency risks due to our operations in the Dominican Republic. We have significant operations in the Dominican Republic which are denominated in Dominican pesos. We are subject to the risk that currency exchange rates between the United States and the Dominican Republic will fluctuate significantly, potentially resulting in an increase in some of our expenses when US dollars are transferred to Dominican pesos to pay these expenses.

ITEM 1B: UNRESOLVED STAFF COMMENTS.

Not applicable.

ITEM 2: PROPERTIES.

The Company owns executive offices and production and warehousing facilities at 333 Bayview Avenue, Amityville, New York. This facility consists of a fully-utilized 90,000 square foot building on a six acre plot. This six-acre plot provides the Company with space for expansion of office, manufacturing and storage capacities. These facilities are pledged as security in the Company's credit facilities with its primary bank.

The Company's foreign subsidiary located in the Dominican Republic, NAPCO DR, S.A. (formerly known as NAPCO/Alarm Lock Grupo International, S.A.), owns a building of approximately 167,000 square feet of production and warehousing space in the Dominican Republic. That subsidiary also leases the land associated with this building under a 99-year lease expiring in the year 2092 at an annual cost of approximately \$288,000. As of June 30, 2016, a majority of the Company's products were manufactured at this facility, utilizing U.S. quality control standards.

Management believes that these facilities are more than adequate to meet the needs of the Company in the foreseeable future.

ITEM 3: LEGAL PROCEEDINGS.

There are no pending or threatened material legal proceedings to which NAPCO or its subsidiaries or any of their property is subject.

In the normal course of business, the Company is a party to claims and/or litigation. Management believes that the settlement of such claims and/or litigation, considered in the aggregate, will not have a material adverse effect on the Company's financial position and results of operations.

ITEM 4: MINE SAFETY DISCLOSURE.

Not Applicable.

PART II

ITEM 5: MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

Principal Market

NAPCO's Common Stock is traded on the NASDAQ Stock Market, Global Market System, under the symbol NSSC.

The tables set forth below reflect the range of high and low sales of the Common Stock in each quarter of the past two fiscal years as reported by the NASDAQ Global Market System.

		<u>Quarter Ended Fiscal 2016</u>		
Common Stock	<u>Sept. 30</u>	<u>Dec. 31</u>	<u>March 31</u>	<u>June 30</u>
High	\$6.09	\$7.33	\$6.32	\$6.64
Low	\$5.47	\$5.41	\$5.18	\$5.57
		<u>Quarter Ended Fiscal 2015</u>		
Common Stock	<u>Sept. 30</u>	<u>Dec. 31</u>	<u>March 31</u>	<u>June 30</u>
High	\$5.43	\$4.78	\$5.82	\$6.09
Low	\$4.33	\$4.07	\$4.63	\$5.03

Approximate Number of Security Holders

The number of holders of record of NAPCO's Common Stock as of September 06, 2016 was 96 (such number does not include beneficial owners of stock held in nominee name).

Dividend Information

NAPCO has declared no cash dividends during the past two years with respect to its Common Stock. Any cash dividends must be approved by the Company's lenders.

Equity Compensation Plan Information as of June 30, 2016

PLAN CATEGORY	NUMBER OF SECURITIES TO BE ISSUED UPON EXERCISE OF OUTSTANDING OPTIONS (a)	WEIGHTED AVERAGE EXERCISE PRICE OF OUTSTANDING OPTIONS (b)	NUMBER OF SECURITIES REMAINING AVAILABLE FOR FUTURE ISSUANCE (EXCLUDING SECURITIES REFLECTED IN COLUMN (a) (c)
Equity compensation plans approved by security holders:	250,000 (1)	\$5.76	852,500 (2)
Equity compensation plans not approved by security holders:	—	—	—
Total	250,000 (1)	\$5.76	852,500 (2)

(1) The 2002 Employee Stock Option Plan expired in 2012. 102,500 options are outstanding under the 2002 Plan. No further options may be granted under this plan.

(2) In December 2012, the stockholders approved the 2012 Employee Stock Option Plan which authorizes the granting of awards, the exercise of which would allow up to an aggregate of 950,000 shares of the Company's common stock to be acquired by the holders of such awards. In December 2012, the stockholders also approved the 2012 Non-Employee Stock Option Plan which authorizes the granting of awards, the exercise of which would allow up to an aggregate of 50,000 shares of the Company's common stock to be acquired by the holders of such awards.

ITEM 6: SELECTED FINANCIAL DATA.

The table below summarizes selected financial information. For further information, refer to the audited consolidated financial statements and the notes thereto beginning on page FS-1 of this report.

	Fiscal Year Ended and at June 30				
	(In thousands, except share and per share data)				
	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
<u>Statement of earnings data:</u>					
Net Sales	\$82,513	\$77,762	\$74,382	\$71,386	\$70,928
Gross Profit	27,584	26,047	23,713	21,724	21,152
Income from Operations	6,323	5,281	4,316	3,717	3,761
Net Income	5,773	4,845	3,476	3,021	2,286
<u>Cash Flow Data:</u>					
Net cash flows provided by operating activities	9,160	3,887	4,743	4,899	4,096
Net cash flows used in investing activities	(693)	(730)	(753)	(383)	(606)
Net cash flows used in financing activities	(7,008)	(3,294)	(4,736)	(4,266)	(3,588)
<u>Per Share Data:</u>					
Net earnings per common share:					
Basic	\$0.31	\$0.25	\$0.18	\$0.16	\$0.12
Diluted	\$0.31	\$0.25	\$0.18	\$0.16	\$0.12
Weighted average common shares outstanding:					
Basic	18,874,000	19,164,000	19,392,000	19,210,000	19,096,000
Diluted	18,894,000	19,169,000	19,428,000	19,362,000	19,303,000
Cash Dividends declared per common share (1)	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
<u>Balance sheet data:</u>					
Working capital (2)	\$36,888	\$35,590	\$33,436	\$33,221	\$32,205
Total assets	64,769	65,037	63,364	63,903	64,750
Long-term debt	4,500	9,100	10,200	14,800	18,657
Stockholders' equity	51,273	46,504	43,752	40,335	37,723

(1) The Company has never paid a dividend on its common stock.

(2) Working capital is calculated by deducting Current Liabilities from Current Assets.

ITEM 7: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

The Company is a diversified manufacturer of security products, encompassing access control systems, door security products, intrusion and fire alarm systems and video surveillance products for commercial and residential use. These products are used for commercial, residential, institutional, industrial and governmental applications, and are sold worldwide principally to independent distributors, dealers and installers of security equipment. International sales accounted for approximately 3% and 4% of our revenues for the fiscal years ended June 30, 2016 and 2015, respectively.

The Company owns and operates manufacturing facilities in Amityville, New York and the Dominican Republic. A significant portion of our operating costs are fixed, and do not fluctuate with changes in production levels or utilization of our manufacturing capacity. As production levels rise and factory utilization increases, the fixed costs are spread over increased output, which may contribute to increasing profit margins. Conversely, when production levels decline our fixed costs are spread over reduced levels, which may contribute to decreasing margins.

The security products market is characterized by constant incremental innovation in product design and manufacturing technologies. Generally, the Company devotes 6-8% of revenues to research and development (R&D) on an annual basis. The Company does not expect products resulting from our R&D investments in fiscal 2016 to contribute materially to revenue during fiscal 2016, but should benefit the Company over future years. In general, the new products introduced by the Company are initially shipped in limited quantities, and increase over time. Prices and manufacturing costs tend to decline over time as products and technologies mature.

Economic and Other Factors

We are subject to the effects of general economic and market conditions. In the event that the U.S. or international economic conditions deteriorate, our revenue, profit and cash-flow levels could be materially adversely affected in future periods. In the event of such deterioration, many of our current or potential future customers may experience serious cash flow problems and as a result may, modify, delay or cancel purchases of our products. Additionally, customers may not be able to pay, or may delay payment of, accounts receivable that are owed to us. If such events do occur, they may result in our expenses being too high in relation to our revenues and cash flows.

Seasonality

The Company's fiscal year begins on July 1 and ends on June 30. Historically, the end users of NAPCO's products want to install its products prior to the summer; therefore sales of its products historically peak in the period April 1 through June 30, the Company's fiscal fourth quarter, and are reduced in the period July 1 through September 30, the Company's fiscal first quarter. In addition, demand is affected by the housing and construction markets. Deterioration of the current economic conditions may also affect this trend.

Critical Accounting Policies and Estimates

The Company's significant accounting policies are fully described in Note 1 to the Company's consolidated financial statements included in its 2016 Annual Report on Form 10-K. Management believes the following critical accounting policies, among others, affect its more significant judgments and estimates used in the preparation of its consolidated financial statements.

Revenue Recognition

The Company recognizes revenue when the following criteria are met: (i) persuasive evidence of an agreement exists, (ii) there is a fixed and determinable price for the Company's product or service, (iii) shipment and passage of title occurs or service has been provided, and (iv) collectability is reasonably assured. Revenues from product sales are recorded at the time the product is shipped or delivered to the customer pursuant to the terms of the sale. Revenues for services are recorded at the time the service is provided to the customer pursuant to the

terms of sale. The Company reports its sales on a net sales basis, with net sales being computed by deducting from gross sales the amount of actual sales returns and other allowances and the amount of reserves established for anticipated sales returns and other allowances.

The Company analyzes sales returns and is able to make reasonable and reliable estimates of product returns based on the Company's past history. Estimates for sales returns are based on several factors including actual returns and based on expected return data communicated to it by its customers. Accordingly, the Company believes that its historical returns analysis is an accurate basis for its allowance for sales returns. Actual results could differ from those estimates.

Concentration of Credit Risk

An entity is more vulnerable to concentrations of credit risk if it is exposed to risk of loss greater than it would have had if it mitigated its risk through diversification of customers. Such risks of loss manifest themselves differently, depending on the nature of the concentration, and vary in significance. The Company had one customer with an accounts receivable balance that comprised 22% of the Company's accounts receivable at both June 30, 2016 and 2015. Sales to this customer comprised 13% of net sales in each of the fiscal years ended June 30, 2016 and 2015.

In the ordinary course of business, we have established a reserve for doubtful accounts and customer deductions in the amount of \$145,000 and \$175,000 as of June 30, 2016 and 2015, respectively. Our reserve for doubtful accounts is a subjective critical estimate that has a direct impact on reported net earnings. This reserve is based upon the evaluation of accounts receivable agings, specific exposures and historical or anticipated events.

Inventories

Inventories are valued at the lower of cost or fair market value, with cost being determined on the first-in, first-out (FIFO) method. The reported net value of inventory includes finished saleable products, work-in-process and raw materials that will be sold or used in future periods. Inventory costs include raw materials, direct labor and overhead. The Company's overhead expenses are applied based, in part, upon estimates of the proportion of those expenses that are related to procuring and storing raw materials as compared to the manufacture and assembly of finished products. These proportions, the method of their application, and the resulting overhead included in ending inventory, are based in part on subjective estimates and actual results could differ from those estimates.

In addition, the Company records an inventory obsolescence reserve, which represents the difference between the cost of the inventory and its estimated market value, based on various product sales projections. This reserve is calculated using an estimated obsolescence percentage applied to the inventory based on age, historical trends, requirements to support forecasted sales, and the ability to find alternate applications of its raw materials and to convert finished product into alternate versions of the same product to better match customer demand. There is inherent professional judgment and subjectivity made by both production and engineering members of management in determining the estimated obsolescence percentage. In addition, and as necessary, the Company may establish specific reserves for future known or anticipated events. The Company also regularly reviews the period over which its inventories will be converted to sales. Any inventories expected to convert to sales beyond 12 months from the balance sheet date are classified as non-current.

Intangible Assets

The Company evaluates its Intangible Assets for impairment at least on an annual basis and will evaluate them earlier if there are indicators of a potential impairment. Those intangible assets that are classified as goodwill or as other intangibles with indefinite lives are not amortized. Impairment testing is performed in two steps: (i) the Company determines if there is impairment by comparing the fair value of a reporting unit with its carrying value, and (ii) if there is impairment, the Company measures the amount of impairment loss by comparing the implied fair value of intangible assets with the carrying amount of the intangible assets.

Income Taxes

The Company has identified the United States and New York State as its major tax jurisdictions. The fiscal 2012 and forward years are still open for examination.

For the year ended June 30, 2016, the Company recognized a net income tax expense of \$371,000. During the year ending June 30, 2016 the Company increased its reserve for uncertain income tax positions by \$46,000. The Company's practice is to recognize interest and penalties related to income tax matters in income tax expense and accrued income taxes. As of June 30, 2016, the Company had accrued interest totaling \$0 and \$148,000 of unrecognized net tax benefits that, if recognized, would favorably affect the Company's effective income tax rate in any future period. The Company uses the flow through method to account for investment tax credits earned on eligible research and development expenditures. Under this method, the investment tax credits are recognized as a reduction to income tax expense.

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred income tax expense represents the change during the period in the deferred tax assets and deferred tax liabilities. The components of the deferred tax assets and liabilities are individually classified as current and non-current based on their characteristics. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The Company measures and recognizes the tax implications of positions taken or expected to be taken in its tax returns on an ongoing basis.

Liquidity and Capital Resources

The Company's cash on hand as of June 30, 2015 combined with proceeds from operating activities during fiscal 2016 were adequate to meet the Company's capital expenditure needs and debt obligations during fiscal 2016. The Company's primary internal source of liquidity is the cash flow generated from operations. The primary source of external financing is a revolving credit facility of \$11,000,000 (the "Revolving Credit Facility") which expires in June 2021. As of June 30, 2016, \$2,000,000 was outstanding under this revolving line of credit. As of June 30, 2016, the Company's unused sources of funds consisted principally of \$3,805,000 in cash and \$9,000,000 unused balance available under its revolving line of credit.

During the year ended June 30, 2016 the Company utilized its cash on hand at June 30, 2015 (\$2,346,000) and a portion of its cash from operations (\$5,355,000 of \$9,160,000) to repay outstanding debt (\$5,900,000), purchase treasury stock (\$1,108,000) and purchase property, plant and equipment (\$693,000).

As of June 30, 2016, long-term debt consisted of a revolving credit facility of \$11,000,000 (the "Revolving Credit Facility") which expires in June 2021 and one term loan for \$6,000,000 which expires in June 2019 (the "Term Loan"). The Revolving Credit Facility had an expiration date of June 2017 which was extended to June 2021 at the end of fiscal 2016. Repayment of the Term Loan commenced on September 30, 2012. The Term Loan is being repaid with 28 equal, quarterly payments of \$75,000 and the remaining balance of \$1,900,000 due on or before the expiration date. As of June 30, 2016, the Company had \$2,000,000 in outstanding borrowings and \$9,000,000 in availability under the Revolving Credit Facility and \$2,800,000 outstanding under the Term Loan. The Company's long-term debt is described more fully in Note 6 to the condensed consolidated financial statements.

The agreements contain various restrictions and covenants including, among others, restrictions on payment of dividends, restrictions on borrowings and compliance with certain financial ratios, as defined in the restated agreement.

Outstanding balances and interest rates as of June 30, 2016 and June 30, 2015 are as follows:

	June 30, 2016		June 30, 2015	
	Outstanding	Interest Rate	Outstanding	Interest Rate
Revolving line of credit	\$2,000	1.6%	\$3,000	1.7%
Term loans	2,800	1.6%	7,700	1.7%
Total debt	<u>\$4,800</u>	<u>1.6%</u>	<u>\$10,700</u>	<u>1.7%</u>

The Company believes its current working capital, anticipated cash flows from operations and its revolving credit agreement will be sufficient to fund the Company's operations through at least the next twelve months.

The Company takes into consideration several factors in measuring its liquidity, including the ratios set forth below:

	As of June 30,	
	2016	2015
Current Ratio	5.1 to 1	4.8 to 1
Sales to Receivables	4.3 to 1	4.3 to 1
Total debt to equity	.09 to 1	.23 to 1

As of June 30, 2016, the Company had no material commitments for capital expenditures or inventory purchases other than purchase orders issued in the normal course of business. On April 26, 1993, the Company's foreign subsidiary entered into a 99-year land lease of approximately 4 acres of land in the Dominican Republic, on which the Company's principle manufacturing facility is located, at an annual cost of approximately \$288,000.

Working Capital. Working capital increased by \$1,298,000 to \$36,888,000 at June 30, 2016 from \$35,590,000 at June 30, 2015. Working capital is calculated by deducting Current Liabilities from Current Assets.

Accounts Receivable. Accounts Receivable increased by \$1,018,000 to \$19,012,000 at June 30, 2016 as compared to \$17,994,000 at June 30, 2015. The increase in Accounts Receivable was due primarily to an increase in sales for the quarter ended June 30, 2016 as compared to the same quarter a year ago.

Inventories. Inventories, which include both current and non-current portions, decreased by \$1,533,000 to \$25,337,000 at June 30, 2016 as compared to \$26,870,000 at June 30, 2015. The decrease was due primarily to the Company increasing stock of several of its new products at the end of fiscal 2015. The initial rollout of these new products and the fulfillment of these orders were completed during fiscal 2016, allowing the Company to reduce its inventory.

Accounts Payable and Accrued Expenses. Accounts payable and accrued expenses increased by \$860,000 to \$8,688,000 as of June 30, 2016 as compared to \$7,828,000 at June 30, 2015. This increase is primarily due to the higher sales volume in the fourth quarter of fiscal 2016 as compared to fiscal 2015. This increase resulted in the Company increasing purchases of raw materials at the end of fiscal 2016 in order to restock its finished goods inventory.

Off-Balance Sheet Arrangements

The Company does not maintain any off-balance sheet arrangements.

Contractual Obligations

The following table summarizes the Company's contractual obligations by fiscal year:

Contractual obligations	Payments due by period:				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Long-term debt obligations	\$4,800,000	\$300,000	\$2,500,000	\$2,000,000	\$ --
Land lease (76 years remaining) (1)	21,888,000	288,000	576,000	576,000	20,448,000
Operating lease obligations	59,000	23,000	36,000	--	--
Other long-term obligations (employment agreements) (1)	2,092,000	1,311,000	781,000	--	--
Total	\$28,839,000	\$1,922,000	\$3,893,000	\$2,576,000	\$20,448,000

(1) See footnote 10 to the accompanying consolidated financial statements.

Results of Operations

Fiscal 2016 Compared to Fiscal 2015

	Fiscal year ended June 30,		% Increase/ (decrease)
	2016	2015	
Net sales	\$82,513	\$77,762	6.1%
Gross profit	27,584	26,047	5.9%
Gross profit as a % of net sales	33.4%	33.5%	(0.3)%
Selling, general and administrative	21,261	20,766	2.4%
Selling, general and administrative as a % of net sales	25.8%	26.7%	(3.4)%
Income from operations	6,323	5,281	19.7%
Interest expense, net	179	215	(16.7)%
Other expense, net	--	5	(100.0)%
Provision for income taxes	371	216	71.8%
Net income	5,773	4,845	19.2%

Net sales in fiscal 2016 increased by \$4,751,000 to \$82,513,000 as compared to \$77,762,000 in fiscal 2015. The increase in net sales was primarily due to increased sales of the Company's NAPCO brand intrusion products (\$2,676,000), Alarm Lock brand door-locking products (\$253,000), and Marks brand door-locking products (\$2,947,000) and was partially offset by decreases in the Company's Continental brand access control products (\$1,125,000).

The Company's gross profit increased by \$1,537,000 to \$27,584,000 or 33.4% of net sales in fiscal 2016 as compared to \$26,047,000 or 33.5% of net sales in fiscal 2015. Gross profit was primarily affected by the increase in net sales as discussed above as partially offset by increased Research and Development expenditures which are included in Cost of Sales.

Selling, general and administrative expenses for fiscal 2016 increased by \$495,000 to \$21,261,000 as compared to \$20,766,000 in fiscal 2015. Selling, general and administrative expenses as a percentage of net sales decreased to

25.8% in fiscal 2016 from 26.7% in fiscal 2015. The increases in dollars resulted primarily from increases in selling wages and commissions as well as increased advertising and tradeshow expenditures. The Company increased expenditures in these areas in order to generate higher sales. The decrease as a percentage of net sales was due primarily to Net sales increasing at a higher rate than Selling, general and administrative expenses.

Interest expense for fiscal 2016 decreased by \$36,000 to \$179,000 from \$215,000 for the same period a year ago. The decrease in interest expense is primarily the result of the Company's reduction of its outstanding borrowings under its revolving line of credit and its term loan.

Other expenses remained relatively constant at \$0 and \$5,000 for fiscal 2016 and 2015, respectively.

The Company's provision for income taxes for fiscal 2016 increased by \$155,000 to \$371,000 as compared to \$216,000 for the same period a year ago. The increase in income taxes from fiscal 2015 to fiscal 2016 resulted primarily from the higher pre-tax income in fiscal 2016 as compared to fiscal 2015 as well as a benefit recognized in fiscal 2015 resulting from R&D Credits and a decrease in certain of the Company's income tax reserves.

Net income for fiscal 2016 increased by \$928,000 to \$5,773,000 as compared to \$4,845,000 in fiscal 2015. This resulted primarily from the items discussed above.

Forward-looking Information

This Annual Report on Form 10-K and the information incorporated by reference may include "Forward-Looking Statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Exchange Act of 1934. The Company intends the Forward-Looking Statements to be covered by the Safe Harbor Provisions for Forward-Looking Statements. All statements regarding the Company's expected financial position and operating results, its business strategy, its financing plans and the outcome of any contingencies are Forward-Looking Statements. The Forward-Looking Statements are based on current estimates and projections about our industry and our business. Words such as "anticipates," "expects," "intends," "plans," "believes," "seeks," "estimates," or variations of such words and similar expressions are intended to identify such Forward-Looking Statements. The Forward-Looking Statements are subject to risks and uncertainties that could cause actual results to differ materially from those set forth or implied by any Forward-Looking Statements. For example, the Company is highly dependent on its Chief Executive Officer for strategic planning. If he is unable to perform his services for any significant period of time, the Company's ability to grow could be adversely affected. In addition, factors that could cause actual results to differ materially from the Forward-Looking Statements include, but are not limited to, uncertain economic, military and political conditions in the world, our ability to maintain and develop competitive products, adverse tax consequences of offshore operations, the ability to maintain adequate financing and significant fluctuations in the exchange rate between the Dominican Peso and the U.S. Dollar. The Company's Risk Factors are discussed in more detail in Item 1A.

ITEM 7A: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's principal financial instrument is long-term debt (consisting of a revolving credit facility and term loan) that provides for interest based on the prime rate or LIBOR as described in the agreement. The Company is affected by market risk exposure primarily through the effect of changes in interest rates on amounts payable by the Company under these credit facilities. At June 30, 2016, an aggregate principal amount of approximately \$4,800,000 was outstanding under the Company's credit facilities with a weighted average interest rate of approximately 1.6%. If principal amounts outstanding under the Company's credit facilities remained at this level for an entire year and the interest rate increased or decreased, respectively, by 1% the Company would pay or save, respectively, an additional \$48,000 in interest that year.

All foreign sales transactions by the Company are denominated in U.S. dollars. As such, the Company has shifted foreign currency exposure onto its foreign customers. As a result, if exchange rates move against foreign customers, the Company could experience difficulty collecting unsecured accounts receivable, the cancellation of existing orders or the loss of future orders. The foregoing could materially adversely affect the Company's business, financial

condition and results of operations. We are also exposed to foreign currency risk relative to expenses incurred in Dominican Pesos ("RD\$"), the local currency of the Company's production facility in the Dominican Republic. The result of a 10% strengthening or weakening in the U.S. dollar to the RD\$ would result in an annual increase or decrease in income from operations of approximately \$630,000.

ITEM 8: FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

a. Financial Statements: Financial statements required pursuant to this Item are presented on pages FS-1 through FS-25 of this report as follows:

NAPCO SECURITY TECHNOLOGIES, INC. AND SUBSIDIARIES

	<u>Page</u>
Report of Independent Registered Public Accounting Firm	FS-1
Consolidated Financial Statements:	
Consolidated Balance Sheets as of June 30, 2016 and 2015	FS-2
Consolidated Statements of Income for the Fiscal Years Ended June 30, 2016 and 2015	FS-4
Consolidated Statements of Stockholders' Equity for the Fiscal Years Ended June 30, 2016 and 2015	FS-5
Consolidated Statements of Cash Flows for the Fiscal Years Ended June 30, 2016 and 2015	FS-6
Notes to Consolidated Financial Statements	FS-7

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders, Audit Committee and Board of Directors
Napco Security Technologies, Inc. and Subsidiaries
Amityville, New York

We have audited the accompanying consolidated balance sheets of Napco Security Technologies, Inc. and Subsidiaries (the "Company") as of June 30, 2016 and 2015, and the related consolidated statements of income, stockholders' equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of its internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Napco Security Technologies, Inc. and Subsidiaries as of June 30, 2016 and 2015 and the results of their operations and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ BAKER TILLY VIRCHOW KRAUSE, LLP

New York, New York
September 8, 2016

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NAPCO SECURITY TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

June 30, 2016 and 2015
(In Thousands)

	<u>2016</u>	<u>2015</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$3,805	\$2,346
Accounts receivable, net of reserves and allowances	19,012	17,994
Inventories	21,428	22,757
Prepaid expenses and other current assets	936	1,046
Deferred income taxes	<u>703</u>	<u>880</u>
Total Current Assets	45,884	45,023
Inventories - non-current	3,909	4,113
Deferred income taxes	436	634
Property, plant and equipment, net	6,049	6,234
Intangible assets, net	8,357	8,886
Other assets	<u>134</u>	<u>147</u>
 TOTAL ASSETS	 <u><u>\$64,769</u></u>	 <u><u>\$65,037</u></u>

See accompanying notes to consolidated financial statements.

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NAPCO SECURITY TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

June 30, 2016 and 2015
(In Thousands, Except Share Data)

LIABILITIES AND STOCKHOLDERS' EQUITY

	2016	2015
CURRENT LIABILITIES		
Current maturities of long term debt	\$300	\$1,600
Accounts payable	4,328	3,954
Accrued expenses	1,893	1,624
Accrued salaries and wages	2,467	2,250
Accrued income taxes	8	5
Total Current Liabilities	8,996	9,433
Long-term debt, net of current maturities	4,500	9,100
Total Liabilities	13,496	18,533
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY		
Common Stock, par value \$0.01 per share; 40,000,000 shares authorized; 21,116,743 and 21,049,243 shares issued; and 18,786,893 and 18,966,028 shares outstanding, respectively	211	210
Additional paid-in capital	16,622	16,133
Retained earnings	46,172	40,399
	63,005	56,742
Less: Treasury Stock, at cost (2,329,850 and 2,083,215 shares, respectively)	(11,732)	(10,238)
TOTAL STOCKHOLDERS' EQUITY	51,273	46,504
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$64,769	\$65,037

See accompanying notes to consolidated financial statements.

NAPCO SECURITY TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

Years Ended June 30, 2016 and 2015
(In Thousands, Except Share and Per Share Data)

	2016	2015
Net sales	\$82,513	\$77,762
Cost of sales	54,929	51,715
Gross Profit	27,584	26,047
Selling, general, and administrative expenses	21,261	20,766
Operating Income	6,323	5,281
Other expense:		
Interest expense, net	179	215
Other, net	--	5
	179	220
Income before Provision for Income Taxes	6,144	5,061
Provision for Income Taxes	371	216
Net Income	\$5,773	\$4,845
Income per share:		
Basic	\$0.31	\$0.25
Diluted	\$0.31	\$ 0.25
Weighted average number of shares outstanding:		
Basic	18,874,000	19,164,000
Diluted	18,894,000	19,169,000

See accompanying notes to consolidated financial statements.

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NAPCO SECURITY TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

Years Ended June 30, 2016 and 2015
(In Thousands, Except Share Data)

	Common Stock			Treasury Stock		Retained Earnings	Total
	Number of Shares Issued	Amount	Additional Paid-in Capital	Number of Shares	Amount		
BALANCE June 30, 2014	21,049,243	\$210	\$16,032	(1,630,167)	\$(8,044)	\$35,554	\$43,752
Repurchase of Treasury Shares	--	--	--	(453,048)	(2,194)	--	(2,194)
Stock-based compensation expense	--	--	101	--	--	--	101
Net income	--	--	--	--	--	4,845	4,845
BALANCE June 30, 2015	21,049,243	\$210	\$16,133	(2,083,215)	\$(10,238)	\$40,399	\$46,504
Repurchase of Treasury Shares	--	--	--	(192,767)	(1,108)	--	(1,108)
Stock Options Exercised	67,500	1	386	(53,868)	(386)	--	1
Stock-based compensation expense	--	--	103	--	--	--	103
Net income	--	--	--	--	--	5,773	5,773
BALANCE June 30, 2016	<u>21,116,743</u>	<u>\$211</u>	<u>\$16,622</u>	<u>(2,329,850)</u>	<u>\$(11,732)</u>	<u>\$46,172</u>	<u>\$51,273</u>

See accompanying notes to consolidated financial statements.

NAPCO SECURITY TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended June 30, 2016 and 2015 (In Thousands)

	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$5,773	\$4,845
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,420	1,570
Charge to obsolescence reserve	(455)	(472)
Provision for doubtful accounts	(30)	66
Deferred income taxes	375	230
Non-cash stock based compensation expense	103	101
Changes in operating assets and liabilities:		
Accounts receivable	(988)	(1,156)
Inventories	1,988	(1,388)
Prepaid expenses and other current assets	110	(57)
Income tax receivable	--	121
Other assets	--	6
Accounts payable, accrued expenses, accrued salaries and wages, accrued income taxes	864	21
Net Cash Provided by Operating Activities	9,160	3,887
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property, plant, and equipment	(693)	(730)
Net Cash Used in Investing Activities	(693)	(730)
CASH FLOWS FROM FINANCING ACTIVITIES		
Principal payments on long-term debt	(5,900)	(1,600)
Proceeds from long-term debt	--	500
Cash paid for purchase of treasury stock	(1,108)	(2,194)
Net Cash Used in Financing Activities	(7,008)	(3,294)
Net Change in Cash and Cash Equivalents	1,459	(137)
CASH AND CASH EQUIVALENTS - Beginning	2,346	2,483
CASH AND CASH EQUIVALENTS - Ending	\$3,805	\$2,346
SUPPLEMENTAL CASH FLOW INFORMATION		
Interest paid, net	\$184	\$215
Income taxes paid	\$ --	\$29
Surrender of Common Shares	\$ 54	\$ --

See accompanying notes to consolidated financial statements.

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NAPCO SECURITY TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - Nature of Business and Summary of Significant Accounting Policies

Nature of Business:

NAPCO Security Technologies, Inc. and Subsidiaries (the "Company") is a diversified manufacturer of security products, encompassing access control systems, door-locking products, intrusion and fire alarm systems and video surveillance products for commercial and residential use. These products are used for commercial, residential, institutional, industrial and governmental applications, and are sold worldwide principally to independent distributors, dealers and installers of security equipment.

The Company's fiscal year begins on July 1 and ends on June 30. Historically, the end users of the Company's products want to install its products prior to the summer; therefore sales of its products historically peak in the period April 1 through June 30, the Company's fiscal fourth quarter, and are reduced in the period July 1 through September 30, the Company's fiscal first quarter. In addition, demand is affected by the housing and construction markets.

Significant Accounting Policies:

Principles of Consolidation

The consolidated financial statements include the accounts of NAPCO Security Technologies, Inc. and all of its wholly-owned subsidiaries. All inter-company balances and transactions have been eliminated in consolidation.

Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent gains and losses at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Critical estimates include management's judgments associated with reserves for sales returns and allowances, concentration of credit risk, inventory reserves, intangible assets and income taxes. Actual results could differ from those estimates.

Fair Value of Financial Instruments

The methods and assumptions used to estimate the fair value of the following classes of financial instruments were: Current Assets and Current Liabilities - The carrying amount of cash, certificates of deposits, current receivables and payables and certain other short-term financial instruments approximate their fair value as of June 30, 2016 due to their short-term maturities; Long-Term Debt - The carrying amount of the Company's long-term debt, including the current portion, at June 30, 2016 in the amount of \$4,800,000 approximates fair value.

Cash and Cash Equivalents

Cash and cash equivalents include approximately \$460,000 of short-term time deposits at June 30, 2016 and June 30, 2015. The Company considers all highly liquid investments with original maturities of three months or less to be cash equivalents. The Company has cash balances in banks in excess of the maximum amount insured by the FDIC and other international agencies as of June 30, 2016 and June 30, 2015. The Company has historically not experienced any credit losses with balances in excess of FDIC limits

Accounts Receivable

Accounts receivable is stated net of the reserves for doubtful accounts of \$145,000 and \$175,000 and for returns and other allowances of \$1,255,000 and \$1,260,000 as of June 30, 2016 and June 30, 2015, respectively. Our reserves for doubtful accounts and for returns and other allowances are subjective critical estimates that have a direct impact

on reported net earnings. These reserves are based upon the evaluation of our accounts receivable aging, specific exposures, sales levels and historical trends.

Inventories

Inventories are valued at the lower of cost or fair market value, with cost being determined on the first-in, first-out (FIFO) method. The reported net value of inventory includes finished saleable products, work-in-process and raw materials that will be sold or used in future periods. Inventory costs include raw materials, direct labor and overhead. The Company's overhead expenses are applied based, in part, upon estimates of the proportion of those expenses that are related to procuring and storing raw materials as compared to the manufacture and assembly of finished products. These proportions, the method of their application, and the resulting overhead included in ending inventory, are based in part on subjective estimates and actual results could differ from those estimates.

In addition, the Company records an inventory obsolescence reserve, which represents any excess of the cost of the inventory over its estimated market value, based on various product sales projections. This reserve is calculated using an estimated obsolescence percentage applied to the inventory based on age, historical trends, requirements to support forecasted sales, and the ability to find alternate applications of its raw materials and to convert finished product into alternate versions of the same product to better match customer demand. In addition, and as necessary, the Company may establish specific reserves for future known or anticipated events. There is inherent professional judgment and subjectivity made by both production and engineering members of management in determining the estimated obsolescence percentage.

The Company also regularly reviews the period over which its inventories will be converted to sales. Any inventories expected to convert to sales beyond 12 months from the balance sheet date are classified as non-current.

Property, Plant, and Equipment

Property, plant, and equipment are carried at cost less accumulated depreciation. Expenditures for maintenance and repairs are charged to expense as incurred; costs of major renewals and improvements are capitalized. At the time property and equipment are retired or otherwise disposed of, the cost and accumulated depreciation are eliminated from the asset and accumulated depreciation accounts and the profit or loss on such disposition is reflected in income.

Depreciation is recorded over the estimated service lives of the related assets using primarily the straight-line method. Amortization of leasehold improvements is calculated by using the straight-line method over the estimated useful life of the asset or lease term, whichever is shorter.

Intangible Assets

Intangible assets determined to have indefinite lives are not amortized but are tested for impairment at least annually. Intangible assets with definite lives are amortized over their useful lives. Intangible assets are reviewed for impairment at least annually at the Company's fiscal year end of June 30 or more often whenever there is an indication that the carrying amount may not be recovered.

The Company's acquisition of substantially all of the assets and certain liabilities of G. Marks Hardware, Inc. ("Marks") in August 2008 included intangible assets recorded at fair value on the date of acquisition. The intangible assets are amortized over their estimated useful lives of twenty years (customer relationships) and seven years (non-compete agreement). The Marks trade name was deemed to have an indefinite life.

Changes in intangible assets are as follows (in thousands):

	June 30, 2016			June 30, 2015		
	Cost	Accumulated amortization	Net book value	Cost	Accumulated amortization	Net book value
Customer relationships	\$9,800	\$ (7,343)	\$2,457	\$9,800	\$(6,820)	\$2,980
Non-compete agreement	340	(340)	--	340	(334)	6
Trade name	5,900	--	5,900	5,900	--	5,900
	<u>\$16,040</u>	<u>\$(7,683)</u>	<u>\$8,357</u>	<u>\$16,040</u>	<u>\$(7,154)</u>	<u>\$8,886</u>

Amortization expense for intangible assets subject to amortization was approximately \$529,000 and \$667,000 for the fiscal years ended June 30, 2016 and 2015, respectively. Amortization expense for each of the next five fiscal years is estimated to be as follows: 2017 - \$441,000; 2018 - \$371,000; 2019 - \$313,000 and 2020 - \$264,000 and 2021 - \$223,000. The weighted average amortization period for intangible assets was 12.1 years and 13.1 years at June 30, 2016 and 2015, respectively.

Long-Lived Assets

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets in question may not be recoverable. Impairment would be recorded in circumstances where undiscounted cash flows expected to be generated by an asset are less than the carrying value of that asset.

Revenue Recognition

The Company recognizes revenue when the following criteria are met: (i) persuasive evidence of an agreement exists, (ii) there is a fixed and determinable price for the Company's product or service, (iii) shipment and passage of title occurs or service has been provided, and (iv) collectability is reasonably assured. Revenues from product sales are recorded at the time the product is shipped or delivered to the customer pursuant to the terms of the sale. Revenues for services are recorded at the time the service is provided to the customer pursuant to the terms of sale. The Company reports its sales on a net sales basis, with net sales being computed by deducting from gross sales the amount of actual sales returns and other allowances and the amount of reserves established for anticipated sales returns and other allowances.

Sales Returns and Other Allowances

The Company analyzes sales returns and is able to make reasonable and reliable estimates of product returns based on the Company's past history. Estimates for sales returns are based on several factors including actual returns and based on expected return data communicated to it by its customers. Accordingly, the Company believes that its historical returns analysis is an accurate basis for its allowance for sales returns. Actual results could differ from those estimates. As a percentage of gross sales, sales returns, rebates and allowances were 7% and 8% for the fiscal years ended June 30, 2016 and 2015, respectively.

Advertising and Promotional Costs

Advertising and promotional costs are included in "Selling, General and Administrative" expenses in the consolidated statements of operations and are expensed as incurred. Advertising expense for the fiscal years ended June 30, 2016 and 2015 was \$2,132,000 and \$1,671,000, respectively.

Research and Development Costs

Research and development costs incurred by the Company are charged to expense as incurred and are included in "Cost of Sales" in the consolidated statements of operations. Company-sponsored research and development expense for the fiscal years ended June 30, 2016 and 2015 was \$6,169,000 and \$5,382,000, respectively.

Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred income tax expense represents the change during the period in the deferred tax assets and deferred tax liabilities. The components of the deferred tax assets and liabilities are individually classified as current and non-current based on their characteristics. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The Company measures and recognizes the tax implications of positions taken or expected to be taken in its tax returns on an ongoing basis.

Net Income Per Share

Basic net income per common share (Basic EPS) is computed by dividing net income by the weighted average number of common shares outstanding. Diluted net income per common share (Diluted EPS) is computed by dividing net income by the weighted average number of common shares and dilutive common share equivalents and convertible securities then outstanding.

The following provides a reconciliation of information used in calculating the per share amounts for the fiscal years ended June 30 (in thousands, except per share data):

	Net Income		Weighted Average Shares		Net Income per Share	
	2016	2015	2016	2015	2016	2015
Basic EPS	\$5,773	\$4,845	18,874	19,164	\$0.31	\$0.25
Effect of Dilutive Securities:						
Stock Options	--	--	20	5	--	--
Diluted EPS	<u>\$5,773</u>	<u>\$4,845</u>	<u>18,894</u>	<u>19,169</u>	<u>\$0.31</u>	<u>\$0.25</u>

Options to purchase 127,404 and 255,688 shares of common stock for the fiscal years ended June 30, 2016 and 2015, respectively, were not included in the computation of Diluted EPS because their inclusion would be anti-dilutive. These options were still outstanding at the end of the respective periods.

Stock-Based Compensation

The Company has established two share incentive programs as discussed in Note 7.

Stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense on a straight-line basis over the vesting period. Determining the fair value of share-based awards at the grant date requires assumptions and judgments about expected volatility and forfeiture rates, among other factors.

Stock-based compensation costs of \$103,000 and \$101,000 were recognized for fiscal years ended June 30, 2016 and 2015, respectively. The effect on both Basic and Diluted Earnings per share was \$0.01 for each of the fiscal years ended June 30, 2016 and 2015.

Foreign Currency

All assets and liabilities of foreign subsidiaries are translated into U.S. Dollars at fiscal period-end exchange rates. Income and expense items are translated at average exchange rates prevailing during the fiscal year. The realized and unrealized gains and losses associated with foreign currency translation, as well as related other comprehensive income, were not material for the fiscal years ended June 30, 2016 and 2015.

Comprehensive Income

For the fiscal years ended June 30, 2016 and 2015, the Company's operations did not give rise to material items includable in comprehensive income, which were not already included in net income. Accordingly, the Company's comprehensive income approximates its net income for all periods presented.

Segment Reporting

The Company's reportable operating segments are determined based on the Company's management approach. The management approach is based on the way that the chief operating decision maker organizes the segments within an enterprise for making operating decisions and assessing performance. The Company's results of operations are reviewed by the chief operating decision maker on a consolidated basis and the Company operates in only one segment. The Company has presented required geographical data in Note 11, and no additional segment data has been presented.

Shipping and Handling Revenues and Costs

The Company records the amount billed to customers for shipping and handling in net sales (\$492,000 and \$515,000 in the fiscal years ended June 30, 2016 and 2015, respectively) and classifies the costs associated with these revenues in cost of sales (\$918,000 and \$945,000 in fiscal years ended June 30, 2016 and 2015).

Recently Issued Accounting Standards

In March 2016, the Financial Accounting Standards Board ("FASB") issued authoritative guidance that changes the way companies account for certain aspects of share-based payments to employees. The most significant impact relates to the accounting for income tax effects of share-based compensation awards. This new guidance is part of the FASB's simplification initiative and requires that all excess tax benefits and tax deficiencies be recorded as income tax expense or benefit in the income statement. In addition, companies are required to treat the tax effects of exercised or vested awards as discrete items in the period that they occur. Other updates include changing the threshold on tax withholding requirements. Under this guidance, an employer can withhold up to the maximum statutory withholding rates in a jurisdiction without tainting the award classification. Additionally, this guidance allows companies to elect a forfeiture recognition method whereby they account for forfeitures as they occur (actual) or they estimate the number of awards expected to be forfeited (current GAAP). Lastly, as it relates to public entities, this guidance also provides requirements for the cash flow classification of cash paid by an employer when directly withholding shares for tax-withholding purposes and excess tax benefits. This guidance becomes effective for the Company's fiscal 2018 first quarter, with early adoption permitted, and the guidance prescribes different transition methods for the various provisions (i.e., retrospective, modified retrospective, or prospective). The Company is currently evaluating the impact of applying this guidance on its consolidated financial statements.

In February 2016, the FASB issued authoritative guidance that requires lessees to account for most leases on their balance sheets with the liability being equal to the present value of the lease payments. The right-of-use asset will be based on the lease liability adjusted for certain costs such as direct costs. Lease expense will be recognized similar to current accounting guidance with operating leases resulting in a straight-line expense and financing leases resulting in a front-loaded expense similar to the current accounting for capital leases. This guidance becomes effective for the Company's fiscal 2020 first quarter, with early adoption permitted. This guidance must be adopted using a modified retrospective transition approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements, and provides for certain practical expedients. The Company is currently evaluating the timing, impact and method of applying this guidance on its consolidated financial statements.

In November 2015, the FASB issued ASU 2015-17 “Balance Sheet Classification of Deferred Taxes”. The amendments require deferred tax assets and liabilities, along with related valuation allowances, to be classified as noncurrent on the balance sheet. As a result, each tax jurisdiction will now only have one net noncurrent deferred tax asset or liability. The new guidance does not change the existing requirement that prohibits offsetting deferred tax liabilities from one jurisdiction against deferred tax assets of another jurisdiction. ASU 2015-17 is effective for the Company’s quarter ended September 30, 2016. Early application is permitted. We have not early adopted ASU 2015-17. The new guidance must be applied prospectively after the date of adoption. We have evaluated the adoption of this ASU, and do not expect this to have a material effect on our consolidated results of operations and financial condition.

In July 2015, the FASB issued ASU 2015-11 “Inventory (Topic 330): Simplifying the Measurement of Inventory” (ASU 2015-11). The amendments in ASU 2015-11 simplify the subsequent measurement of inventory by requiring inventory to be measured at the lower of cost and net realizable value. ASU 2015-11 is effective for the Company’s quarter ended September 30, 2017. Early application is permitted. We have not early adopted ASU 2015-11. The new guidance must be applied prospectively after the date of adoption. We are in the process of evaluating the adoption of this ASU, and do not expect this to have a material effect on our consolidated results of operations and financial condition.

In May 2014, the FASB issued authoritative guidance that defines how companies should report revenues from contracts with customers. The standard requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. It provides companies with a single comprehensive five-step principles-based model to use in accounting for revenue and supersedes current revenue recognition requirements, including most industry-specific and transaction-specific revenue guidance. In August 2015, the FASB deferred the effective date of the new revenue standard by one year. As a result, the new standard would not be effective for the Company until fiscal 2019. In addition, the FASB is allowing companies to early adopt this guidance for the Company’s fiscal 2018. The guidance permits an entity to apply the standard retrospectively to all prior periods presented, with certain practical expedients, or apply the requirements in the year of adoption, through a cumulative adjustment. The Company will apply this new guidance when it becomes effective and has not yet selected a transition method. The Company is currently evaluating the impact of adoption on its consolidated financial statements.

NOTE 2 - Business and Credit Concentrations

An entity is more vulnerable to concentrations of credit risk if it is exposed to risk of loss greater than it would have had if it mitigated its risk through diversification of customers. Such risks of loss manifest themselves differently, depending on the nature of the concentration, and vary in significance. The Company had one customer with an accounts receivable balance that comprised 22% of the Company’s accounts receivable at both June 30, 2016 and 2015. Sales to this customer comprised 13% of net sales in each of the fiscal years ended June 30, 2016 and 2015.

NOTE 3 - Inventories

Inventories, net of reserves are valued at lower of cost (first-in, first-out method) or market. The Company regularly reviews parts and finished goods inventories on hand and, when necessary, records a provision for excess or obsolete inventories. The Company also regularly reviews the period over which its inventories will be converted to sales. Any inventories expected to convert to sales beyond 12 months from the balance sheet date are classified as non-current.

Inventories, net of reserves consist of the following (in thousands):

	June 30,	
	2016	2015
Component parts	\$14,021	\$15,037
Work-in-process	3,758	4,136
Finished product	7,558	7,697
	<u>\$25,337</u>	<u>\$26,870</u>
Classification of inventories, net of reserves:		
Current	\$21,428	\$22,757
Non-current	3,909	4,113
	<u>\$25,337</u>	<u>\$26,870</u>

NOTE 4 - Property, Plant, and Equipment

Property, plant and equipment consist of the following (in thousands):

	June 30,		Useful Life in Years
	2016	2015	
Land	\$904	\$904	--
Buildings	8,911	8,911	30 to 40
Molds and dies	7,036	7,002	3 to 5
Furniture and fixtures	2,531	2,478	5 to 10
Machinery and equipment	21,035	20,429	7 to 10
Leasehold improvements	294	294	Shorter of the lease term or life of asset
	<u>40,711</u>	<u>40,018</u>	
Less: accumulated depreciation and amortization	<u>34,662</u>	<u>33,784</u>	
	<u>\$6,049</u>	<u>\$6,234</u>	

Depreciation and amortization expense on property, plant, and equipment was approximately \$878,000 and \$890,000 in fiscal 2016 and 2015, respectively.

NOTE 5 - Income Taxes

The provision for income taxes is comprised of the following (in thousands):

	<u>For the Years Ended June 30,</u>	
	<u>2016</u>	<u>2015</u>
Current income taxes:		
Federal	\$ (31)	\$ (49)
State	<u>27</u>	<u>35</u>
	(4)	(14)
Deferred income tax provision	<u>375</u>	<u>230</u>
Provision for income taxes	<u><u>\$371</u></u>	<u><u>\$216</u></u>

A reconciliation of the U.S. Federal statutory income tax rate to our actual effective tax rate on earnings before income taxes is as follows for the years ended June 30, (dollars in thousands):

	<u>2016</u>		<u>2015</u>	
	<u>Amount</u>	<u>% of Pre-tax Income</u>	<u>Amount</u>	<u>% of Pre-tax Income</u>
Tax at Federal statutory rate	\$2,089	34.0%	\$1,721	34.0%
Increases (decreases) in taxes resulting from:				
Meals and entertainment	61	1.0%	66	1.3%
State income taxes, net of Federal income tax benefit	20	0.3%	21	0.4%
Foreign source income not subject to tax	(1,278)	(20.8)%	(1,069)	(21.1)%
R&D Credit refund	(415)	(6.8)%	(328)	(6.5)%
Undistributed foreign earnings	(90)	(1.4)%	(93)	(1.8)%
Other, net	<u>(16)</u>	<u>(0.3)%</u>	<u>(102)</u>	<u>(2.0)%</u>
Effective tax rate	<u><u>\$371</u></u>	<u><u>6.0%</u></u>	<u><u>\$216</u></u>	<u><u>4.3%</u></u>

Deferred tax assets and deferred tax liabilities at June 30, 2016 and 2015 are as follows (in thousands):

	<u>Current Deferred Tax Assets (Liabilities)</u>		<u>Long-term Deferred Tax Assets (Liabilities)</u>	
	<u>2016</u>	<u>2015</u>	<u>2016</u>	<u>2015</u>
Accounts receivable	\$26	\$36	\$ --	\$ --
Inventories	364	533	200	261
Accrued Liabilities	313	311	87	86
Stock based compensation expense	--	--	154	147
Goodwill	--	--	(14)	214
R&D credit	--	--	1,214	804
Property, plant and equipment	--	--	(503)	(512)
Other deferred tax liabilities	<u>--</u>	<u>--</u>	<u>(702)</u>	<u>(366)</u>
	703	880	436	634
Valuation allowance	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>
Net deferred tax assets	<u><u>\$703</u></u>	<u><u>\$880</u></u>	<u><u>\$436</u></u>	<u><u>\$634</u></u>

The Company has identified the United States and New York State as its major tax jurisdictions. The fiscal 2012 and forward years are still open for examination.

During the year ending June 30, 2016 the Company increased its reserve for uncertain income tax positions by \$46,000. The Company's practice is to recognize interest and penalties related to income tax matters in income tax expense and accrued income taxes. As of June 30, 2016, the Company had accrued interest totaling \$0 and \$148,000 of unrecognized net tax benefits that, if recognized, would favorably affect the Company's effective income tax rate in any future period. The Company uses the flow through method to account for investment tax credits earned on eligible research and development expenditures. Under this method, the investment tax credits are recognized as a reduction to income tax expense.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows (in thousands):

	<u>Tax</u>	<u>Interest</u>	<u>Total</u>
Balance of gross unrecognized tax benefits as of July 1, 2015	\$102	\$ --	\$102
Increases to unrecognized tax benefits resulting from the generation of additional R&D credits	<u>46</u>	<u>--</u>	<u>46</u>
Balance of gross unrecognized tax benefits as of June 30, 2016	<u>\$148</u>	<u>\$ --</u>	<u>\$148</u>

The Company plans to permanently reinvest a substantial portion of its foreign earnings and as such has not provided US corporate taxes on the permanently reinvested earnings. As of June 30, 2016, the Company had approximately \$7.6 million of undistributed earnings of foreign subsidiaries.

NOTE 6 - Long-Term Debt

As of June 30, 2016, long-term debt consisted of a revolving credit facility of \$11,000,000 (the "Revolving Credit Facility") which expires in June 2021 and one loan for \$6,000,000 which expires in June 2019 (the "Term Loan"). The Revolving Credit Facility had an expiration date of June 2017 which was extended to June 2021 at the end of fiscal 2016. Repayment of the Term Loan commenced on September 30, 2012. The Term Loan is being repaid with 28 equal, quarterly payments of \$75,000 and the remaining balance of \$1,900,000 due on or before the expiration date.

Outstanding balances and interest rates as of June 30, 2016 and June 30, 2015 are as follows:

	<u>June 30, 2016</u>		<u>June 30, 2015</u>	
	<u>Outstanding</u>	<u>Interest Rate</u>	<u>Outstanding</u>	<u>Interest Rate</u>
Revolving line of credit	\$2,000	1.6%	\$3,000	1.7%
Term loans	<u>2,800</u>	<u>1.6%</u>	<u>7,700</u>	<u>1.7%</u>
Total debt	<u>\$4,800</u>	<u>1.6%</u>	<u>\$10,700</u>	<u>1.7%</u>

The Revolving Credit Facility and Term Loans (collectively the "Agreement") also provides for a LIBOR-based interest rate option of LIBOR plus 1.15% to 2.00%, depending on the ratio of outstanding debt to EBITDA, which is to be measured and adjusted quarterly, a prime rate-based option of the prime rate plus 0.25% and other terms and conditions as more fully described in the Agreement. In addition, the Agreement provides for availability under the Revolving Credit Facility to be limited to the lesser of \$11,000,000 or the result of a borrowing base formula based upon the Company's Accounts Receivables and Inventory values net of certain deductions. The Company's obligations under the Agreement continue to be secured by all of its assets, including but not limited to, deposit accounts, accounts receivable, inventory, and the Company's corporate headquarters in Amityville, NY, equipment and fixtures and intangible assets. In addition, the Company's wholly-owned subsidiaries, with the exception of the Company's foreign subsidiaries, have issued guarantees and pledges of all of their assets to secure the Company's obligations under the Agreement. All of the outstanding common stock of the Company's domestic subsidiaries and

65% of the common stock of the Company's foreign subsidiaries has been pledged to secure the Company's obligations under the Agreement.

The Agreement contains various restrictions and covenants including, among others, restrictions on payment of dividends, restrictions on borrowings and compliance with certain financial ratios, as defined in the Agreement.

NOTE 7 - Stock Options

The Company follows ASC 718 ("Share-Based Payment"), which requires that all share based payments to employees, including stock options, be recognized as compensation expense in the consolidated financial statements based on their fair values and over the requisite service period. For the fiscal years ended June 30, 2016 and 2015, the Company recorded non-cash compensation expense of \$103,000 (\$0.01 per basic and diluted share) and \$101,000 (\$0.01 per basic and diluted share), respectively, relating to stock-based compensation

2012 Employee Stock Option Plan

In December 2012, the stockholders approved the 2012 Employee Stock Option Plan (the 2012 Employee Plan). The 2012 Employee Plan authorizes the granting of awards, the exercise of which would allow up to an aggregate of 950,000 shares of the Company's common stock to be acquired by the holders of such awards. Under this plan, the Company may grant stock options, which are intended to qualify as incentive stock options (ISOs), to valued employees. Any plan participant who is granted ISOs and possesses more than 10% of the voting rights of the Company's outstanding common stock must be granted an option with a price of at least 110% of the fair market value on the date of grant.

Under the 2012 Employee Plan, stock options may be granted to valued employees with a term of up to 10 years at an exercise price equal to or greater than the fair market value on the date of grant and are exercisable, in whole or in part, at 20% per year beginning on the date of grant. An option granted under this plan shall vest in full upon a "change in control" as defined in the plan. At June 30, 2016, 112,500 stock options were granted, 55,700 stock options were exercisable and 837,500 stock options were available for grant under this plan.

The fair value of each option granted during fiscal 2016 and 2015 were estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

	<u>2016</u>	<u>2015</u>
Risk-free interest rates	1.8%	2.3%
Expected lives	10 years	10 years
Expected volatility	54%	54%
Expected dividend yields	0%	0%

The Company uses a weighted-average expected stock-price volatility assumption that is a combination of both current and historical implied volatilities of the underlying stock. The implied volatilities were obtained from publicly available data sources. For the weighted-average expected option life assumption, the Company considers the exercise behavior of past grants. The average risk-free interest rate is based on the U.S. Treasury Bond rate for the expected term of the options and the average dividend yield is based on historical experience.

The following table reflects activity under the 2012 Plan for the fiscal years ended June 30,:

	2016		2015	
	Options	Weighted average exercise price	Options	Weighted average exercise price
Outstanding, beginning of year	112,500	\$5.30	78,500	\$5.73
Granted	15,000	6.05	44,000	4.43
Terminated	(15,000)	4.29	(10,000)	4.88
Exercised	--	--	--	--
Outstanding, end of year	<u>112,500</u>	<u>\$5.54</u>	<u>112,500</u>	<u>\$5.30</u>
Exercisable, end of year	<u>55,700</u>	<u>\$5.59</u>	<u>27,500</u>	<u>\$5.26</u>
Weighted average fair value at grant date of options granted	\$3.86		\$2.82	
Total intrinsic value of options exercised	n/a		n/a	
Total intrinsic value of options outstanding	\$93,000		\$73,000	
Total intrinsic value of options exercisable	\$43,000		\$18,000	

The following table summarizes information about stock options outstanding under the 2012 Employee Plan at June 30, 2016:

Range of exercise prices	Options outstanding			Options exercisable	
	Number outstanding	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable	Weighted average exercise price
\$4.29-\$6.31	112,500	7.9	\$5.54	55,700	\$5.59
	<u>112,500</u>	<u>7.9</u>	<u>\$5.54</u>	<u>55,700</u>	<u>\$5.59</u>

As of June 30, 2016, there was \$260,000 of unearned stock-based compensation cost related to share-based compensation arrangements granted under the 2012 Employee Plan. 15,000 and 44,000 options were granted during the fiscal years ended June 30, 2016 and 2015, respectively. The total fair value of the options vesting during the fiscal years ended June 30, 2016 and 2015 under this plan was \$119,000 and \$41,000, respectively.

2012 Non-Employee Stock Option Plan

In December 2012, the stockholders approved the 2012 Non-Employee Stock Option Plan (the 2012 Non-Employee Plan). This plan authorizes the granting of awards, the exercise of which would allow up to an aggregate of 50,000 shares of the Company's common stock to be acquired by the holders of such awards. Under this plan, the Company may grant stock options to non-employee directors and consultants to the Company and its subsidiaries.

Under the 2012 Non-Employee Plan, stock options may be granted with a term of up to 10 years at an exercise price equal to or greater than the fair market value on the date of grant and are exercisable in whole or in part at 20% per year beginning on the date of grant. An option granted under this plan shall vest in full upon a "change in control" as defined in the plan. At June 30, 2016, 35,000 stock options were granted, 19,000 stock options were exercisable and 15,000 stock options were available for grant under this plan.

The following table reflects activity under the 2012 Non-Employee Plan for the fiscal years ended June 30,:

	2016		2015	
	Options	Weighted average exercise price	Options	Weighted average exercise price
Outstanding, beginning of year	35,000	\$4.73	25,000	\$4.88
Granted	--	--	10,000	4.37
Terminated	--	--	--	--
Exercised	--	--	--	--
Outstanding, end of year	<u>35,000</u>	<u>\$4.73</u>	<u>35,000</u>	<u>\$4.73</u>
Exercisable, end of year	<u>19,000</u>	<u>\$4.77</u>	<u>12,000</u>	<u>\$4.80</u>
Weighted average fair value at grant date of options granted				
	n/a		\$2.86	
Total intrinsic value of options exercised				
	n/a		n/a	
Total intrinsic value of options outstanding				
	\$57,000		\$35,000	
Total intrinsic value of options exercisable				
	\$30,000		\$11,000	

The following table summarizes information about stock options outstanding under the 2012 Non-Employee Plan at June 30, 2016:

Range of exercise prices	Options outstanding			Options exercisable	
	Number outstanding	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable	Weighted average exercise price
\$4.37 - \$4.88	35,000	7.5	\$4.73	19,000	\$4.77
	<u>35,000</u>	<u>7.5</u>	<u>\$4.73</u>	<u>19,000</u>	<u>\$4.77</u>

As of June 30, 2016, there was \$73,000 of unearned stock-based compensation cost related to share-based compensation arrangements granted under the 2012 Non-Employee Plan. 0 and 10,000 options were granted during the fiscal years ended June 30, 2016 and 2015, respectively. The total fair value of the options vesting during the fiscal years ended June 30, 2016 and 2015 under this plan was \$22,000 and \$6,000, respectively.

2002 Employee Stock Option Plan

In December 2002, the stockholders approved the 2002 Employee Stock Option Plan (the 2002 Employee Plan). This plan expired in October 2012. This plan authorized the granting of awards, the exercise of which would allow up to an aggregate of 1,836,000 shares of the Company's common stock to be acquired by the holders of such awards. Under this plan, the Company may have granted stock options, which were intended to qualify as incentive stock options (ISOs), to key employees. Any plan participant who was granted ISOs and possessed more than 10% of the voting rights of the Company's outstanding common stock must have been granted an option with a price of at least 110% of the fair market value on the date of grant.

Under the 2002 Employee Plan, stock options have been granted to key employees with a term of 10 years at an exercise price equal to the fair market value on the date of grant and are exercisable in whole or in part at 20% per year from the date of grant. At June 30, 2016, 1,471,480 stock options had been granted, 102,500 stock options were exercisable and no further stock options were available for grant under this plan after the plans expiration in October 2012.

The following table reflects activity under the 2002 Employee plan for the fiscal years ended June 30,:

	2016		2015	
	Options	Weighted average exercise price	Options	Weighted average exercise price
Outstanding, beginning of year	208,500	\$6.86	265,750	\$6.51
Granted	--	--	--	--
Terminated/Lapsed	(38,500)	11.03	(57,250)	5.24
Exercised	(67,500)	5.73	--	--
Outstanding, end of period	<u>102,500</u>	<u>\$6.04</u>	<u>208,500</u>	<u>\$6.86</u>
Exercisable, end of period	<u>102,500</u>	<u>\$6.04</u>	<u>208,500</u>	<u>\$6.86</u>
Weighted average fair value at grant date of options granted	n/a		n/a	
Total intrinsic value of options exercised	\$42,000		n/a	
Total intrinsic value of options outstanding	\$40,000		\$6,000	
Total intrinsic value of options exercisable	\$40,000		\$6,000	

As of June 30, 2016, there was no unearned stock-based compensation cost related to share-based compensation arrangements granted under the 2002 Non-Employee Plan. 67,500 and 0 stock options were exercised during the fiscal years ended June 30, 2016 and 2015, respectively. The 67,500 stock options exercised during the fiscal year ended June 30, 2015 were settled by exchanging 53,868 shares of the Company's common stock which was included in Treasury Stock upon receipt. No cash was received from option exercises for either of the fiscal years ended June 30, 2016 and 2015 and the actual tax benefit realized for the tax deductions from option exercises was \$0 for each of these periods.

The following table summarizes information about stock options outstanding under the 2002 Employee Plan at June 30, 2016:

Range of exercise prices	Options outstanding and exercisable		
	Number outstanding	Weighted average remaining contractual life	Weighted average exercise price
\$5.35-\$6.62	<u>102,500</u>	<u>0.7</u>	<u>\$6.04</u>
	<u>102,500</u>	<u>0.7</u>	<u>\$6.04</u>

NOTE 8 – Stockholders' Equity Transactions

On September 16, 2014 the Company's board of directors authorized the repurchase of up to 1 million of the approximately 19.4 million shares of the Company's common stock outstanding. The repurchase will be made from time to time in the open market or in privately negotiated transactions subject to market conditions and the market price of the common stock. Relative to the loan agreements described in Note 6, the Company's lender gave its consent to this stock repurchase plan. During the fiscal year ended June 30, 2016 the Company repurchased 192,767 shares of its outstanding common stock for a weighted average price of \$5.73 per share. These repurchased shares are included in the Company's Treasury Stock as of June 30, 2016.

During fiscal 2016, certain employees exercised incentive stock options under the Company's 2002 Plan totaling 67,500 shares. All of these exercises were completed as cashless exercises as allowed for under the 2002 Plan, where the exercise shares are issued by the Company in exchange for shares of the Company's common stock that

are owned by the optionees. The number of shares surrendered by the optionees was 53,868 and was based upon the per share price on the effective date of the option exercise.

NOTE 9 - 401(k) Plan

The Company maintains a 401(k) plan (“the Plan”) that covers all U.S. non-union employees with one or more years of service and is qualified under Sections 401(a) and 401(k) of the Internal Revenue Code. Company contributions to this plan are discretionary and totaled \$111,000 and \$122,000 for the years ended June 30, 2016 and 2015, respectively.

NOTE 10 - Commitments and Contingencies

Leases

The Company is committed under various operating leases, not including the land lease discussed below, which do not extend beyond fiscal 2019. Minimum lease payments through the expiration dates of these leases, with the exception of the land leases referred to below, are as follows:

<u>Year Ending June 30,</u>	<u>Amount</u>
2017	\$23,000
2018	22,000
2019	<u>14,000</u>
Total	<u><u>\$59,000</u></u>

Rent expense, with the exception of the land lease referred to below, totaled approximately \$26,000 and \$30,000 for the fiscal years ended June 30, 2016 and 2015, respectively.

Land Lease

On April 26, 1993, one of the Company's foreign subsidiaries entered into a 99 year lease, expiring in 2092, for approximately four acres of land in the Dominican Republic at an annual cost of \$288,000, on which the Company's principal production facility is located.

Litigation

In the normal course of business, the Company is a party to claims and/or litigation. Management believes that the settlement of such claims and/or litigation, considered in the aggregate, will not have a material adverse effect on the Company's financial position and results of operations.

Employment Agreements

As of June 30, 2016, the Company was obligated under three employment agreements and one severance agreement. The employment agreements are with the Company's CEO, Senior Vice President of Sales and Marketing (“the SVP of Sales”) and the Senior Vice President of Engineering (“the SVP of Engineering”). The employment agreement with the CEO provides for an annual salary of \$670,000, as adjusted for inflation; incentive compensation as may be approved by the Board of Directors from time to time and a termination payment in an amount up to 299% of the average of the prior five calendar year's compensation, subject to certain limitations, as defined in the agreement. The employment agreement renews annually in August unless either party gives the other notice of non-renewal at least six months prior to the end of the applicable term. The employment agreement with the SVP of Sales expires in October 2018 and provides for an annual salary of \$315,000, a bonus arrangement for fiscal 2016 and, if terminated by the Company without cause, severance of nine months' salary and continued company-sponsored health

insurance for six months from the date of termination. The employment agreement with the SVP of Engineering expires in August 2018 and provides for an annual salary of \$285,000, a bonus arrangement and, if terminated by the Company without cause, severance of nine month's salary and continued company-sponsored health insurance for six months from the date of termination. The severance agreement is with the Senior Vice President of Operations and Finance and provides for, if terminated by the Company without cause or within three months of a change in corporate control of the Registrant, severance of nine month's salary, continued company-sponsored health insurance for six months from the date of termination and certain non-compete and other restrictive provisions.

NOTE 11 - Geographical Data

The Company is engaged in one major line of business: the development, manufacture, and distribution of access control systems, door security products, intrusion and fire alarm systems and video surveillance products for commercial and residential use. Sales to unaffiliated customers are primarily shipped from the United States. The Company has customers worldwide with major concentrations in North America.

Financial Information Relating to Domestic and Foreign Operations

	<u>2016</u>	<u>2015</u>
	(in thousands)	
Sales to external customers(1):		
Domestic	\$79,931	\$74,736
Foreign	<u>2,582</u>	<u>3,026</u>
Total Net Sales	<u>\$82,513</u>	<u>\$77,762</u>
Identifiable assets:		
United States	\$51,272	\$50,998
Dominican Republic (2)	<u>13,497</u>	<u>14,039</u>
Total Identifiable Assets	<u>\$64,769</u>	<u>\$65,037</u>

(1) All of the Company's sales originate in the United States and are shipped primarily from the Company's facilities in the United States. There were no sales into any one foreign country in excess of 10% of total Net Sales.

(2) Consists primarily of inventories (2016 = \$10,076; 2015 = \$10,546) and fixed assets (2016 = \$3,311; 2015 = \$3,347) located at the Company's principal manufacturing facility in the Dominican Republic.

NOTE 12 – Subsequent Events

The Company has evaluated subsequent events occurring after the date of the consolidated financial statements for events requiring recording or disclosure in the financial statements.

ITEM 9: CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None

ITEM 9A: CONTROL AND PROCEDURES

Evaluation of Disclosure Controls and Procedures. At the conclusion of the period ended June 30, 2016, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of June 30, 2016.

Management's Annual Report on Internal Control Over Financial Reporting. Management is responsible for the preparation of the Company's consolidated financial statements and related information. Management uses its best judgment to ensure that the consolidated financial statements present fairly, in all material respects, the Company's consolidated financial position and results of operations in conformity with generally accepted accounting principles.

The consolidated financial statements have been audited by an independent registered public accounting firm in accordance with the standards of the Public Company Accounting Oversight Board. Their report expresses the independent accountant's judgment as to the fairness of management's reported operating results, cash flows and financial position. This judgment is based on the procedures described in the second paragraph of their report.

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting. Under the supervision of management, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework *Internal Control – Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and other guidance prepared specifically for smaller public companies. Based on that evaluation, our management concluded that our internal control over financial reporting was effective as of June 30, 2016.

Our internal control over financial reporting includes policies and procedures that pertain to the maintenance of records that accurately and fairly reflect, in reasonable detail, transactions and dispositions of assets; and provide reasonable assurances that: (1) transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States; (2) receipts and expenditures are being made only in accordance with authorizations of management and the directors of our Company; and (3) unauthorized acquisition, use, or disposition of our assets that could have a material effect on our financial statements are prevented or timely detected.

Limitations on Internal Control

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

This annual report does not include an attestation report of Baker Tilly Virchow Krause, LLP, our registered public accounting firm, regarding internal control over financial reporting. Management's Report was not subject to attestation by the Company's registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permit us to provide only Management's Report in this annual report.

The Board of Directors of the Company has an Audit Committee comprised of three non-management directors. The Committee meets periodically with financial management and the independent auditors to review accounting, control, audit and financial reporting matters. Baker Tilly Virchow Krause, LLP has full and free access to the Audit Committee, with and without the presence of management.

Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting during the quarter ended June 30, 2016 that has materially affected or is likely to materially affect our internal controls over financial reporting.

ITEM 9B: OTHER INFORMATION

None

PART III

ITEM 10: DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information about our directors appearing in the Company's Definitive Proxy Statement for the 2016 Annual Meeting of Stockholders, to be filed with the Securities and Exchange Commission pursuant to Regulation 14A within 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K ("Proxy Statement") under the heading "Election of Directors", is incorporated herein by reference.

We have adopted a Code of Ethics which applies to our senior executive and financial officers, among others. The Code is posted on our website, www.napcosecurity.com, under the "Investors – Other" caption. We intend to make all required disclosures regarding any amendment to, or waiver of, a provision of the Code of Ethics for senior executive and financial officers by posting such information on our website.

The information appearing in the Proxy Statement relating to the members of the Audit Committee and the Audit Committee financial expert under the headings "Corporate Governance and Board Matters – Board Structure and Committee Composition" and "Corporate Governance and Board Matters – Board Structure and Committee Composition – Audit Committee" and the information appearing in the Proxy Statement under the heading "Section 16(a) Beneficial Ownership Reporting Compliance" is incorporated herein by this reference.

The information set forth in the Proxy Statement under the heading "Information Concerning Executive Officers" is incorporated herein by reference.

ITEM 11: EXECUTIVE COMPENSATION

The information appearing in the Proxy Statement under the heading "Executive Compensation" and the information appearing in the Proxy Statement relating to the compensation of directors under the caption "Compensation of Directors" is incorporated herein by this reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information appearing in the Proxy Statement under the heading "Beneficial Ownership of Common Stock" is incorporated herein by this reference.

Information regarding Equity Compensation Plan Information as of June 30, 2016 is included in Item 5.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information appearing in the Proxy Statement under the headings "Corporate Governance and Board Matters – Independence of Directors," "Corporate Governance and Board Matters – Board Structure and Committee Composition," "Corporate Governance – Policy with Respect to Related Person Transactions," and "Executive Compensation – Certain Transactions" is incorporated herein by this reference.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

Information appearing in the Proxy Statement under the headings "Principal Accountant Fees" and "Policy on Audit Committee Pre-Approval of Audit and Permissible Non-Audit Services of Independent Auditors" is incorporated herein by this reference.

PART IV

ITEM 15: EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.

Omitted.

Upon written request of any stockholder of the Company, the Company will provide such shareholder a copy of the Company's Annual Report on Form 10-K for 2016, including the financial statements and schedules thereto, filed with the Security and Exchange Commission. Any such request should be directed to Secretary, NAPCO Security Technologies, Inc., 333 Bayview Avenue, Amityville, New York 11701. There will be no charge for such report unless one or more exhibits thereto are requested, in which case the Company's reasonable expenses of furnishing such exhibits thereto are requested, in which case the Company's reasonable expenses of furnishing such exhibits may be charged.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

September 8, 2016

NAPCO SECURITY TECHNOLOGIES, INC.

(Registrant)

By: /s/RICHARD SOLOWAY

*Richard Soloway
Chairman of the Board of
Directors, President and Secretary
(Principal Executive Officer)*

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Registrant and in the capacities and the dates indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/RICHARD SOLOWAY</u> Richard Soloway	Chairman of the Board of Directors, President and Secretary and Director (Principal Executive Officer)	September 8, 2016
<u>/s/KEVIN S. BUCHEL</u> Kevin S. Buchel	Senior Vice President of Operations and Finance and Treasurer and Director (Principal Financial and Accounting Officer)	September 8, 2016
<u>/s/PAUL STEPHEN BEEBER</u> Paul Stephen Beeber	Director	September 8, 2016
<u>/s/RANDY B. BLAUSTEIN</u> Randy B. Blaustein	Director	September 8, 2016
<u>/s/ARNOLD BLUMENTHAL</u> Arnold Blumenthal	Director	September 8, 2016
<u>/s/DONNA SOLOWAY</u> Donna Soloway	Director	September 8, 2016
<u>/s/ANDREW J. WILDER</u> Andrew J. Wilder	Director	September 8, 2016

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NAPCO SECURITY TECHNOLOGIES, INC. AND SUBSIDIARIES

NON-GAAP MEASURES OF PERFORMANCE* (unaudited)

(In thousands, except for shares)

	Three months ended June 30,		Twelve months ended June 30,	
	2016	2015	2016	2015
Net income	\$3,438	\$3,340	\$5,773	\$4,845
Add back provision for income taxes	288	65	371	216
Add back interest and other expense	30	57	179	202
Operating income (GAAP)	3,756	3,462	6,323	5,281
Adjustments for non-GAAP measures of performance:				
Add back amortization of acquisition-related intangibles	131	166	529	666
Add back stock-based compensation expense	11	–	103	100
Adjusted non-GAAP operating income	3,898	3,628	6,955	6,047
Add back depreciation and other amortization	251	260	891	904
Adjusted EBITDA (earnings before interest, taxes, depreciation and amortization)	\$4,149	\$3,888	\$7,846	\$6,951
Adjusted EBITDA per Diluted Share	\$0.22	\$0.20	\$0.42	\$0.36
Weighted average number of Diluted Shares outstanding	18,804,000	18,989,000	18,894,000	19,169,000

* Non-GAAP Information

Certain non-GAAP measures are included above, including EBITDA, non-GAAP operating income and Adjusted EBITDA. We define EBITDA as GAAP net income plus income tax expense (benefit), net interest expense and depreciation and amortization expense. Non-GAAP operating income does not include impairment of goodwill, amortization of intangibles, restructuring charges, stock-based compensation expense and other infrequent or unusual charges. These non-GAAP measures are provided to enhance the user's overall understanding of our financial performance. By excluding these charges our non-GAAP results provide information to management and investors that is useful in assessing NAPCO's core operating performance and in comparing our results of operations on a consistent basis from period to period. The presentation of this information is not meant to be a substitute for the corresponding financial measures prepared in accordance with generally accepted accounting principles. Investors are encouraged to review the reconciliation of GAAP to non-GAAP financial measures included in the above.



Officers

Richard L. Soloway
Chairman, President and C.E.O.

Kevin S. Buchel
Senior Vice President of Operations
and Finance and Treasurer

Jorge D. Hevia
Senior Vice President of Sales
and Marketing

Michael Carrieri
Senior Vice President of
Engineering

Alfred DePierro
Vice President of Engineering
Microcomputer Applications

Raymond Gaudio
Vice President of Engineering
Software Applications

George R. Marks
President, Marks USA

Common Stock Listing

Nasdaq Global Market System®
(Symbol—"NSSC")

Directors

Richard L. Soloway
Chairman, President and C.E.O.

Paul Stephen Beeber
Attorney

Randy B. Blaustein, Esq.
Tax Attorney

Arnold B. Blumenthal
Group Publisher Emeritus,
Security Dealer, Locksmith Ledger;
Publisher, Security Line

Kevin S. Buchel
Senior Vice President of Operations
and Finance and Treasurer

Donna A. Soloway
Security Industry Publicist

Andrew J. Wilder
Officer of Israeloff,
Trattner & Company
(Certified Public Accountants)

Primary Bank

HSBC Bank USA
534 Broadhollow Road
Melville, NY 11747

Investor Relations

Copies of the Company's Annual
Report, Forms 10-K and 10-Q and
other information filed with the
Securities and Exchange
Commission may be obtained
directly from the Corporation by
contacting:

NAPCO Security Technologies, Inc.
333 Bayview Avenue
Amityville, NY 11701
Attention: Corporate Secretary

Independent Accountants

Baker Tilly Virchow Krause, LLP
125 Baylis Road
Melville, NY 11747-3823

Legal Counsel

Forman & Shapiro LLP
1345 Avenue of the Americas
New York, NY 10105

Transfer Agent

Continental Stock Transfer &
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