

# 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 December 31, 2019.
- 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 0-24020

### SYPRIS SOLUTIONS, INC.

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction  
of incorporation or organization)

**61-1321992**

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

**101 Bullitt Lane, Suite 450  
Louisville, Kentucky 40222**

(Address of principal executive  
offices, including zip code)

**(502) 329-2000**

(Registrant's telephone number,  
including area code)

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

<u>Title of each class</u>	<u>Trading Symbol</u>	<u>Name of each exchange on which registered</u>
Common Stock	SYPR	NASDAQ

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 Sections 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.  Yes  No

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company  
 Emerging Growth Company

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

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold as of the last business day of the registrant's most recently completed second fiscal quarter (June 30, 2019) was \$8,814,182.

There were 21,309,580 shares of the registrant's common stock outstanding as of March 10 2020.

### DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement to be delivered to stockholders in connection with the Annual Meeting of Stockholders to be held May 12, 2020 are incorporated by reference into Part III to the extent described therein.

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In this Annual Report on Form 10-K, “Sypris,” “the Company,” “we,” “us” and “our” refer to Sypris Solutions, Inc. and its subsidiaries and predecessors, collectively. “Sypris Solutions” and “Sypris” are our trademarks. All other trademarks, servicemarks or trade names referred to in this Annual Report on Form 10-K are the property of their respective owners.

## PART I

### Item 1. Business

#### General

We were formed as a Delaware corporation in 1997. We are a diversified provider of truck components, oil and gas pipeline components and aerospace and defense electronics. We produce a wide range of manufactured products, often under multi-year, sole-source contracts.

We are organized into two business segments, Sypris Technologies and Sypris Electronics. Sypris Technologies, which is comprised of Sypris Technologies, Inc. and its subsidiaries, generates revenue primarily from the sale of forged, machined, welded and heat-treated steel components primarily for the heavy commercial vehicle and high-pressure energy pipeline applications. Sypris Electronics, which is comprised of Sypris Electronics, LLC, is focused on circuit card and full “box build” manufacturing, high reliability manufacturing, systems assembly and integration, design for manufacturability and design to specification work.

We focus on those markets where we believe we have the expertise, qualifications and leadership position to sustain a competitive advantage. We target our resources to support the needs of industry participants that embrace multi-year contractual relationships as a strategic component of their supply chain management. These contracts, many of which are sole-source by part number, historically have created opportunities to invest in leading-edge processes or technologies to help our customers remain competitive. The productivity and innovation that can result from such investments helps to differentiate us from our competition when it comes to cost, quality, reliability and customer service.

Our manufacturing processes frequently involve the fabrication or assembly of a product or subassembly according to specifications provided by our customers. We strive to enhance our manufacturing capabilities by advanced quality and manufacturing techniques, lean manufacturing, just-in-time procurement and continuous flow manufacturing, six sigma, total quality management, stringent and real-time engineering change control routines and total cycle time reduction techniques. At the same time, we are working to develop new designs and product innovations by re-engineering traditional solutions to eliminate cost without reducing durability or quality.

*Sypris Technologies.* Through Sypris Technologies, we are a significant supplier of forged and machined components, serving the commercial vehicle, off highway vehicle, light truck, automotive and energy markets in North America. We have the capacity to produce drive train components including axle shafts, transmission shafts, gear sets, steer axle knuckles, and other components for ultimate use by the leading automotive and truck manufacturers, including FCA US (Fiat Chrysler Automobiles), General Motors Company (GM), Nissan Motor Corporation (Nissan), Freightliner LLC (Freightliner), Mack Truck (Mack), Navistar International Corporation (Navistar), PACCAR, Inc. (PACCAR) and Volvo Truck Corporation (Volvo). We support our customers’ strategies to outsource non-core operations by supplying additional components and providing additional value added operations for drive train assemblies. We also manufacture high-pressure closures and other fabricated products for oil and gas pipelines.

Our manufacturing contracts for the truck components and assemblies markets are often sole-source by part number. Part numbers may be specified for inclusion in a single model or a range of models. Where we are the sole-source provider by part number, we are generally the exclusive provider to our customer of those specific parts for the duration of the manufacturing contract.

Sypris Technologies also manufactures energy-related products such as pressurized closures, insulated joints and other specialty products, primarily for oil and gas pipelines and related energy markets. This product line is an important source of diversified revenues and is becoming an area of greater focus for the Company going forward. We are committed to exploring new product developments and potential new markets, which will also be an increasing area of focus for the Company going forward.

Sypris Technologies represented approximately 70% of our net revenues in 2019.

*Sypris Electronics.* Sypris Electronics generates revenue primarily through circuit card and full box build manufacturing, high reliability manufacturing, systems assembly and integration, design for manufacturability and

design to specification, for customers in the aerospace and defense electronics markets. This includes circuit card assemblies for electronic sensors and systems including radar and targeting systems, tactical ground stations, navigation systems, weapons systems, targeting and warning systems and those used in the nation's high priority space programs.

We provide our customers with a broad variety of value added solutions, from low-volume prototype assembly to high-volume turnkey manufacturing. Our manufacturing contracts for the aerospace and defense electronics market are generally sole-source by part number. Our customers include large aerospace and defense companies such as Lockheed Martin Corporation (Lockheed Martin), Northrop Grumman Corporation (Northrop Grumman), L3Harris Technologies (L3Harris), Collins Aerospace Systems, BAE Systems (BAE) and Analog Devices, Inc. (ADI).

The engineering and manufacturing of highly complex components for the aerospace and defense industries is a fragmented industry with no dominant player in the market. The industry has continued to grow with more companies developing printed circuit board assembly capabilities and others entering the market via mergers and acquisitions of smaller companies. This competitive business environment, along with the impact of federal government spending uncertainties in the U.S. and the allocation of funds by the U.S. Department of Defense has challenged Sypris Electronics over the past several years.

We announced new program awards for Sypris Electronics that contributed to revenue in 2018 and 2019, with certain programs continuing into 2020. In addition to program awards related to weapons systems, electronic warfare and infrared countermeasures in our traditional aerospace and defense markets, we have also been awarded programs related to the communication and navigation markets which align with our capabilities for delivering products for complex, high cost of failure platforms. The President of the U.S. proposed a Fiscal Year 2020 budget requesting nearly \$750 billion for national security, which is expected to support program growth and market expansion during the coming year for aerospace and defense participants.

Certain electronic component shortages and extensive lead-time issues are prevalent in many of the segments in the electronic manufacturing industry that we serve. These shortages and extended lead times are expected to continue for the foreseeable future. We are working with our customers to qualify alternative components or suppliers to mitigate the impact on our business. The majority of our aerospace and defense programs require specific components that are sole-sourced from specific suppliers; therefore, the resolution of supplier constraints requires coordination with our customers or the end-users of the products.

Sypris Electronics accounted for approximately 30% of net revenue in 2019.

## **Our Markets**

*Sypris Technologies.* The industrial manufacturing markets include automotive, truck and off-highway components and assemblies and specialty closures. The automotive and truck components and assemblies market consists of the original equipment manufacturers, or OEMs, including FCA, Freightliner, GM, Mack, Navistar, PACCAR and Volvo, and an extensive supply chain of companies of all types and sizes that are classified into different levels or tiers. Tier 1 companies represent the primary suppliers to the OEMs and include Meritor, Dana Inc. (Dana), Detroit Diesel Corporation (Detroit Diesel), American Axle & Manufacturing Holdings, Inc. (America Axle) and Transmisiones y Equipos Mecanicos, S.A. de C.V. (Tremec), among others. Below this group of companies reside numerous suppliers that either supply the OEMs directly or supply the Tier 1 companies. In all segments of the truck components and assemblies, however, suppliers are under intense competitive pressure to improve product quality and to reduce capital expenditures, production costs and inventory levels. The Company has determined to migrate away from certain of its traditional Tier 1 customers in the commercial vehicle markets, while seeking to replace these customers with mutually beneficial relationships, especially among the heavy truck, off-highway and automotive OEMs, Tier 1 suppliers and others who place a higher value on the Company's innovation, flexibility and core commitment to lean manufacturing principles. The customers for our specialty closure products consists primarily of operators and builders of oil and gas pipelines, which are also facing significant pressures to improve quality, reduce costs and defer capital expenditures.

*Sypris Electronics* Although we believe that our programs are well aligned with national defense and other priorities, shifts in domestic and international spending and tax policy, changes in security, defense and intelligence

priorities, the affordability of our products, changes in or preferences for new or different technologies, general economic conditions, tariffs and other factors may affect the level of funding for existing or proposed programs.

Market conditions for our electronic manufacturing business are characterized by a number of obstacles. The nature of providing manufactured products to the aerospace and defense electronics industry as well as other regulated markets differs substantially from the commercial electronics manufacturing industry. The cost of failure can be extremely high, the manufacturing requirements are typically complex and products are produced in relatively small quantities. Companies within this industry are required to maintain and adhere to a number of strict and comprehensive certifications, security clearances and traceability standards.

## **Our Business Strategy**

Our objective is to improve our position in each of our core markets by increasing our number of multi-year relationships with customers and investing in highly innovative and efficient production capacity to remain competitive on a global scale. We intend to serve our customers and achieve this objective by continuing to:

*Concentrate on our Core Markets.* We are a significant supplier of forged, machined, welded and heat-treated components and subassemblies, serving the commercial vehicle, off highway vehicle, light truck and energy markets in North America. We have been an established supplier to major aerospace and defense companies and agencies of the U.S. Government for over 40 years. We will continue to focus on those markets where we have the expertise, capacity and qualifications to achieve a competitive advantage.

*Dedicate our Resources to Support Strategic Partnerships.* We will continue to prioritize our resources to support the needs of industry leaders that embrace multi-year contractual relationships as a strategic component of their supply chain management and have the potential for long-term growth. We prefer contracts that are sole-source by part number so we can work closely with the customer to the mutual benefit of both parties.

*Pursue the Strategic Acquisition of Assets.* Over the long-term, we may consider the strategic acquisition of assets to consolidate our position in our core markets, expand our presence outside the U.S., create or strengthen our relationships with leading companies and expand our range of products in return for multi-year supply agreements. We will consider assets that can be integrated with our core businesses and that can be used to support other customers, thereby improving asset utilization and achieving greater productivity, flexibility and economies of scale.

*Grow Through the Addition of New Value-Added Manufacturing Capabilities.* We hope to grow through the addition of new value-added manufacturing capabilities and the introduction of additional components in the supply chain that enable us to provide a more complete solution by improving quality and reducing product cost, inventory levels and cycle times for our customers. In many instances, we offer a variety of state-of-the-art machining capabilities to our customers in the industrial manufacturing markets that enable us to reduce labor and shipping costs and minimize cycle times for our customers over the long-term, which we believe will provide us with additional growth opportunities in the future.

We believe that the number and duration of our strategic relationships should grow to enable us to invest in our business with greater certainty and with less risk. The investments we make in support of these relationships are targeted to provide us with the productivity, flexibility, technological edge and economies of scale that we believe will help to differentiate us from the competition in the future when it comes to cost, quality, reliability and customer service.

## **Our Customers**

Our five largest customers in 2019 were Sistemas Automotrices de Mexico, S.A de C.V. (Sistemas), Detroit Diesel, Northrop Grumman, L3Harris and SubCom, which in the aggregate accounted for 61% of net revenue. Our five largest customers in 2018 were Sistemas, Northrop Grumman, Detroit Diesel, L3Harris and Jamison Products (Jamison), which in the aggregate accounted for 61% of net revenue. In 2019, Sistemas, Detroit Diesel and Northrop Grumman represented approximately 22%, 14% and 11% of our net revenue, respectively. No other customer accounted for more than 10% of our net revenue in 2019. In 2018, Sistemas, Northrop Grumman and Detroit Diesel represented approximately 19%, 14% and 14% of our net revenue, respectively. No other customer accounted for more than 10% of our net revenue in 2018.

## **Geographic Areas and Currency Fluctuations**

Our operations are located in the U.S. and Mexico. Our Mexican subsidiaries and affiliates are a part of Sypris Technologies and manufacture and sell a number of products similar to those Sypris Technologies produces or previously produced in the U.S. In addition to normal business risks, operations outside the U.S. may be subject to a greater risk of changing political, economic and social environments, changing governmental laws and regulations, currency revaluations and market fluctuations. Fluctuations in foreign currency exchange rates have primarily impacted our earnings only to the extent of remeasurement gains or losses related to U.S. dollar denominated accounts of our foreign subsidiaries, because the vast majority of our transactions are denominated in U.S. dollars. For the years ended December 31, 2019 and 2018, “other income, net” included foreign currency translation gains of \$0.2 million and \$0.1 million, respectively.

Net revenues from Mexican operations were \$40.5 million, or 46%, and \$39.7 million, or 45%, of our consolidated net revenues in 2019 and 2018, respectively. In 2019, net income from our Mexican operations was \$1.1 million, as compared to our consolidated net loss of \$3.9 million. In 2018, net income from our Mexican operations was \$1.6 million, as compared to our consolidated net loss of \$3.5 million. Revenues from our Mexican operations have grown significantly as a percentage of our consolidated net revenues, especially in connection with the shutdown of the Broadway Plant, which occurred at the end of 2017. You can find more information about our regional operating results, including our export sales, in Note 21 to our consolidated financial statements included in Item 8 of this Annual Report on Form 10-K.

## **Sales and Business Development**

Our principal sources of new business originate from the expansion of existing relationships, referrals and direct sales through senior management, direct sales personnel, domestic and international sales representatives, distributors and market specialists. We supplement these selling efforts with a variety of sales literature, advertising in trade media and participating in trade shows. We also utilize engineering specialists to facilitate the sales process by working with potential customers to reduce the cost of the products they need. Our specialists achieve this objective by working with the customer to improve their product’s design for ease of manufacturing or by reducing the amount of set-up time or material that may be required to produce the product. The award of contracts or programs can be a lengthy process, which in some circumstances can extend well beyond 24 months. Upon occasion, we commit resources to potential contracts or programs that we ultimately do not win.

Our objective is to increase the value we provide to the customer on an annual basis beyond the contractual terms that may be contained in a supply agreement. To achieve this objective, we commit to the customer that we will continuously look for ways to reduce the cost, improve the quality, reduce the cycle time and improve the life span of the products we supply the customer. Our ability to deliver on this commitment over time is expected to have a significant impact on customer satisfaction, loyalty and follow-on business.

We have signed long term supply agreements with Detroit Diesel, Volvo, Tremec and Sistemas. We have also been awarded purchase orders for various products and components from American Axle, Meritor, and Dana. We have launched the Sypris Ultra<sup>®</sup> axle shaft with Detroit Diesel and have strong interest from others within the customer base who are interested in this patented product. We are continuing to explore other opportunities as they arise and have a significant number of outstanding quotations in progress, but there can be no assurances that our efforts to develop new sources of revenues will be successful.

## **Competition**

The markets that we serve are highly competitive, and we compete against numerous domestic and international companies in addition to the internal capabilities of some of our customers. In the industrial manufacturing markets, we compete primarily against other component suppliers such as Ramkrishna Forgings Limited, Mid-West Forge, Inc., GNA Axles Limited, Brunner International, Inc., Bharat Forge, Commercial Forged Products, Spencer Forge and Machine, Inc., Traxle, SPX Flow, Inc., T.D. Williamson Inc. and National Oilwell Varco, Inc., certain of which serve as suppliers to many Tier I and smaller companies. In the aerospace and defense electronics market, we compete primarily against companies such as Celestica Inc., Jabil Circuit, Inc. and Spartan Corporation. We may face new competitors in the future as the outsourcing industry evolves and existing or start-up

companies develop capabilities similar to ours. In addition, we will face new competitors as we attempt to increase and expand our business.

We believe that the principal competitive factors in our markets include the availability of capacity, currency exchange rates (especially in low-cost countries), technological capability, flexibility, financial strength and timeliness in responding to design and schedule changes, price, quality and delivery. Although we believe that we generally compete favorably with respect to many of these factors, some of our competitors, as compared to us, are larger and have greater financial and operating resources, greater geographic breadth and range of products, customer bases and brand recognition than we do. We also face competition from manufacturing operations of our current and potential customers that continually evaluate the relative benefits of internal manufacturing compared to outsourcing.

## **Suppliers**

For portions of our business, we purchase raw materials and component parts from our customers or from suppliers chosen by our customers, at prices negotiated by our customers. When these suppliers increase their prices, cause delays in production schedules or fail to meet our customers' quality standards, these customers have typically agreed to reimburse us for the costs associated with such price increases and not to charge us for costs caused by such delays or quality issues. Accordingly, our risks are largely limited to accurate inspections of such materials, timely communications and the collection of such reimbursements or charges, along with any additional costs incurred by us due to delays in, interruptions of, or non-optimal scheduling of production schedules. However, for a meaningful part of our business, we arrange our own suppliers and assume the additional risks of price increases, quality concerns and production delays.

Raw steel and fabricated steel parts are a major component of our cost of sales and net revenue for the industrial manufacturing business. We purchase a portion of our steel for use in this business at the direction of our customers, with periodic changes in the price of steel being reflected in the prices we are paid for our products. Increases in the costs of steel or other supplies can increase our working capital requirements, scrap expenses and borrowing costs.

The Company has encountered higher than normal electronic component shortages and extended lead time issues due to shortages of certain components in the marketplace for the Sypris Electronics business. These shortages and extended lead times are expected to continue for the foreseeable future. This may result in higher prices, extension of our product delivery dates, and increased inventory levels for these components as we seek to secure the necessary components from our suppliers or alternative suppliers.

There can be no assurance that supply interruptions, tariffs or price increases will not slow production, delay shipments to our customers or increase costs in the future, any of which could adversely affect our financial results. Delays, interruptions or non-optimal scheduling of production related to interruptions in raw materials supplies can be expected to increase our costs.

## **Patents, Trademarks and Licenses**

We own or license a number of patents and trademarks, but our business as a whole is not materially dependent upon any one patent, trademark, license or technologically related group of patents or licenses.

We regard our manufacturing processes and certain designs as proprietary trade secrets and confidential information. We rely largely upon a combination of trade secret laws, non-disclosure agreements with customers, suppliers and consultants, and our internal security systems, confidentiality procedures and employee confidentiality agreements to maintain the trade secrecy of our designs and manufacturing processes.

## **Government Regulation**

Our operations are subject to compliance with regulatory requirements of federal, state and local authorities, in the U.S. and Mexico, including regulations concerning financial reporting and controls, labor relations, minimum pension funding levels, export and import matters, health and safety matters and protection of the environment. While compliance with applicable regulations has not adversely affected our operations in the past, there can be no assurance

that we will continue to be in compliance in the future or that these regulations will not change or that the costs of compliance will not be material to us.

We must comply with detailed government procurement and contracting regulations and with U.S. Government security regulations, certain of which carry substantial penalty provisions for nonperformance or misrepresentation in the course of negotiations. Our failure to comply with our government procurement, contracting or security obligations could result in penalties or our suspension or debarment from government contracting, which would have a material adverse effect on our consolidated results of operations.

We are required to maintain U.S. Government security clearances in connection with certain activities of Sypris Electronics. These clearances could be suspended or revoked if we were found not to be in compliance with applicable security regulations. Any such revocation or suspension would delay our delivery of products to customers. Although we have adopted policies designed to ensure compliance with applicable regulations, there can be no assurance that the approved status of our facilities or personnel will continue without interruption.

We are also subject to comprehensive and changing federal, state and local environmental requirements, both in the U.S. and in Mexico, including those governing discharges to air and water, the handling and disposal of solid and hazardous wastes and the remediation of contamination associated with releases of hazardous substances. We use hazardous substances in our operations and, as is the case with manufacturers in general, if a release of hazardous substances occurs on or from any properties that we may own or operate, we may be held liable and may be required to pay the cost of remedying the condition. The amount of any resulting liability could be material.

### **Employees**

As of December 31, 2019, we had a total of 630 employees, of which 456 were engaged in manufacturing, 15 were engaged in sales and marketing, 61 were engaged in engineering and 98 were engaged in administration. Approximately 359 of our employees were covered by collective bargaining agreements with various unions that expire on various dates through 2022. Excluding certain Mexico employees covered under an annually ratified agreement, there are no collective bargaining agreements expiring within the next 12 months. Our ability to maintain our workforce depends on our ability to attract and retain new and existing customers. Although we believe overall that relations with our labor unions are positive, there can be no assurance that present and future issues with our unions will be resolved favorably, that negotiations will be successful or that we will not experience a work stoppage, which could adversely affect our consolidated results of operations.

### **Internet Access**

Copies of our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to these reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 are available free of charge through our website ([www.sypris.com](http://www.sypris.com)) as soon as reasonably practicable after we electronically file the material with, or furnish it to, the Securities and Exchange Commission (“SEC”). The SEC maintains an internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, including us, at [www.sec.gov](http://www.sec.gov). The references to these website addresses do not constitute incorporation by reference of the information contained on the websites, which should not be considered part of this document.

## **Item 1A. Risk Factors**

### **Risks Related to Our Business and Forward-Looking Statements**

This annual report and our other oral or written communications may contain “forward-looking” statements. These statements include our expectations or projections about the future of our industries, business strategies, the markets in which we operate, potential acquisitions, contracts with customers, new business opportunities, controlling or cutting our costs, winning new customers, returning to profitability on a consolidated basis, our financial results, our financial condition and our views about developments beyond our control, including government spending, domestic or global economic conditions, trends and market forces. These statements are based on management’s views and assumptions at the time originally made, and we undertake no obligation to update these statements, except as may be required by law. There can be no assurance that our expectations, projections or views will come to pass, and you should not place undue reliance on these forward-looking statements.

A number of significant risk factors could materially affect our specific business operations and cause our performance to differ materially from any future results projected or implied by our prior statements, including those described below. Many of these risk factors are also identified in connection with the more specific descriptions contained throughout this report.

#### ***Customers and Revenue Growth***

**We have experienced recent operating losses, and anticipate further operating losses in the near term, as we seek to generate new business revenues to replace the nonrenewal of several large customer contracts.**

Our businesses generally require a higher level of new business revenues in order to operate profitably. We have recently experienced operating losses and may not become profitable if we are unable to execute on management’s plans. We are working to increase our revenues with new and existing customers. However, without near term success, we may be unable to maintain the critical mass of capital investments or talented employees that are needed to succeed in our chosen markets or to maintain our existing facilities, which could result in additional restructuring or exit costs. As we expand our customers and our products, we must also effectively manage a more diverse production schedule to avoid slowing our production output. As we are awarded new products with new customers, we must onboard new operational processes in an effective and efficient manner. There can be no assurance that we will be able to successfully complete final contract negotiations with regard to our announced contract “orders”, “wins” or “awards” or that these contracts will generate the additional revenue needed to return to profitability.

**We depend on a few key customers in challenging industries for most of our revenues.**

Our five largest customers in 2019 were Sistemas, Detroit Diesel, Northrop Grumman, L3Harris and SubCom, which in the aggregate accounted for 61% of net revenue. While we have reduced the dependence of Sypris Technologies on certain non-strategic customers, an inability to increase our revenues while effectively controlling our costs would materially adversely affect our business, results of operations and financial condition. In 2020 and beyond, we will need to continue attracting new clients and diversifying our customer base, despite the longer lead times typically required for new programs.

The truck components and assemblies industry has experienced consolidation, credit risk, highly cyclical market demand, labor unrest, rising steel costs, bankruptcy and other obstacles. We expect the North America truck market’s economic climate to deteriorate as compared to 2019. The medium/heavy truck market in North America is expected to be down considerably in 2020, with Class 8 demand down over 30% and Classes 5-7 lower by approximately 10% compared to 2019. In the light vehicle market, light truck demand in 2020 is expected to be comparable to slightly weaker than 2019. The demand for our energy-related products lines, historically, has risen and fallen with the prices of oil and/or natural gas, as our customers’ capital expenditures budgets tend to be dependent upon energy prices. We depend on the continued growth and financial stability of customers in these industries and our core markets, as well as general economic conditions. Adverse changes affecting these customers, markets or economic conditions could harm our operating results.

The aerospace and defense electronics industry has experienced consolidation, increased competition, disruptive new technologies and uncertain funding levels. The aerospace and defense industry is also pressured by cyclical, rapid technological change, shortening product life cycles, decreasing margins, component obsolescence and shortages and government procurement and certification processes. Our aerospace and defense business faces reduced revenues in the final phases of several key legacy programs which must be replenished with new technologies if we are to successfully maintain or expand our market share. Our failure to address any of these factors could impair our ability to grow and diversify our base of customers in this segment.

There can be no assurance that any of our customers will not default on, delay or dispute payment of, or seek to reject our outstanding invoices in bankruptcy or otherwise. In addition, the existence of these factors may result in fewer customers in our target markets due to consolidation, bankruptcy, competitive or other market reasons, making it more difficult to obtain new clients and diversify our customer base in the near future.

**Customer contracts could be less profitable than expected.**

We generally bear the risk that our contracts could be unprofitable or less profitable than planned, despite our estimates of revenues and future costs to complete such contracts.

A material portion of our business, historically, has been conducted under multi-year contracts, which generally include fixed prices or periodic price reductions without minimum purchase requirements. Over time, our revenues may not cover any increases in our operating costs which could adversely impact our results. Our financial results are at greater risk when we accept contractual responsibility for raw material or component prices, when we cannot offset price reductions, freight penalties, importation fees and cost increases with operating efficiencies or other savings, when we must submit contract bid prices before all key design elements are finalized or when we are subjected to other competitive pressures which erode our margins. The profitability of our contracts also can be adversely affected by unexpected start-up costs on new programs, inability to negotiate milestone billings, operating inefficiencies, scheduling constraints, ineffective capital investments, inflationary pressures or inaccurate forecasts of future unit costs.

Unexpected changes in our customers' demand levels and our ability to execute our production efficiently have harmed our operating results in the past and could do so in the future. Many of our customers will not commit to firm production or delivery schedules. Inaccurate forecasting of our customers' requirements can disrupt the efficient utilization of our manufacturing capacity, inventories or workforce and can cause increases in our inventory and working capital levels. If we receive unanticipated orders or rapid increases in demand, these incremental volumes could be unprofitable due to the higher costs of operating above our optimal capacity. Disagreements over pricing, quality, delivery, capacity, exclusivity or trade credit terms could disrupt order schedules. Orders may also fluctuate due to changing global capacity and demand, new products, changes in market share, reorganizations or bankruptcies, material shortages, labor disputes, freight costs, tariffs or other factors that discourage outsourcing. These forces could increase, decrease, accelerate, delay or cancel our delivery schedules.

Our ability to stabilize employee retention and execute on existing customer orders could put current revenues at risk as we proceed with the execution of our plans. If we lose anticipated revenues, we might not succeed in redeploying our substantial capital investments and other fixed costs, potentially forcing additional plant closures, impairments of long-lived and other assets or increased losses.

**Congressional budgetary constraints or reallocations could reduce our government related sales.**

Sypris Electronics serves as a contractor for large aerospace and defense companies such as Northrop Grumman, Lockheed Martin and L3Harris, typically under federally funded programs, which represented approximately 23% and 25% of net revenue in 2019 and 2018, respectively.

Sypris Electronics was adversely affected by declines in the overall government defense market due to the effects of sequestration in the past, and may be further affected if funding for programs in which we participate, either by selling products directly to U.S. government agencies or as a subcontractor to prime contractors such as Northrop Grumman, L3Harris, SubCom, LLC (SubCom) and ADI, is reduced, delayed or cancelled. Our ability to obtain new contract awards also could be negatively affected.

## ***Competition***

### **Increasing competition could limit or reduce our market share.**

As an outsourced manufacturer, we operate in highly competitive environments that often include our customers' internal capabilities. We believe that the principal competitive factors in our markets include the availability of manufacturing capacity, increasingly unfavorable currency exchange rates (especially in low-cost countries), technological strength, speed and flexibility in responding to design or schedule changes, price, quality, delivery, cost management and financial strength. Our earnings could decline if our competitors or customers can provide comparable speed and quality at a lower cost, or if we fail to adequately invest in the range and quality of products our customers require.

Many of our competitors are larger and have greater financial and organizational resources, geographic breadth and range of products, customer bases and brand recognition than we do. As a result, our competitors may respond more quickly to technological changes or customer needs, consume lower fixed and variable unit costs, negotiate reduced component prices, and obtain better terms for financing growth. If we fail to compete in any of these areas, we may lose market share and our business could be seriously harmed. There can be no assurance that we will not experience increased competition or that we will be able to achieve profitability as these new challenges arise.

### **Our technologies could become obsolete, reducing our revenues and profitability.**

The markets for our products are characterized by changing technology and continuing process development. The future of our business will depend in large part upon the continuing relevance of our technological capabilities. We could fail to make required capital investments, develop or successfully market products that meet changing customer needs and anticipate or respond to technological changes in a cost-effective and timely manner. Our inability to successfully launch or sustain new or next generation programs or product features, especially in accordance with budgets or committed delivery schedules, could materially adversely affect our financial results. We could encounter competition from new or developing technologies that render our technologies and equipment less profitable or obsolete in our chosen markets and our operating results may suffer. In particular, the Company is currently developing new products and pursuing new programs in an attempt to increase Sypris Electronics' revenue stream. However, commercializing the new products and programs is costly and has been slower than anticipated. The launch of any new products or programs within Sypris Electronics may not be successful.

## ***Execution***

### **Contract terminations or delays could harm our business.**

We often provide products under contracts that contain detailed specifications, quality standards and other terms. If we are unable to perform in accordance with such terms, our customers might seek to terminate such contracts, demand price concessions or other financial consideration or downgrade our performance ratings or eligibility for new business. Moreover, many of our contracts are subject to termination for convenience or upon default. These provisions could provide only limited recoveries of certain incurred costs or profits on completed work and could impose liability for our customers' costs in procuring undelivered items from another source. If any of our significant contracts were to be repudiated, terminated or not renewed, we could lose substantial revenues, and our operating results as well as prospects for future business opportunities could be adversely affected.

We are subject to various audits, reviews and investigations, including private party "whistleblower" lawsuits, relating to our compliance with federal and state laws. Should our business be charged with wrongdoing, or determined not to be a "presently responsible contractor," we could be temporarily suspended or debarred from receiving new government contracts or government-approved subcontracts.

### **We must operate more efficiently due to lower revenues.**

If we are unable to improve the cost, efficiency and yield of our operations, and if we are not able to control costs, our financial results could suffer and we could be forced to sell additional assets, take on additional debt at higher costs or take other measures to restructure our operations or capital structure. A number of major obstacles could include:

- difficulties arising from our present financial condition, including difficulties in maintaining customer and supplier relationships and difficulties acquiring new business due to lingering concerns until we have returned to consistent profitability;
- efforts to increase our manufacturing capacity, maintain quality control systems and launch new programs, especially as we increase production at our Mexico operations;
- the breakdown or the need for major repairs of critical machinery or equipment, especially as we increase production at our Mexico operations;
- the risk of warranty and product liability claims, as well as product recalls, if our products fail to perform to specifications or cause property damage, injury or death;
- inflationary pressures;
- tariffs or trade restrictions imposed on imports or exports, particularly in the United States and Mexico;
- increased borrowing due to declines in sales;
- changes in anticipated product mix and the associated variances in our profit margins;
- the need to identify and eliminate our root causes of scrap;
- our ability to achieve expected annual savings or other synergies from past and future business combinations;
- inventory risks due to forecasting errors, shifts in market demand, the unanticipated loss of future business, or the obsolescence and/or price erosion of raw materials or component parts on hand;
- any inability to successfully manage growth, contraction or competitive pressures in our primary markets.

Our management or systems could be inadequate to support our existing or future operations, especially as we downsize our operating staff to reduce expenses while we work to increase revenues. New customers or new contracts, particularly with new product offerings, could require us to invest in additional equipment or other capital expenditures which exceed our budgeted plans. We may have limited experience or expertise in installing or operating such equipment, which could negatively impact our ability to deliver products on time or with acceptable costs. In addition, a material portion of our manufacturing equipment requires significant maintenance to operate effectively, and we may experience maintenance and repair issues. The risk of technical failures, nonconformance with customer specifications, an inability to deliver next generation products or other quality concerns could materially impair our operating results. Similarly, expanding production for our energy-related products without effective process controls could materially increase scrap rates and may impact the safety of our operating environment.

**Cyber security risks could negatively affect operations and result in increased costs.**

Sypris Electronics, as a U.S. defense contractor, and our Company overall, face cyber security threats, threats to the physical security of our facilities and employees and terrorist or criminal acts, as well as the potential for business disruptions associated with information technology failures and natural disasters.

We routinely experience cyber security threats, threats to our information technology infrastructure and attempts to gain access to our sensitive information, as do our customers, suppliers and subcontractors. Prior cyber attacks directed at us have not had a material impact on our financial results. Due to the evolving nature of these security threats, however, the impact of any future incident cannot be predicted.

Although we work cooperatively with our customers and our suppliers, subcontractors, and other partners to seek to minimize the impacts of cyber threats, other security threats or business disruptions, we must rely on the safeguards put in place by those entities, and those safeguards might not be effective.

The costs related to cyber security or other security threats or disruptions may not be fully insured or indemnified by other means. Occurrence of any of these events could adversely affect our internal operations, the products we provide to customers, loss of competitive advantages derived from our research and development efforts, early obsolescence of our products, our future financial results, our reputation or our stock price.

### *Suppliers*

#### **Interruptions in the supply of key components and quality systems could disrupt production.**

Some of our products require one or more components that are available from a limited number of providers or from sole-source providers. In the past, some of the materials we use, including steel, certain forgings or castings, capacitors and memory and logic devices, have been subject to industry-wide shortages or capacity allocations. As a result, suppliers have been forced to allocate available quantities among their customers, and we have not been able to obtain all of the materials desired. Some of our suppliers have struggled to implement reliable quality control systems which can negatively impact our operating efficiency and financial results. In downward business cycles, the tightening of credit markets has threatened the financial viability of an increasing number of suppliers of key components and raw materials and forced unanticipated shutdowns. Our inability to reliably obtain these or any other materials when and as needed could slow production or assembly, delay shipments to our customers, cause noncompliance with product certifications, impair the recovery of our fixed costs and increase the costs of recovering to customers' schedules, including overtime, expedited freight, equipment maintenance, operating inefficiencies, higher working capital and the obsolescence risks associated with larger buffer inventories. Each of these factors could adversely affect operating results.

#### **Shortages or increased costs of utilities could harm our business and our customers.**

We and our customers depend on a constant supply of electricity and natural gas from utility providers for the operation of our respective businesses and facilities. In the past, we have experienced power outages which reduced our ability to deliver products and meet our customers' demand for those products. If we or our customers experience future interruptions in service from these providers, our production and/or delivery of products could be negatively affected. We have experienced increased costs due to the heavy consumption of energy in our production process, which have been offset through revised production schedules. However, if the cost of energy continues to increase, our results of operations and those of certain customers could be negatively impacted.

#### **Fluctuations in the price of raw materials, including tariffs or other trade restrictions on imported steel or other goods, could negatively impact us.**

For significant portions of our business, we purchase raw materials and component parts which have been designated or specified by our customers, at prices negotiated by our customers. Raw material price fluctuations and volatility in the commodity markets, including tariffs and trade restriction could impact prices in the future. While our customers have generally agreed to reimburse us for the cost of such materials, this could change in the future, and our risks will continue to include the timely communication and successful collection of any such reimbursements. In any event, for a growing part of our business, we arrange our own suppliers and we could be impacted by the risks of any landed price increases, trade restrictions or production delays. Increases in the costs of steel or other supplies could also increase our working capital requirements, scrap expenses and borrowing costs.

In general, there can be no assurance that any price fluctuations relating to tariffs or trade restrictions will not reduce demand, slow production, delay shipments to our customers or increase our costs in the future, any of which could adversely affect our financial results.

### *Access to Capital and Acquisitions*

#### **Until we have returned to sustained levels of profitability, our access to capital may be limited.**

Until the Company becomes profitable again, there can be no assurances that the Company will succeed in attracting new, affordable, sources of debt or equity capital. If we are unable to become profitable on a timely basis, we may need to use existing cash resources or other assets to fund operating losses. While we have borrowed from Gill Family Capital Management, Inc. (“GFCM”) on acceptable terms in the past, there can be no assurances that such debt financing would be available in the future.

#### **Our ability to finance expansion or new business opportunities may be limited.**

Our future liquidity and capital requirements depend on numerous factors other than bank borrowings or debt financing, including the pace at which we can effectively cut costs, increase revenues or successfully launch new products. One method we have historically used to increase our revenues and obtain multi-year supply agreements is to buy a customer’s non-core manufacturing assets, or to acquire alternative, but equivalent, production capabilities and to produce products for such customers under a multi-year contract. We have also pursued strategies that rely on research and development efforts to develop and commercialize our new products. We may not have the financial resources or be able to raise funds necessary to pursue these strategies under our future debt agreements which could further limit our ability to replace the loss of revenues.

#### **Our growth strategies could be ineffective due to the risks associated with further acquisitions.**

Our growth strategy has included acquiring complementary businesses. We could fail to identify, obtain financing or complete suitable acquisitions on acceptable terms and prices. Acquisition efforts entail a number of risks, including: diversion of management’s attention; difficulties in integrating systems, operations and cultures; potential loss of key employees and customers of the acquired companies; lack of experience operating in the geographic market of the acquired business; an increase in our expenses and working capital requirements; risks of entering into markets or producing products where we have limited or no experience; difficulties in integrating purchased technologies and products with our technologies and products; our ability to improve productivity and implement cost reductions; our ability to secure collective bargaining agreements with employees; and exposure to unanticipated liabilities.

Our discovery of, or failure to discover, material issues during due diligence investigations of acquisition targets, either before closing with regard to potential risks of the acquired operations, or after closing with regard to the timely discovery of breaches of representations or warranties, or of certain indemnified environmental conditions, could seriously harm our business.

#### **We could fail to fully implement our growth plans.**

As the Company seeks to expand its revenues and strategically diversify its customer base, we could fail to adequately overcome significant obstacles such as slowing markets, the loss of key employees, unexpected increases in costs, or new competitors or technologies in our key markets, among other risks. The failure to fully implement our growth plans could materially adversely affect our revenues, operating results and financial condition.

### *Labor Relations*

#### **We must attract and retain qualified employees while successfully managing related costs.**

Our future success in a changing business environment, including during rapid changes in the size, complexity or skills required of our workforce, as we experienced in 2018 and 2017, will depend to a large extent upon the efforts and abilities of our executive, managerial and technical employees. The loss of key employees, especially in a strong economic environment, and our ability to effectively train existing employees, could have a material adverse effect on our operations. Our future success will also require an ability to attract and retain qualified employees, especially those with engineering or production expertise in our core business lines.

Changes in our labor costs such as salaries, wages and benefits, or the cost of providing pension and other employee benefits, changes in health care costs, investment returns on plan assets and discount rates used to calculate pension and related liabilities or other requirements to accelerate the level of our pension fund contributions to reduce or eliminate underfunded liabilities, could lead to increased costs or disruptions of operations in any of our business units.

**Disputes with labor unions could disrupt our business plans.**

As of December 31, 2019, we had collective bargaining agreements covering approximately 359 employees (all of which were in Sypris Technologies), or 57% of our total employees. Excluding certain Mexico employees covered under an annually ratified agreement, there are no collective bargaining agreements expiring within the next 12 months. Certain Mexico employees are covered by an annually ratified collective bargaining agreement. These employees in Mexico represented approximately 51% of the Company's workforce, or 319 employees at December 31, 2019. Our ability to maintain our workforce depends on our ability to attract and retain new and existing customers. We could experience a work stoppage or other disputes which could disrupt our operations or the operations of our customers and could harm our operating results.

***Regulatory***

**Environmental, natural disasters, health and safety risks could expose us to potential liability.**

We are subject to a variety of environmental regulations relating to the use, storage, discharge and disposal of hazardous chemicals and substances used in our operations. If we fail to comply with present or future regulations, we could be forced to alter, suspend or discontinue our manufacturing processes and pay substantial fines or penalties.

Groundwater and other contamination has occurred at certain of our current and former facilities during the operation of those facilities by their former owners, and this contamination may occur at future facilities we operate or acquire. There is no assurance that environmental indemnification agreements we have secured from the former owners of certain of these properties will be adequate to protect us from liability.

Our business is also subject to potential liabilities with respect to health and safety matters. We are required to comply with federal, state, local and foreign laws and regulations governing the health and safety of our workforce, and we could be held liable for damages arising out of human exposure to hazardous substances or other dangerous working conditions. Health and safety laws and regulations are complex and change frequently. As a result, our future costs to comply with such laws or the liabilities incurred in the event of any violations may increase significantly.

A natural disaster could disrupt our operations, or our customers' or suppliers' operations and could adversely affect our results of operations and financial condition. Although we have plans designed to mitigate the impact of natural disasters on our operations, those plans may be insufficient, and any catastrophe may disrupt our ability to manufacture and deliver products to our customers, resulting in an adverse impact on our business and results of operations. In addition, our global operations expose us to risks associated with public health crises, such as pandemics and epidemics, which could harm our business and cause our operating results to suffer. For example, during December 2019 and the first quarter of 2020, an outbreak of a new strain of coronavirus in Wuhan, China has resulted in travel disruption, trade disruption and has effected certain companies' operations in China and several other countries. At this point in time, the extent to which the coronavirus may impact our results is uncertain. Infections may become more widespread, including to other countries where we have operations, and travel restrictions may remain or worsen, all of which could lead to reduced demand for our products and services, disruptions in our supply chain, any of which could have a negative impact on our business and operating results. Under our self-insured employee health program, the costs associated with a large number of employees infected could significantly impact our results.

**Changes in interest rates and asset returns could increase our pension funding obligations and reduce our profitability.**

We have unfunded obligations under certain of our defined benefit pension plans. The valuation of our future payment obligations under the plans and the related plan assets are subject to significant adverse changes if the credit

and capital markets cause interest rates and projected rates of return to decline. Such declines could also require us to make significant additional contributions to our pension plans in the future. A material increase in the unfunded obligations of these plans could also result in a significant increase in our pension expense in the future.

**We may incur additional tax expense or become subject to additional tax exposure.**

Our provision for income taxes and the cash outlays required to satisfy our income tax obligations in the future could be adversely affected by numerous factors. These factors include changes in the level of earnings in the tax jurisdictions in which we operate, changes in the valuation of deferred tax assets and liabilities, changes in our plans to repatriate the earnings of our non-U.S. operations to the U.S. and changes in tax laws and regulations.

In December 2017, the U.S. introduced broad ranging tax reform with the passage of the Tax Cuts and Jobs Act (“Act”) legislation. Among the tax reforms was a reduction of the corporate tax rate from 35% to 21%. Although the tax reform in the U.S. reduced the statutory tax rate to 21% for 2018, the effects of the lower rate were offset in part by the effects of increased nondeductible expenses and the global intangible low taxed income (“GILTI”) provisions which result in a certain amount of foreign earnings being subjected to U.S. tax. Considering the exclusion of foreign subsidiary dividends from taxation in the U.S., we believe the Act will provide some greater flexibility to repatriate future earnings of our foreign operations.

Our income tax returns are subject to examination by federal, state and local tax authorities in the U.S. and tax authorities outside the U.S. The results of these examinations and the ongoing assessments of our tax exposures could also have an adverse effect on our provision for income taxes and the cash outlays required to satisfy our income tax obligations.

**Adverse regulatory developments or litigation could harm our business.**

Our businesses operate in heavily regulated environments. We must successfully manage the risk of changes in or adverse actions under applicable law or in our regulatory authorizations, licenses and permits, governmental security clearances or other legal rights to operate our businesses, to manage our work force or to import and export goods and services as needed. Our business activities expose us to the risks of litigation with respect to our customers, suppliers, creditors, stockholders or from product liability, environmental or asbestos-related matters. We also face the risk of other adverse regulatory actions, compliance costs or governmental sanctions, as well as the costs and risks related to our ongoing efforts to design and implement effective internal controls.

***Other Risks***

**If we fail to establish and maintain proper internal controls, our ability to produce accurate financial statement or comply with applicable regulations could be impaired.**

Under Section 404(a) of the Sarbanes-Oxley Act, our management is required, among other things, to assess and report annually on the effectiveness of our internal control over financial reporting and identify any material weaknesses in our internal control over financial reporting. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”). Any failure to implement required new or improved controls, or difficulties encountered in their implementation, could cause us to fail to meet our reporting obligations.

We previously identified material weaknesses in internal control over financial reporting that pertain to our ERP system conversion that took place on January 1, 2019 involving (1) the ineffective design and implementation of effective controls with respect to the ERP system conversion, and (2) inadequate or ineffective process level and monitoring controls in the area of accounting close and financial reporting. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. Although we believe the material weakness has since been remediated, we cannot assure that the measures we have taken to date, and are continuing to implement, or any measures we may take in the future, will be sufficient to identify or prevent future material weaknesses. If other material weaknesses or other deficiencies occur, our ability to

accurately and timely report our financial position could be impaired, which could result in a material misstatement of our financial statements that would not be prevented or detected on a timely basis.

**Implementation of our new enterprise resource planning system has adversely impacted and could continue to negatively affect our business.**

We rely extensively on our information technology (“IT”) systems to assist us in managing our business and summarizing our operational results. On January 1, 2019 we deployed a new ERP system at Sypris Electronics. The new ERP system was implemented to position the Company for long-term growth, further enhance operating efficiencies and provide more effective management of our business operations, including sales order processing, inventory control, purchasing and supply chain management, and financial reporting. Implementing the new ERP system has been costly and has required, and may continue to require, the investment of significant personnel and financial resources. In addition to the risks inherent in the conversion to any new IT system, including the loss of information, disruption to our normal operations, and changes in accounting procedures, the implementation of our new ERP system has resulted in reporting disruptions related to maintaining an effective internal control environment.

Failure to properly or adequately address any issues with our new ERP system could result in increased costs and the diversion of management’s and employees’ attention and resources and could materially adversely affect our operating results, internal control over financial reporting and ability to manage our business effectively. While the ERP system is intended to further improve and enhance our information management systems, the ongoing implementation of this new ERP system exposes us to the risks of integrating that system with our existing systems and processes, including possible continued disruption of our financial reporting.

**Our insurance coverage may be inadequate to cover all significant risk exposures.**

We carry a range of insurance policies intended to protect our assets and operations, including general liability insurance and property damage insurance. While we endeavor to purchase insurance coverage appropriate to our risk assessment, we are unable to predict with certainty the frequency, nature or magnitude of claims for direct or consequential damages, and as a result our insurance program may not fully cover us for losses we may incur. In addition, as a result of a number of catastrophic weather and other events in the United States, insurance companies have incurred substantial losses and accordingly in many cases they have substantially reduced the nature and amount of insurance coverage available to the market, have broadened exclusions, and/or have substantially increased the cost of such coverage. It is likely that the tight insurance market will continue into the foreseeable future. Our business requires that we maintain various types of insurance. If such insurance is not available or not available on economically acceptable terms, our business could be materially and adversely affected.

**We face other factors which could seriously disrupt our operations.**

Many other risk factors beyond our control could seriously disrupt our operations, including: risks relating to war, future terrorist activities, or political uncertainties; risks relating to natural disasters or other casualties which could shut down our domestic or foreign facilities, disrupt transportation of products or supplies, increase the costs under our self-insurance program or change the timing and availability of funding in our aerospace and defense electronics markets; risks inherent in operating abroad, including foreign currency exchange rates, adverse regulatory developments, and miscommunications or errors due to inaccurate foreign language translations or currency exchange rates; or our failure to anticipate or to adequately insure against other risks and uncertainties present in our businesses including unknown or unidentified risks.

**Item 1B. Unresolved Staff Comments**

None.

## Item 2. Properties

Our principal manufacturing operations are engaged in electronics manufacturing for our aerospace and defense customers and industrial manufacturing for our truck components and assemblies and oil and gas pipeline component customers. The following chart indicates the significant facilities that we own or lease, the location and size of each such facility and the manufacturing certifications that each facility possesses. The facilities listed below (other than the corporate office) are used principally as manufacturing facilities.

Location	Segment (Market Served)	Own or Lease (Expiration)	Approximate Square Feet	Certifications
<i>Corporate Office:</i>				
Louisville, Kentucky		Lease (2024)	13,800	
<i>Manufacturing Facilities:</i>				
Louisville, Kentucky	Sypris Technologies (Oil & Gas Pipeline Components)	Own	57,000	ISO 9001
Tampa, Florida	Sypris Electronics (Aerospace & Defense Electronics)	Lease (2027)	50,000	ISO 9001 ISO 13485 ISO 14001 AS 9100 AS5553 NASA-STD-8739 IPC-A-610, Rev D, Class 3 J-STD-001, Rev D, Class 3 NADCAP accredited
Toluca, Mexico	Sypris Technologies (Truck Components and Oil & Gas Pipeline Components)	Lease (2026)	215,000	TS 16949 ASME Certified Clean Industry Certified

The Company also owns a 450,000 square foot facility in Louisville, Kentucky (the “Broadway Plant”), which is included in Assets held for sale as of December 31, 2019.

Below is a listing and description of the various manufacturing certifications or specifications that we utilize at various of our facilities.

<u>Certification/Specification</u>	<u>Description</u>
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AS 9100.....	A quality management system developed by the aerospace industry to measure supplier conformance with basic common acceptable aerospace quality requirements.
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AS 5553.....	A certification process intended for use by aerospace and military manufactures to mitigate the risk of receiving and installing counterfeit electronic parts.
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ASME Certified.....	Performance criteria determined by the American Society of Mechanical Engineers.
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Clean Industry Certified ...	Mexican Environmental Protection Agency sponsored voluntary regulatory program for pollution control.
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<u>Certification/Specification</u>	<u>Description</u>
IPC-A-610 .....	A certification process for electronics assembly manufacturing which describes materials, methods and verification criteria for producing high quality electronic products. Class 3 specifically includes high performance or performance-on-demand products where equipment downtime cannot be tolerated, end-use environment may be uncommonly harsh, and the equipment must function when required.
J-STD-001 .....	A family of voluntary standards of industry-accepted workmanship criteria for electronic assemblies.
ISO 9001 .....	A certification process comprised of quality system requirements to ensure quality in the areas of design, development, production, installation and servicing of products.
ISO 14001 .....	A family of voluntary standards and guidance documents defining specific requirements for an Environmental Management System.
ISO 13485 .....	An internationally recognized voluntary system of quality management for companies that design, develop, manufacture, distribute, and service medical devices.
NADCAP accredited .....	The National Aerospace and Defense Contractors Accreditation Program is a global cooperative accreditation program for aerospace engineering, defense and related industries.
NASA-STD-8739.....	A specification for space programs designated by the National Aeronautics and Space Administration.
TS 16949.....	A quality certification system developed within the automotive sector. Using ISO 9001:2000 as its foundation, ISO/TS 16949:2002 specifies the quality management system (QMS) requirements for the design, development, production, installation and servicing of automotive related products.

**Item 3. Legal Proceedings**

Groundwater and other contamination has occurred at certain of our current and former facilities during the operation of those facilities by their former owners, and this contamination may occur at future facilities we operate or acquire. There is no assurance that environmental indemnification agreements we have secured from the former owners of certain of these properties will be adequate to protect us from liability. No administrative or judicial proceedings with respect to these or any other environmental regulations or conditions are pending against the Company or known by the Company to be contemplated by Government authorities.

The Company is subject to other legal proceedings and claims that have not been fully resolved and that have arisen in the ordinary course of business. In the opinion of management, there was not at least a reasonable possibility the Company may have incurred a material loss, or a material loss in excess of a recorded accrual, with respect to loss contingencies for these other asserted legal and other claims. However, the outcome of legal proceedings and claims brought against the Company is subject to significant uncertainty. In addition, there may be other potential claims, liabilities, materials or design defects, or other customer complaints that have not been asserted, but which could adversely impact us in the future. Therefore, although management considers the likelihood of such an outcome to be remote, if one or more of these other legal matters or potential matters were resolved against the Company in a reporting period for amounts in excess of management’s expectations, the Company’s consolidated financial statements for that reporting period could be materially adversely affected.

**Item 4. Mine Safety Disclosures**

Not applicable.

## PART II

### **Item 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

We are a smaller reporting company as defined in Item 10(f)(1) of Regulation S-K and thus are not required to provide the performance graph required in paragraph (e) of Item 201 of Regulation S-K.

Our common stock is traded on the NASDAQ Global Market under the symbol "SYPR."

As of March 9, 2020, there were 584 holders of record of our common stock. No cash dividends were declared during 2019 or 2018.

Dividends may be paid on common stock only when, as and if declared by our Board of Directors in its sole discretion. We do not anticipate paying dividends in 2020.

There were no shares of common stock repurchased during the three months ended December 31, 2019.

### **Item 6. Selected Financial Data**

We are a smaller reporting company as defined in Item 10(f)(1) of Regulation S-K and thus are not required to report the selected financial data in Item 301 of Regulation S-K.

## Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion of our consolidated results of operations and financial condition should be read together with the other financial information and consolidated financial statements included in this Annual Report on Form 10-K. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from the results anticipated in the forward-looking statements as a result of a variety of factors, including those discussed in “Item 1A. Risk Factors” and elsewhere in this Annual Report on Form 10-K.

### Overview

We are a diversified provider of truck components, oil and gas pipeline components and aerospace and defense electronics. We offer a wide range of manufactured products, often under multi-year sole-source contracts.

We are organized into two business segments, Sypris Technologies and Sypris Electronics. Sypris Technologies, which is comprised of Sypris Technologies, Inc. and its subsidiaries, generates revenue primarily from the sale of forged, machined, welded and heat-treated steel components primarily for the heavy commercial vehicle and high-pressure energy pipeline applications. Sypris Electronics, which is comprised of Sypris Electronics, LLC, generates revenue primarily through circuit card and full “box build” manufacturing, high reliability manufacturing, systems assembly and integration, design for manufacturability and design to specification work.

We focus on those markets where we believe we have the expertise, qualifications and leadership position to sustain a competitive advantage. We target our resources to support the needs of industry participants that embrace technological innovation and flexibility, coupled with multi-year contractual relationships, as a strategic component of their supply chain management. These contracts, many of which are sole-source by part number, have historically created opportunities to invest in leading-edge processes or technologies to help our customers remain competitive. The productivity and innovation that can result from such investments helps to differentiate us from our competition when it comes to cost, quality, reliability and customer service.

### *Sypris Technologies Outlook*

During 2016, the continued strength of the U.S. dollar, the tightening of margins in certain sectors of the commercial vehicle markets and the generally softening of certain key market segments led us to reevaluate the strategic importance of each of our customers to the Sypris Technologies’ long-term success. We have reduced our reliance on certain traditional Tier 1 customers that represent the primary suppliers to the original equipment manufacturers (“OEMs”) in the commercial vehicle markets, while targeting to replace these customers with more diversified, longer-term relationships, especially among the OEMs and others who place a higher value on our innovation, flexibility and core commitment to lean manufacturing principles.

We are pursuing new business in a wide variety of markets from light automotive to new energy related product lines to achieve a more balanced portfolio across our customers, markets and products. We have recently announced new program awards in each of these markets that have contributed to revenue growth for Sypris Technologies in 2018 and 2019.

After two years of record high volumes, the commercial vehicle market softened materially during the fourth quarter of 2019, impacting production rates as customers responded to the demand reduction and balanced inventory levels. We expect this softness to continue in the near term, as industry analysts expect North American Class 8 shipments to decline 29% and Class 4-7 to decline 8% in 2020. Class 8 shipments in the years 2020 through 2022 are expected to be in line with the historical average replacement volume of 240,000 units per year. We believe Sypris Technologies’ recently announced program awards provide a solid multi-year foundation for growth and that additional prospective business may result in increased revenue going forward to help offset the anticipated short-term cyclical decrease in production volumes in the commercial vehicle market.

The oil and gas markets, served by our Tube Turns® brand of engineered product lines, have strengthened along with the overall economy, and domestic pipeline projects continue to be active with U.S. domestic gas and oil production increasing in 2018 and 2019. We are committed to exploring new product developments and potential new markets, which will be an increasing area of focus for the Company going forward.

## *Sypris Electronics Outlook*

In the past few years, we have faced challenges within Sypris Electronics, including the emergence of new competitors to our manufacturing capabilities. Additionally, certain electronic component shortages and extensive lead-time issues are prevalent in many of the segments in the electronic manufacturing industry that we serve. This had a negative impact on our production schedules and margin performance in 2018 and 2019. We have partnered with our customers to qualify alternative components or suppliers and will continue to exercise our supply chain to mitigate the impact on our business. We expect that these issues will be resolved for some component shortages, but overall component shortages may persist as a challenge throughout 2020. The majority of our aerospace and defense programs require specific components that are sole-sourced to specific suppliers; therefore, the resolution of supplier constraints requires coordination with our customers or the end-users of the products. As a result, there can be no assurance that we will be successful in addressing these shortages and issues.

Despite these challenges, in 2018 and 2019, we announced new program awards for Sypris Electronics that contributed to revenue in 2019, with certain programs continuing into 2020. In addition to program awards related to weapons systems, electronic warfare and infrared countermeasures in our traditional aerospace and defense markets, we have also been awarded programs related to the communication and navigation markets which align with our advanced capabilities for delivering products for complex, high cost of failure platforms. In 2019, the President of the U.S. proposed a FY 2020 budget requesting \$750 billion for national security. The President's budget request addresses various capabilities highlighted in the U.S. National Security Strategy, the National Defense Strategy and the Missile Defense Review. On August 2, 2019, the Bipartisan Budget Act of 2019 was enacted, increasing spending caps under the Budget Control Act (BCA) for FY 2020 and FY 2021, the final two fiscal years covered by the BCA, and suspending the debt ceiling through July 31, 2021. On December 20, 2019, FY 2020 appropriations for all federal agencies were enacted, representing a 3 percent increase from FY 2019. The budget is expected to support program growth and market expansion for 2020 for aerospace and defense participants. We expect to compete for follow-on business opportunities on future builds of several existing programs.

### **Critical Accounting Policies and Estimates**

The preparation of the consolidated financial statements and accompanying notes in conformity with U.S. generally accepted accounting principles requires that we make estimates and assumptions that affect the amounts reported. Changes in facts and circumstances could have a significant impact on the resulting estimated amounts included in our consolidated financial statements. We believe the following critical accounting policies affect our more complex judgments and estimates. We also have other policies that we consider to be key accounting policies, such as our policies for revenue recognition for Sypris Technologies, including cost of sales; however, these policies do not meet the definition of critical accounting policies because they do not generally require us to make estimates or judgments that are difficult or subjective. The following discussion of accounting estimates is intended to supplement the Summary of Significant Accounting Policies presented as Note 1 to our consolidated financial statements in Item 8.

*Allowance for Doubtful Accounts.* We establish reserves for uncollectible accounts receivable based on overall receivable aging levels, a specific evaluation of accounts for customers with known financial difficulties and evaluation of customer chargebacks, if any. These reserves and corresponding write-offs could significantly increase if our customers experience deteriorating financial results or in the event we receive a significant chargeback, which is deemed uncollectible.

*Net Revenue and Cost of Sales.* The Company recognizes revenue when it satisfies a performance obligation by transferring control of a promised product or rendering a service to a customer. The amount of revenue recognized reflects the consideration the Company expects to be entitled to in exchange for the product or service (the "transaction price"). The Company's transaction price in its contracts with customers is generally fixed; no payment discounts, rebates or refunds are included within its contracts. The Company does not provide service-type warranties, nor does it allow customer returns. In connection with the sale of various parts to customers, the Company is subject to typical assurance warranty obligations covering the compliance of the electronics parts produced to agreed-upon specifications (See Note 1 to the consolidated financial statements in this Form 10-K). Customer returns, when they occur, relate to quality rework issues and are not connected to any repurchase obligation of the Company.

A performance obligation is a promise in a contract to transfer a distinct product or render a service to a customer and is the unit of account to which the transaction price is allocated under ASC 606, *Revenue from Contracts*

*with Customers.* When a contract contains multiple performance obligations, we allocate the transaction price to the individual performance obligations using the price at which the promised goods or services would be sold to customers on a standalone basis. For most sales within our Sypris Technologies segment and a portion of sales within Sypris Electronics, control transfers to the customer at a point in time. Indicators that control has transferred to the customer include the Company having a present right to payment, the customer obtaining legal title and the customer having the significant risks and rewards of ownership. The Company's principal terms of sale are FOB Shipping Point, or equivalent, and, as such, the Company primarily transfers control and records revenue for product sales upon shipment.

For contracts where Sypris Electronics serves as a contractor for aerospace and defense companies under federally funded programs, we generally recognize revenue over time as we perform due to the continuous transfer of control to the customer. This continuous transfer of control to the customer is supported by clauses in the contracts that allow the customer to unilaterally terminate the contract for convenience, pay us for costs incurred plus a reasonable profit and take control of any work in process. Because control is transferred over time, revenue is recognized based on the extent of progress towards completion of the performance obligation. We use labor hours incurred as a measure of progress for these contracts because it best depicts the Company's performance of the obligation to the customer, which occurs as we incur labor on our contracts. Under this measure of progress, the extent of progress towards completion is measured based on the ratio of labor hours incurred to date to the total estimated labor hours at completion of the performance obligation.

Our contract profit margins may include estimates of revenues for goods or services on which the customer and the Company have not reached final agreements, such as contract changes, settlements of disputed claims, and the final amounts of requested equitable adjustments permitted under the contract. These estimates are based upon management's best assessment of the totality of the circumstances and are included in our contract profit based upon contractual provisions and our relationships with each customer.

*Long-lived asset impairment.* We perform periodic impairment analysis on our long-lived amortizable assets whenever events or circumstances indicate that the carrying amount of such assets may not be recoverable. When indicators are present, we compare the estimated future undiscounted net cash flows of the operations to which the assets relate to their carrying amount. If the operations are unable to recover the carrying amount of their assets, the long-lived assets are written down to their estimated fair value. Fair value is determined based on discounted cash flows, third party appraisals or other methods that provide appropriate estimates of value. A considerable amount of management judgment and assumptions are required in performing the impairment test, principally in determining whether an adverse event or circumstance has triggered the need for an impairment review. The Company did not have any long-lived assets measured at fair value on a nonrecurring basis as of December 31, 2019 or 2018.

*Pension Plan Funded Status.* Our U.S. defined benefit pension plans are closed to new entrants and only \$4,000 of service-related costs was recorded in 2019 related to a small number of participants who are still accruing benefits in the Louisville Hourly and Salaried Plans. Changes in our net obligations are principally attributable to changing discount rates and the performance of plan assets. Pension obligations are valued using discount rates established annually in consultation with our outside actuarial advisers using a theoretical bond portfolio, adjusted according to the timing of expected cash flows for our future obligations. Plan liabilities at December 31, 2019 are based upon a discount rate of 3.15% which reflects the Above Mean Mercer Yield Curve rate as of December 31, 2019 rounded to the nearest 5<sup>th</sup> basis point. Declining discount rates increase the present value of future pension obligations; a 25 basis point decrease in the discount rate would increase our U.S. pension liability by about \$0.8 million. As indicated above, when establishing the expected long-term rate of return on our U.S. pension plan assets, we consider historical performance and forward looking return estimates reflective of our portfolio mix and investment strategy. Based on the most recent analysis of projected portfolio returns, we concluded that the use of 3.90% for the Louisville Hourly Plan, 3.85% for the Marion Plan and 3.65% for the Louisville Salaried Plan as the expected return on our U.S. pension plan assets for 2019 was appropriate. A change in the assumed rate of return on plan assets of 100 basis points would result in a \$0.3 million change in the estimated 2020 pension expense.

At December 31, 2019, we have \$13.0 million of unrecognized losses relating to our U.S. pension plans. Actuarial gains and losses, which are primarily the result of changes in the discount rate and other assumptions and differences between actual and expected asset returns, are deferred in Accumulated Other Comprehensive Income and amortized to expense following the corridor approach. We use the average remaining service period of active participants unless almost all of the plan's participants are inactive, in which case we use the average remaining life expectancy for all active and inactive participants.

Based on the current funded status of our U.S. plans, we expect to contribute approximately \$0.9 million during 2020, which represents the minimum funding amounts required by federal law.

*Reserve for Excess, Obsolete and Scrap Inventory.* We record inventory at the lower of cost, determined under the first-in, first-out method, or net realizable value, and we reserve for excess, obsolete or scrap inventory. These reserves are primarily based upon management's assessment of the salability of the inventory, historical usage of raw materials, historical demand for finished goods and estimated future usage and demand. An improper assessment of salability or improper estimate of future usage or demand, or significant changes in usage or demand could result in significant changes in the reserves and a positive or a negative impact on our consolidated results of operations in the period the change occurs.

*Stock-based Compensation.* We account for stock-based compensation in accordance with the fair value recognition provisions using the Black-Scholes option-pricing method, which requires the input of several subjective assumptions. These assumptions include estimating the length of time employees will retain their vested stock options before exercising them (expected term) and the estimated volatility of our common stock price over the expected term. The dividend yield is assumed to be zero as we have not paid dividends nor do we anticipate paying any dividends in the foreseeable future. Changes in the subjective assumptions can materially affect the fair value estimate of stock-based compensation and consequently, the related expense recognized in the consolidated statements of operations.

*Income Taxes.* We account for income taxes as required by the provisions of ASC 740, *Income Taxes*, under which deferred tax assets and liabilities are recognized for the tax effects of temporary differences between the financial reporting and tax bases of assets and liabilities measured using enacted tax rates.

Management judgment is required in determining income tax expense and the related balance sheet amounts. In addition, under ASC 740-10, *Accounting for Uncertainty in Income Taxes*, judgments are required concerning the ultimate outcome of uncertain income tax positions. Actual income taxes paid may vary from estimates, depending upon changes in income tax laws, actual results of operations and the final audit of tax returns by taxing authorities. Tax assessments may arise several years after tax returns have been filed. We believe that our recorded income tax liabilities adequately provide for the probable outcome of these assessments.

Deferred tax assets are also recorded for operating losses and tax credit carryforwards. However, ASC 740 requires that a valuation allowance be recorded when it is more likely than not that some portion or all of the deferred tax assets will not be realized. This assessment is largely dependent upon projected near-term profitability including the effects of tax planning. Deferred tax assets and liabilities are determined separately for each tax jurisdiction in which we conduct our operations or otherwise incur taxable income or losses. We have recorded valuation allowances against deferred tax assets in the U.S. and a portion of deferred tax assets in Mexico where realization has been determined to be uncertain. If we determine that we would be able to realize our deferred tax assets in the future in excess of the net recorded amount, an adjustment to reduce the valuation allowance would increase net income in the period that such determination is made.

## Results of Operations

We operate in two segments, Sypris Technologies and Sypris Electronics. The table presented below compares our segment and consolidated results of operations from 2019 to 2018. The table presents the results for each year, the change in those results from one year to another in both dollars and percentage change and the results for each year as a percentage of net revenue.

- The first two columns in each table show the absolute results for each period presented.
- The columns entitled “Year-Over-Year Change” and “Year-Over-Year Percentage Change” show the change in results, both in dollars and percentages. These two columns show favorable changes as positive and unfavorable changes as negative. For example, when our net revenue increases from one period to the next, that change is shown as a positive number in both columns. Conversely, when expenses increase from one period to the next, that change is shown as a negative number in both columns.
- The last two columns in each table show the results for each period as a percentage of net revenue. In these two columns, the cost of sales and gross profit for each are given as a percentage of each segment’s net revenue. These amounts are shown in italics.

### Year Ended December 31, 2019 Compared to Year Ended December 31, 2018

	Year Ended December 31,		Year Over Year Change	Year Over Year Percentage Change	Results as Percentage of Net Revenue for the Year Ended December 31,	
	2019	2018	Favorable (Unfavorable)	Favorable (Unfavorable)	2019	2018
	(in thousands, except percentage data)					
Net revenue:						
Sypris Technologies.....	\$ 61,683	\$59,816	\$ 1,867	3.1%	70.2%	68.0%
Sypris Electronics .....	<u>26,208</u>	<u>28,153</u>	<u>(1,945)</u>	(6.9)	<u>29.8</u>	<u>32.0</u>
Total net revenue .....	87,891	87,969	(78)	(0.1)	100.0	100.0
Cost of sales:						
Sypris Technologies.....	51,898	52,293	395	0.8	<i>84.1</i>	<i>87.4</i>
Sypris Electronics .....	<u>26,110</u>	<u>28,104</u>	<u>1,994</u>	7.1	<u><i>99.6</i></u>	<u><i>99.8</i></u>
Total cost of sales .....	78,008	80,397	2,389	3.0	88.8	91.2
Gross profit:						
Sypris Technologies.....	9,785	7,523	2,262	30.1	<i>15.9</i>	<i>12.6</i>
Sypris Electronics .....	<u>98</u>	<u>49</u>	<u>49</u>	100.0	<u><i>0.4</i></u>	<u><i>0.2</i></u>
Total gross profit.....	9,883	7,572	2,311	30.5	11.2	8.6
Selling, general and administrative .....	13,680	10,474	(3,206)	(30.6)	15.5	11.9
Severance, relocation and other costs .....	<u>509</u>	<u>1,394</u>	<u>885</u>	63.5	<u>0.6</u>	<u>1.6</u>
Operating loss .....	(4,306)	(4,296)	(10)	(0.2)	(4.9)	(4.9)
Interest expense, net.....	903	850	(53)	(6.2)	1.0	1.0
Other income, net.....	<u>(1,256)</u>	<u>(1,436)</u>	<u>(180)</u>	(12.5)	<u>(1.4)</u>	<u>(1.7)</u>
Loss before income taxes.....	(3,953)	(3,710)	(243)	(6.5)	(4.5)	(4.2)
Income tax benefit, net.....	<u>(4)</u>	<u>(205)</u>	<u>(201)</u>	(98.0)	<u>(0.0)</u>	<u>(0.2)</u>
Net loss .....	<u>\$ (3,949)</u>	<u>\$ (3,505)</u>	<u>\$ (444)</u>	(12.7)	<u>(4.5)%</u>	<u>(4.0)%</u>

*Net Revenue.* Sypris Technologies derives its revenue from the sale of forged and finished steel components and subassemblies and high-pressure closures and other fabricated products. Net revenue for Sypris Technologies increased \$1.9 million from the prior year to \$61.7 million in 2019. The net revenue growth for the year was primarily attributable to increased energy related product sales of \$1.9 million partially offset by a \$0.9 million decline in volumes with customers in the commercial vehicle market. Additionally, price increases on one of our commercial vehicle programs implemented during the fourth quarter of 2018 resulted in an increase of \$0.9 million for the year. Revenue for Sypris Technologies is expected to decrease slightly in 2020, primarily attributable to the expected decline in the commercial vehicle market partially offset by new program launches.

Sypris Electronics derives its revenue primarily from circuit card and full “box build” manufacturing, high reliability manufacturing and systems assembly and integration. Net revenue for Sypris Electronics decreased \$1.9 million to \$26.2 million in 2019. Net revenue for Sypris Electronics in 2019 was partially affected by shortages of certain electronic components and extensive lead-time issues in the electronic manufacturing industry. The year ended December 31, 2019 was also impacted by shipments accelerated into the fourth quarter of 2018 as the Company planned for the implementation of a new ERP system effective in January 2019. The majority of the programs that generated revenue in 2018 continued into 2019; however volumes declined on certain programs based on customer demand and government funding. The majority of programs that generated revenue in 2019 will continue to generate revenue into 2020.

*Gross Profit.* Sypris Technologies’ gross profit improved \$2.3 million to \$9.8 million in 2019 as compared to \$7.5 million in the prior year. The net increase in volumes contributed to an increase in gross profit of \$0.4 million for the year ended December 31, 2019. Price increases on a commercial vehicle program implemented during the fourth quarter of 2018 resulted in an increase in gross profit of \$0.9 million. Additionally, gross profit for 2019 was positively impacted by improvements in supply, utilities and maintenance expense. These improvements were partially offset during the year by pre-production and ramp up costs on new programs being launched, which led to incremental costs and labor inefficiencies in 2019 that are not expected to repeat in 2020.

Sypris Electronics’ gross profit increased slightly to \$0.1 million in 2019. Although revenue was down from the prior year, margins on certain of the new programs improved during 2019 and served to offset the variance attributable to the lower shipment volume. Another factor in the comparative results was the low margin performance of an engineering manufacturing development program that was substantially complete in 2018. The costs associated with the labor inefficiencies and engineering support costs incurred on this program during 2018 did not recur in 2019, thereby improving gross profit.

*Selling, General and Administrative.* Selling, general and administrative expense increased \$3.2 million to \$13.7 million in 2019 as compared to \$10.5 million in 2018. The prior year amount included a \$1.9 million benefit from the resolution of an outstanding disputed legal fee for an amount less than originally charged. Additionally, the Company experienced an increase in professional fees associated with the restatement of the Company’s unaudited interim financial statements in its 2019 first quarter Form 10-Q, consultation costs associated with the Company’s new ERP implementation effective in January 2019 and higher employee medical insurance claim expenses during the year as compared to the prior period.

*Severance, Relocation and Other Costs.* Severance, relocation and other costs were \$0.5 million and \$1.4 million for the years ended December 31, 2019 and 2018, respectively. The charges for 2019 were primarily related to mothball costs associated with the closure of the Broadway Plant. The charges for 2018 included \$0.4 million in equipment relocation costs and \$1.0 million of other costs primarily related to mothball costs associated with the closure of the Broadway Plant (see Note 4 to the consolidated financial statements in this Form 10-K).

*Other Income, Net.* Other income, net, decreased \$0.2 million to \$1.3 million for 2019 from \$1.4 million in 2018. During 2019, the Company recognized a gain in other income of \$1.5 million related to a settlement agreement reached with one of its customers during the year (see Note 5 to the consolidated financial statements in this Form 10-K). Additionally, the Company recognized a net gain of \$0.7 million related to the sale of idle assets within Sypris Technologies, offset by pension expense of \$1.0 million.

During 2018, the Company recognized an insurance recovery gain of \$2.3 million related to proceeds received for damage sustained at the Broadway Plant (see Note 5 to the consolidated financial statements in this Form 10-K). The gain was partially offset by a loss of \$0.2 million related to the sale or disposal of idle assets and pension expense of \$0.6 million.

*Income Taxes.* The 2019 income tax provision consists of current tax expense of \$0.2 million and a deferred tax benefit of \$0.2 million. The current tax expense in 2019 and 2018 includes taxes paid by our Mexican subsidiaries and domestic state income taxes. The 2019 deferred tax benefit includes a \$0.2 million benefit recorded due to the required intraperiod tax allocation resulting from the loss from continuing operations and other comprehensive income.

The 2018 income tax provision consists of current tax expense of \$0.3 million and a deferred tax benefit of \$0.5 million. The 2018 deferred tax benefit includes a \$0.2 million benefit recorded due to the required intraperiod tax allocation resulting from the loss from continuing operations and other comprehensive income. The deferred tax benefit also includes a \$0.3 million benefit from the partial reversal of a valuation allowance by one of our Mexican subsidiaries.

The Company currently maintains a valuation allowance against its domestic deferred tax assets and a material portion of its foreign deferred tax assets as of December 31, 2019. The Company intends to continue to maintain a valuation allowance on these deferred tax assets until there is sufficient evidence to support the reversal of all or some portion of these allowances. However, given the recent earnings and anticipated future earnings for its Mexican operation, we believe that there is a reasonable possibility that, within the next 12 months, sufficient positive evidence may become available to allow management to reach a conclusion that up to approximately \$3.7 million of the valuation allowance against foreign deferred tax assets will no longer be needed. Release of the valuation allowance would result in the recognition of certain deferred tax assets and a decrease to income tax expense in the period the release is recorded. However, the exact timing and amount of any valuation allowance release are subject to change on the basis of the level of profitability that the Company is able to achieve.

## Quarterly Results

The following table presents our unaudited condensed consolidated statements of operations data for each of the eight quarters in the two-year period ended December 31, 2019. The quarterly results are presented on a 13-week period basis. We have prepared this data on the same basis as our audited consolidated financial statements and, in our opinion, have included all normal recurring adjustments necessary for a fair presentation of this information. You should read these unaudited quarterly results in conjunction with our consolidated financial statements and related notes included elsewhere in this Annual Report on Form 10-K. The consolidated results of operations for any quarter are not necessarily indicative of the results to be expected for any subsequent period. The sum of quarterly earnings per share may differ from the full-year amounts due to rounding.

	2019				2018			
	First	Second	Third	Fourth	First	Second	Third	Fourth
	(in thousands, except per share data)							
Net revenue:								
Sypris Technologies .....	\$ 16,141	\$ 16,878	\$ 15,654	\$ 13,010	\$ 14,507	\$ 15,327	\$ 14,852	\$ 15,130
Sypris Electronics .....	<u>3,423</u>	<u>7,566</u>	<u>6,605</u>	<u>8,614</u>	<u>5,435</u>	<u>7,644</u>	<u>6,249</u>	<u>8,825</u>
Total net revenue.....	19,564	24,444	22,259	21,624	19,942	22,971	21,101	23,955
Cost of sales:								
Sypris Technologies .....	13,837	13,915	13,140	11,006	12,400	13,397	13,523	12,973
Sypris Electronics .....	<u>4,867</u>	<u>6,540</u>	<u>6,793</u>	<u>7,910</u>	<u>5,511</u>	<u>6,640</u>	<u>6,376</u>	<u>9,577</u>
Total cost of sales.....	18,704	20,455	19,933	18,916	17,911	20,037	19,899	22,550
Gross profit (loss):								
Sypris Technologies .....	2,304	2,963	2,514	2,004	2,107	1,930	1,329	2,157
Sypris Electronics .....	<u>(1,444)</u>	<u>1,026</u>	<u>(188)</u>	<u>704</u>	<u>(76)</u>	<u>1,004</u>	<u>(127)</u>	<u>(752)</u>
Total gross profit.....	860	3,989	2,326	2,708	2,031	2,934	1,202	1,405
Selling, general and administrative .....	3,454	3,604	3,148	3,474	3,148	3,171	2,942	1,213
Severance, relocation and other costs .....	<u>98</u>	<u>103</u>	<u>190</u>	<u>118</u>	<u>509</u>	<u>305</u>	<u>274</u>	<u>306</u>
Operating (loss) income .....	(2,692)	282	(1,012)	(884)	(1,626)	(542)	(2,014)	(114)
Interest expense, net .....	217	232	227	227	213	221	231	185
Other expense (income), net.....	<u>51</u>	<u>(1,493)</u>	<u>286</u>	<u>(100)</u>	<u>(84)</u>	<u>(1,623)</u>	<u>56</u>	<u>215</u>
(Loss) income before tax.....	(2,960)	1,543	(1,525)	(1,011)	(1,755)	860	(2,301)	(514)
Income tax expense (benefit) ...	<u>76</u>	<u>40</u>	<u>32</u>	<u>(152)</u>	<u>40</u>	<u>46</u>	<u>35</u>	<u>(326)</u>
Net (loss) income .....	<u>\$ (3,036)</u>	<u>\$ 1,503</u>	<u>\$ (1,557)</u>	<u>\$ (859)</u>	<u>\$ (1,795)</u>	<u>\$ 814</u>	<u>\$ (2,336)</u>	<u>\$ (188)</u>
(Loss) income per common share:								
Basic .....	<u>\$ (0.15)</u>	<u>\$ 0.07</u>	<u>\$ (0.07)</u>	<u>\$ (0.04)</u>	<u>\$ (0.09)</u>	<u>\$ 0.04</u>	<u>\$ (0.11)</u>	<u>\$ (0.01)</u>
Diluted .....	<u>\$ (0.15)</u>	<u>\$ 0.07</u>	<u>\$ (0.07)</u>	<u>\$ (0.04)</u>	<u>\$ (0.09)</u>	<u>\$ 0.04</u>	<u>\$ (0.11)</u>	<u>\$ (0.01)</u>

## Liquidity and Capital Resources

*Gill Family Capital Management Note.* The Company has received the benefit of cash infusions from Gill Family Capital Management, Inc. (“GFCM”) in the form of secured promissory note obligations totaling \$6.5 million in principal as of December 31, 2019 and 2018 (the “Note”). GFCM is an entity controlled by the Company’s chairman, president and chief executive officer, Jeffrey T. Gill and one of our directors, R. Scott Gill. GFCM, Jeffrey T. Gill and R. Scott Gill are significant beneficial stockholders of the Company. As of December 31, 2019, our principal commitment under the Note was \$2.5 million due on April 1, 2021, \$2.0 million on April 1, 2023 and the balance on April 1, 2025. The Note allows for up to an 18-month deferral of payment for up to 60% of the interest due on the notes maturing in April of 2021 and 2023, and provide for a first security interest in substantially all of the Company’s assets, including those in Mexico (see Note 13 to the consolidated financial statements in this Form 10-K).

*Finance Lease Obligations.* On March 9, 2016, the Company completed the sale of its 24-acre Toluca property for 215 million Mexican Pesos, or approximately \$12.2 million in U.S. dollars. Simultaneously, the Company entered into a ten-year lease of the 9 acres and buildings currently occupied by the Company and needed for its ongoing business in Toluca. As a result of the Toluca Sale-Leaseback, the Company has a finance lease obligation of \$2.4 million for the building as of December 31, 2019.

In January 2018, the Company entered into a finance lease for \$1.3 million for new production equipment installed at its Sypris Electronics facility during 2017. The balance of the lease obligation as of December 31, 2019 was \$0.4 million.

In February 2019, the Company entered into a finance lease for \$0.3 million for new machinery at its Sypris Technologies facility in the U.S. The balance of the lease obligation as of December 31, 2019 was \$0.2 million.

*Purchase Commitments.* We also had purchase commitments totaling approximately \$8.8 million at December 31, 2019, primarily for inventory.

*Cash Balance.* At December 31, 2019, we had approximately \$5.1 million of cash and cash equivalents, of which \$2.4 million was held in jurisdictions outside of the U.S. that, if repatriated, could result in withholding taxes. We expect existing cash and cash flows of operations to continue to be sufficient to fund our operating activities and cash commitments for investing and financing activities, such as capital expenditures, for at least the next 12 months.

We have projected that our cash and cash equivalents will be sufficient to allow us to continue operations for the next 12 months. Significant changes from our current forecasts, including, but not limited to: (i) meaningful shortfalls in our projected revenues or in the sales proceeds from underutilized or non-core equipment, (ii) unexpected costs or expenses, and/or (iii) operating difficulties which cause unexpected delays in scheduled shipments, could require us to seek additional funding or force us to make further reductions in spending, extend payment terms with suppliers, liquidate assets where possible and/or suspend or curtail planned programs. Any of these actions could materially harm our business, results of operations and future prospects.

### **Cash Flows from Operating, Investing and Financing Activities**

*Operating Activities.* Net cash used by operating activities was \$5.8 million in 2019, as compared to net cash provided of \$1.9 million in 2018. The aggregate decrease in accounts receivable in 2019 resulted in a source of cash of \$2.4 million due to lower shipments in the fourth quarter of 2019. The investment in inventory in 2019 resulted in a usage of cash of \$2.8 million. The increase in inventory primarily relates to new programs for Sypris Electronics. Accounts payable decreased in 2019, resulting in a usage of cash of \$4.1 million. Additionally, accrued and other liabilities decreased during 2019 resulting in a usage of cash of \$1.0 million primarily as a result of a decrease in unearned revenue.

*Investing Activities.* Net cash provided by investing activities was \$1.0 million in 2019 as compared to \$1.6 million in 2018. Net cash provided by investing activities for the year ended December, 31, 2019 includes proceeds of \$1.9 million from the sale of idle assets by Sypris Technologies during the period partially offset by capital expenditures of \$0.9 million.

Net cash provided by investing activities for the year ended December, 31, 2018 includes \$2.3 million from insurance proceeds related to damage sustained at the Broadway Plant (See Note 5 to the consolidated financial statements in this Form 10-K). Additionally, the Company received proceeds of \$1.4 million from the sale of idle assets by Sypris Technologies during the period. Capital expenditures in both periods represented maintenance levels of investment.

*Financing Activities.* Net cash used in financing activities was \$0.8 million in 2019 as compared to \$0.9 million in 2018. Net cash used in financing activities in 2019 included finance lease payments of \$0.6 million and payments of \$0.2 million for minimum statutory tax withholdings on stock-based compensation. Net cash used in financing activities in 2018 included finance lease payments of \$0.8 million and payments of \$0.1 million for minimum statutory tax withholdings on stock-based compensation.

### **Off-Balance Sheet Arrangements**

On December 31, 2019, we had no material off-balance sheet arrangements.

### **Recent Accounting Pronouncements**

See Note 1 to our consolidated financial statements for a full description of recent accounting pronouncements, including the respective dates of adoption and effects on our results of operations and financial condition.

**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

We are a smaller reporting company as defined in Item 10(f)(1) of Regulation S-K and thus are not required to provide the quantitative and qualitative disclosures about market risk specified in Item 305 of Regulation S-K.

**Item 8. Financial Statements and Supplementary Data**

**SYPRIS SOLUTIONS, INC.**

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## Report of Independent Registered Public Accounting Firm

Stockholders and the Board of Directors of Sypris Solutions, Inc.  
Louisville, Kentucky

### **Opinion on the Financial Statements**

We have audited the accompanying consolidated balance sheets of Sypris Solutions, Inc. (the “Company”) as of December 31, 2019 and 2018, the related consolidated statements of operations, comprehensive loss, stockholders’ equity, and cash flows for the years then ended, and the related notes (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2019 and 2018, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

### **Basis for Opinion**

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (“PCAOB”) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting 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.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ CROWE LLP

We have served as the Company’s auditor since 2014.

Louisville, Kentucky  
March 19, 2020

**SYPRIS SOLUTIONS, INC.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(in thousands, except for per share data)

	<u>Year ended December 31.</u>	
	<u>2019</u>	<u>2018</u>
Net revenue.....	\$ 87,891	\$ 87,969
Cost of sales.....	<u>78,008</u>	<u>80,397</u>
Gross profit.....	9,883	7,572
Selling, general and administrative.....	13,680	10,474
Severance, relocation and other costs.....	<u>509</u>	<u>1,394</u>
Operating loss .....	(4,306)	(4,296)
Interest expense, net .....	903	850
Other income, net .....	<u>(1,256)</u>	<u>(1,436)</u>
Loss before income taxes .....	(3,953)	(3,710)
Income tax benefit, net .....	<u>(4)</u>	<u>(205)</u>
Net loss.....	<u>\$ (3,949)</u>	<u>\$ (3,505)</u>
Loss per common share:		
Basic .....	\$ (0.19)	\$ (0.17)
Diluted.....	\$ (0.19)	\$ (0.17)
Cash dividends per common share .....	\$ —	\$ —
Weighted average shares outstanding:		
Basic .....	20,865	20,512
Diluted.....	20,865	20,512

The accompanying notes are an integral part of the consolidated financial statements.

**SYPRIS SOLUTIONS, INC.**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS**  
(in thousands)

	<u>Year ended December 31,</u>	
	<u>2019</u>	<u>2018</u>
Net loss .....	\$ (3,949)	\$ (3,505)
Other comprehensive income (loss):		
Foreign currency translation adjustments, net of tax expense of \$104 and tax benefit of \$18 in 2019 and 2018, respectively .....	344	(52)
Employee benefit related, net of tax expense of \$136 and \$230 in 2019 and 2018, respectively .....	<u>447</u>	<u>761</u>
Other comprehensive income .....	<u>791</u>	<u>709</u>
Comprehensive loss .....	<u>\$ (3,158)</u>	<u>\$ (2,796)</u>

The accompanying notes are an integral part of the consolidated financial statements.

**SYPRIS SOLUTIONS, INC.**  
**CONSOLIDATED BALANCE SHEETS**  
(in thousands, except for share data)

	<b>December 31,</b>	
	<b>2019</b>	<b>2018</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents.....	\$ 5,095	\$ 10,704
Accounts receivable, net .....	7,444	9,881
Inventory, net .....	20,784	18,584
Other current assets.....	4,282	4,755
Assets held for sale .....	2,233	1,474
Total current assets .....	39,838	45,398
Property, plant and equipment, net .....	11,675	14,655
Operating lease right-of-use assets .....	7,014	—
Other assets.....	1,529	1,515
Total assets .....	\$ 60,056	\$ 61,568
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable .....	\$ 9,346	\$ 13,427
Accrued liabilities .....	12,495	14,965
Operating lease liabilities, current portion .....	841	—
Finance lease obligations, current portion.....	684	593
Total current liabilities .....	23,366	28,985
Note payable – related party .....	6,463	6,449
Operating lease obligations, net of current portion.....	6,906	—
Finance lease obligations, net of current portion .....	2,351	2,804
Other liabilities .....	7,539	8,496
Total liabilities.....	46,625	46,734
Stockholders' equity:		
Preferred stock, par value \$0.01 per share, 975,150 shares authorized; no shares issued.....	—	—
Series A preferred stock, par value \$0.01 per share, 24,850 shares authorized; no shares issued.....	—	—
Common stock, non-voting, par value \$0.01 per share, 10,000,000 shares authorized; no shares issued .....	—	—
Common stock, par value \$0.01 per share, 30,000,000 shares authorized; 21,324,618 shares issued and 21,298,426 outstanding in 2019 and 21,414,374 shares issued and 21,398,182 outstanding in 2018.....	213	214
Additional paid-in capital.....	154,702	154,388
Accumulated deficit .....	(117,433)	(114,926)
Accumulated other comprehensive loss.....	(24,051)	(24,842)
Treasury stock, 26,192 and 16,192 shares in 2019 and 2018, respectively.....	—	—
Total stockholders' equity .....	13,431	14,834
Total liabilities and stockholders' equity.....	\$ 60,056	\$ 61,568

The accompanying notes are an integral part of the consolidated financial statements.

**SYPRIS SOLUTIONS, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in thousands)

	<u>Year ended December 31,</u>	
	<u>2019</u>	<u>2018</u>
Cash flows from operating activities:		
Net loss .....	\$ (3,949)	\$ (3,505)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Depreciation and amortization.....	2,671	2,648
Deferred income taxes .....	(260)	(509)
Non-cash compensation.....	469	637
Deferred loan costs amortized .....	11	14
Insurance recovery gain.....	—	(2,275)
Settlement gain .....	—	(1,890)
Net (gain) loss on sale of assets.....	(654)	249
Provision for excess and obsolete inventory .....	616	520
Non-cash lease expense .....	650	—
Other noncash items .....	(69)	278
Contributions to pension plans .....	(382)	(77)
Changes in operating assets and liabilities:		
Accounts receivable.....	2,425	(612)
Inventory.....	(2,823)	(2,857)
Prepaid expenses and other assets .....	560	(1,163)
Accounts payable.....	(4,066)	2,948
Accrued and other liabilities .....	<u>(1,019)</u>	<u>7,486</u>
Net cash (used in) provided by operating activities .....	(5,820)	1,892
Cash flows from investing activities:		
Capital expenditures.....	(859)	(2,051)
Proceeds from sale of assets.....	1,858	1,380
Insurance proceeds for recovery of property damage, net .....	<u>—</u>	<u>2,275</u>
Net cash provided by investing activities.....	999	1,604
Cash flows from financing activities:		
Finance lease payments.....	(632)	(829)
Indirect repurchase of shares for minimum statutory tax withholdings .....	<u>(156)</u>	<u>(107)</u>
Net cash used in financing activities.....	<u>(788)</u>	<u>(936)</u>
Net (decrease) increase in cash and cash equivalents.....	(5,609)	2,560
Cash and cash equivalents at beginning of year .....	<u>10,704</u>	<u>8,144</u>
Cash and cash equivalents at end of year .....	<u>\$ 5,095</u>	<u>\$ 10,704</u>
Supplemental disclosure of cash flow information:		
Non-cash investing and financing activities:		
Right-of-use assets obtained in exchange for finance lease obligations .....	\$ 269	\$ —

The accompanying notes are an integral part of the consolidated financial statements.

**SYPRIS SOLUTIONS, INC.**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
(in thousands, except for share data)

	<u>Common Stock</u>		<u>Additional Paid-In Capital</u>	<u>Accumulated Deficit</u>	<u>Accumulated Other Comprehensive Loss</u>	<u>Treasury Stock</u>
	<u>Shares</u>	<u>Amount</u>				
January 1, 2018 balance.....	21,422,077	\$ 214	\$ 153,858	\$(111,591)	\$ (25,551)	\$ —
Net loss .....	—	—	—	(3,505)	—	—
Adoption of new accounting standard.....	—	—	—	170	—	—
Employee benefit related, net of tax .....	—	—	—	—	761	—
Foreign currency translation adjustment, net of tax .....	—	—	—	—	(52)	—
Noncash compensation .....	42,000	—	637	—	—	—
Retire treasury stock .....	(65,895)	—	(107)	—	—	—
December 31, 2018 balance.....	21,398,182	\$ 214	\$ 154,388	\$(114,926)	\$ (24,842)	\$ —
Net loss .....	—	—	—	(3,949)	—	—
Adoption of new accounting standard.....	—	—	—	1,442	—	—
Employee benefit related, net of tax .....	—	—	—	—	447	—
Foreign currency translation adjustment, net of tax .....	—	—	—	—	344	—
Noncash compensation .....	60,000	—	469	—	—	—
Treasury stock.....	(10,000)	—	—	—	—	—
Retire treasury stock .....	(149,756)	(1)	(155)	—	—	—
December 31, 2019 balance.....	<u>21,298,426</u>	<u>\$ 213</u>	<u>\$ 154,702</u>	<u>\$(117,433)</u>	<u>\$ (24,051)</u>	<u>\$ —</u>

The accompanying notes are an integral part of the consolidated financial statements.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**December 31, 2019 and 2018**

**(1) Organization and Significant Accounting Policies**

*Consolidation Policy*

The accompanying consolidated financial statements include the accounts of Sypris Solutions, Inc. and its wholly-owned subsidiaries (collectively, “Sypris” or the “Company”) and have been prepared by the Company in accordance with the rules and regulations of the Securities and Exchange Commission. The Company’s operations are domiciled in the United States (U.S.) and Mexico and serve a wide variety of domestic and international customers. All intercompany accounts and transactions have been eliminated.

*Nature of Business*

Sypris is a diversified provider of truck components, oil and gas pipeline components and aerospace and defense electronics. The Company produces a wide range of manufactured products, often under multi-year, sole-source contracts with corporations and government agencies. The Company offers such products through its two business segments, Sypris Technologies, Inc. (“Sypris Technologies”) and Sypris Electronics, LLC (“Sypris Electronics”). Sypris Technologies derives its revenue primarily from the sale of forged, machined, welded and heat-treated steel components primarily for the heavy commercial vehicle and high-pressure energy pipeline applications. Sypris Electronics derives its revenue primarily from circuit card and box build manufacturing, high reliability manufacturing and systems assembly and integration. Most products are built to the customer’s design specifications. The Company also provides engineering design services and repair or inspection services. See Note 21 for additional information regarding our segments.

*Use of Estimates*

The preparation of the consolidated financial statements and accompanying notes in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported. Changes in facts and circumstances could have a significant impact on the resulting estimated amounts included in our consolidated financial statements. Actual results could differ from these estimates.

*Fair Value Estimates*

The Company estimates fair value of its financial instruments utilizing an established three-level hierarchy. The hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date as follows: Level 1 – Valuation is based upon unadjusted quoted prices for identical assets or liabilities in active markets. Level 2 – Valuation is based upon quoted prices for similar assets and liabilities in active markets, or other inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instruments. Level 3 – Valuation is based upon other unobservable inputs that are significant to the fair value measurements.

*Cash Equivalents*

Cash equivalents include all highly liquid investments with a maturity of three months or less when purchased.

*Inventory*

Inventory is stated at the lower of cost or estimated net realizable value. Costs for raw materials, work in process and finished goods is determined under the first-in, first-out method. Indirect inventories, which include perishable tooling, repair parts and other materials consumed in the manufacturing process but not incorporated into finished products are classified as raw materials.

The Company’s reserve for excess and obsolete inventory is primarily based upon forecasted demand for its product sales, and any change to the reserve arising from forecast revisions is reflected in cost of sales in the period the revision is made.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

*Property, Plant and Equipment*

Property, plant and equipment is stated at cost. Depreciation of property, plant and equipment is generally computed using the straight-line method over their estimated economic lives. For land improvements, buildings and building improvements, the estimated economic life is generally 40 years. Estimated economic lives range from three to fifteen years for machinery, equipment, furniture and fixtures. Leasehold improvements are amortized over the shorter of their economic life or the respective lease term using the straight-line method. Expenditures for maintenance, repairs and renewals of minor items are expensed as incurred. Major rebuilds and improvements are capitalized. Also included in plant and equipment are assets under finance lease, which are stated at the present value of minimum lease payments.

*Long-lived Assets*

The Company reviews the carrying value of amortizable long-lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held for sale and held for use is measured by a comparison of the carrying amount of the asset to the undiscounted future net cash flows expected to be generated by the asset. If facts and circumstances indicate that the carrying value of an asset or groups of assets, as applicable, is impaired, the long-lived asset or groups of long-lived assets are written down to their estimated fair value.

*Held for sale*

The Company classifies long-lived assets or disposal groups as held for sale in the period: management commits to a plan to sell; the long-lived asset or disposal group is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such long-lived assets or disposal groups; an active program to locate a buyer and other actions required to complete the plan to sell have been initiated; the sale is probable within one year; the asset or disposal group is being actively marketed for sale at a price that is reasonable in relation to its current fair value; and it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn. Long-lived assets and disposal groups classified as held for sale are measured at the lower of their carrying amount or fair value less costs to sell.

*Leases*

Our lease portfolio represents leases of real estate, including manufacturing, assembly and office facilities, while the remainder represents leases of personal property, including manufacturing and information technology equipment. We have lease agreements with lease and non-lease components, which are accounted for as a single lease component. Leases with an initial term of 12 months or less are not recorded on the balance sheet, and we recognize lease expense for these leases on a straight-line basis over the lease term. Generally, we use our incremental borrowing rate in determining the present value of lease payments, unless the implicit rate is readily available.

*Stock-based Compensation*

The Company accounts for stock-based compensation in accordance with the fair value recognition provisions using the Black-Scholes option-pricing method, which requires the input of several subjective assumptions. These assumptions include estimating the length of time employees will retain their vested stock options before exercising them (expected term) and the estimated volatility of our common stock price over the expected term. Changes in the subjective assumptions can materially affect the fair value estimate of stock-based compensation and consequently, the related expense is recognized in the consolidated statements of operations.

*Income Taxes*

The Company uses the liability method in accounting for income taxes. Deferred tax assets and liabilities are recorded for temporary differences between the tax basis of assets and liabilities and their reported amounts in the consolidated financial statements, using the statutory tax rates in effect for the year in which the differences are expected to reverse. A valuation allowance is recorded to reduce the carrying amounts of deferred tax assets unless it is more likely than not that such assets will be realized.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

In the ordinary course of business there is inherent uncertainty in quantifying the Company's income tax positions. The Company assesses its income tax positions and records tax benefits for all years subject to examination based upon management's evaluation of the facts, circumstances, and information available at the reporting dates. For those tax positions where it is more-likely-than-not that a tax benefit will be sustained, the Company has recorded the largest amount of tax benefit with a greater than 50% likelihood of being realized upon ultimate settlement with a taxing authority that has full knowledge of all relevant information. For those income tax positions where it is not more-likely-than-not that a tax benefit will be sustained, no tax benefit has been recognized in the financial statements. Where applicable, associated interest has also been recognized.

The Company recognizes liabilities or assets for the deferred tax consequences of temporary differences between the tax bases of assets or liabilities and their reported amounts in the financial statements in accordance with ASC 740, *Income Taxes*. The Company recognizes interest accrued related to unrecognized tax benefits in income tax expense. Penalties, if incurred, would be recognized as a component of income tax expense.

*Net Revenue and Cost of Sales*

The Company recognizes revenue when it satisfies a performance obligation by transferring control of a promised product or rendering a service to a customer. The amount of revenue recognized reflects the consideration the Company expects to be entitled to in exchange for the product or service (the "transaction price"). The Company's transaction price in its contracts with customers is generally fixed; no payment discounts, rebates or refunds are included within its contracts. The Company does not provide service-type warranties nor does it allow customer returns. In connection with the sale of various parts to customers, the Company is subject to typical assurance warranty obligations covering the compliance of the electronics parts produced to agreed-upon specifications. Customer returns, when they occur, relate to quality rework issues and are not connected to any repurchase obligation of the Company.

A performance obligation is a promise in a contract to transfer a distinct product or render a service to a customer and is the unit of account to which the transaction price is allocated under ASC 606, *Revenue from Contracts with Customers* ("ASC 606"). When a contract contains multiple performance obligations, we allocate the transaction price to the individual performance obligations using the price at which the promised goods or services would be sold to customers on a standalone basis. For most sales within our Sypris Technologies segment and a portion of sales within Sypris Electronics, control transfers to the customer at a point in time. Indicators that control has transferred to the customer include the Company having a present right to payment, the customer obtaining legal title and the customer having the significant risks and rewards of ownership. The Company's principal terms of sale are FOB Shipping Point, or equivalent, and, as such, the Company primarily transfers control and records revenue for product sales upon shipment.

For contracts where Sypris Electronics serves as a contractor for aerospace and defense companies under federally funded programs, we generally recognize revenue over time as we perform due to the continuous transfer of control to the customer. This continuous transfer of control to the customer is supported by clauses in the contracts that allow the customer to unilaterally terminate the contract for convenience, pay us for costs incurred plus a reasonable profit and take control of any work in process. Because control is transferred over time, revenue is recognized based on the extent of progress towards completion of the performance obligation. We use labor hours incurred as a measure of progress for these contracts because it best depicts the Company's performance of the obligation to the customer, which occurs as we incur labor on our contracts. Under this measure of progress, the extent of progress towards completion is measured based on the ratio of labor hours incurred to date to the total estimated labor hours at completion of the performance obligation.

Our contract profit margins may include estimates of revenues for goods or services on which the customer and the Company have not reached final agreements, such as contract changes, settlements of disputed claims, and the final amounts of requested equitable adjustments permitted under the contract. These estimates are based upon management's best assessment of the totality of the circumstances and are included in our contract profit based upon contractual provisions and our relationships with each customer.

*Allowance for Doubtful Accounts*

An allowance for uncollectible trade receivables is recorded when accounts are deemed uncollectible based on consideration of write-off history, aging analysis, and any specific, known troubled accounts.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

*Product Warranty Costs*

The provision for estimated warranty costs is recorded at the time of sale and is periodically adjusted to reflect actual experience. The Company's warranty liability, which is included in accrued liabilities in the accompanying balance sheets, as of December 31, 2019 and 2018, was \$569,000 and \$582,000, respectively. The Company's warranty expense for the years ended December 31, 2019 and 2018 was \$156,000 and \$136,000, respectively.

*Concentrations of Credit Risk*

Financial instruments which potentially expose the Company to concentrations of credit risk consist of accounts receivable. The Company's customer base consists of a number of customers in diverse industries across geographic areas, primarily in North America and Mexico, and aerospace and defense companies under contract with the U.S. Government. The Company performs periodic credit evaluations of its customers' financial condition and does not require collateral on its commercial accounts receivable. Credit losses are provided for in the consolidated financial statements and consistently have been within management's expectations. Approximately 27% of accounts receivable outstanding at December 31, 2019 is due from two customers. More specifically, SubCom and Detroit Diesel comprise 17% and 10%, respectively, of December 31, 2019 outstanding accounts receivables. Approximately 40% of accounts receivable outstanding at December 31, 2018 is due from two customers. More specifically, Northrop Grumman Corporation (Northrop Grumman) and Sistemas Automotrices de Mexico, S.A. de C. V. (Sistemas) comprise 22% and 18%, respectively, of December 31, 2018 outstanding accounts receivables.

The Company's largest customers for the year ended December 31, 2019 were Sistemas, Detroit Diesel and Northrop Grummon, which represented approximately 22%, 14% and 11%, respectively, of the Company's total net revenue. Detroit Diesel and Sistemas are both customers within the Sypris Technologies segment and Northrop Grummon is a customer within the Sypris Electronics segment. Sistemas, Northrop Grummon and Detroit Diesel were the Company's largest customers for the year ended December 31, 2018, which represented approximately 19%, 14% and 14%, respectively, of the Company's total net revenue. No other single customer accounted for more than 10% of the Company's total net revenue for the years ended December 31, 2019 or 2018.

*Foreign Currency Translation*

The functional currency for the Company's Mexican subsidiaries is the Mexican peso. Assets and liabilities are translated at the period end exchange rate, and income and expense items are translated at the weighted average exchange rate. The resulting translation adjustments are recorded in comprehensive loss as a separate component of stockholders' equity. Remeasurement gains or losses for U.S. dollar denominated accounts of the Company's Mexican subsidiaries are included in other income, net.

*Collective Bargaining Agreements*

Approximately 359, or 57% of the Company's employees, all within Sypris Technologies, were covered by collective bargaining agreements at December 31, 2019. Excluding certain Mexico employees covered under an annually ratified agreement, there are no collective bargaining agreements expiring within the next 12 months. Certain Mexico employees are covered by an annually ratified collective bargaining agreement. These employees represented approximately 51% of the Company's workforce, or 319 employees as of December 31, 2019.

*Recently Issued Accounting Standards*

In February 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-02, *Leases* (ASC 842). The new standard was issued to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. This standard affects any entity that enters into a lease, with some specified scope exemptions.

The Company adopted this update beginning on January 1, 2019 using the alternative modified retrospective transition method and will not recast comparative periods in transition to the new standard. In addition, we elected certain practical expedients which permit us to not reassess whether existing contracts are or contain leases, to not reassess the lease classification of any existing leases, to not reassess initial direct costs for any existing leases, and to

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

not separate lease and nonlease components for all classes of underlying assets. We also made an accounting policy election to keep leases with an initial term of 12 months or less off of the balance sheet for all classes of underlying assets. The adoption of ASC 842 on January 1, 2019 resulted in the recognition of right-of-use assets (ROU) of approximately \$7,664,000 and lease liabilities of operating leases of approximately \$8,549,000. The implementation decreased the accumulated deficit by \$1,442,000, which was primarily due to the recognition of the remaining deferred gain related to the operating lease portion on a 2016 sale-leaseback directly into the accumulated deficit. There was no material impact to our consolidated statements of operations or cash flows as a result of the adoption of ASC 842. See Note 2 for further information regarding the impact of the adoption of ASC 842 on the Company's financial statements.

In February 2018, the FASB issued ASU No. 2018-02, *Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income* (ASU 2018-02). Under existing U.S. GAAP, the effects of changes in tax rates and laws on deferred tax balances are recorded as a component of income tax expense in the period in which the law was enacted. When deferred tax balances related to items originally recorded in accumulated other comprehensive income are adjusted, certain tax effects become stranded in accumulated other comprehensive income. The amendments in ASU 2018-02 allow a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act of 2017 (the "Tax Act"). The guidance was effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Entities are required to make additional disclosures, regardless of whether they elect to reclassify stranded amounts of tax effects. The Company adopted the standard effective January 1, 2019, and has elected to not reclassify the income tax effects of the Tax Act from accumulated other comprehensive loss to accumulated deficit. The adoption of ASU 2018-02 did not have an impact on the Company's consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, *Credit Losses – Measurement of Credit Losses on Financial Instruments*, new guidance for the accounting for credit losses on certain financial instruments. This guidance introduces a new approach to estimating credit losses on certain types of financial instruments and modifies the impairment model for available-for-sale debt securities. This guidance, which becomes effective January 1, 2023, is not expected to have a material impact on our consolidated financial statements.

In August 2018, the FASB issued ASU 2018-14, *Compensation – Retirement Benefits – Defined Benefit Plans – General, Disclosure Framework – Changes to the Disclosure Requirements for Defined Benefit Plans*. The guidance eliminated certain disclosures about defined benefit plans, added new disclosures, and clarified other requirements. This guidance becomes effective January 1, 2020 and early adoption is permitted. There were no changes to interim disclosure requirements. Adoption of this guidance is not expected to have a material effect on our annual financial statement disclosures.

In August 2018, the FASB issued ASU 2018-15, *Intangibles-Goodwill and Other-Internal-Use Software: Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract* (ASU 2018-15). ASU 2018-15 aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. This new guidance will be effective for public companies for fiscal years beginning after December 15, 2019 and interim periods within those fiscal years. Early adoption is permitted. The Company is currently evaluating the effect that the new guidance will have on its consolidated financial statements and related disclosures. This guidance is not expected to have a material impact on our consolidated financial statements.

In December 2019, the FASB issued ASU 2019-12, *Income Taxes – Simplifying the Accounting for Income Taxes*. This guidance is intended to simplify various aspects of income tax accounting including the elimination of certain exceptions related to the approach for intraperiod tax allocation, the methodology for calculating income taxes in an interim period and the recognition of deferred tax liabilities for outside basis differences. The new guidance also simplifies aspects of the accounting for franchise taxes and enacted changes in tax laws or rates and clarifies the accounting for transactions that result in a step-up in the tax basis of goodwill. This guidance becomes effective January 1, 2021 and early adoption is permitted. Adoption of this guidance requires certain changes to primarily be made prospectively, with some changes to be made retrospectively. We are currently assessing the impact of this guidance on our consolidated financial statements.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

**(2) Leases**

The Company determines if an arrangement is a lease at its inception. The Company has entered into operating leases for real estate and personal property, including manufacturing and information technology equipment. These real estate leases have initial terms which range from 10 to 11 years, and often include one or more options to renew. These renewal terms can extend the lease term by 5 years, and will be included in the lease term when it is reasonably certain that the Company will exercise the option. The Company's existing leases do not contain significant restrictive provisions; however, certain leases contain provisions for payment of real estate taxes, insurance and maintenance costs by the Company. The lease agreements do not contain any residual value guarantees. Some of the real estate lease agreements include periods of rent holidays and payments that escalate over the lease term by specified amounts. All operating lease expenses are recognized on a straight-line basis over the lease term. For finance leases, interest expense is recognized on the lease liability and the ROU asset is amortized over the lease term.

Some leases may require variable lease payments based on factors specific to the individual agreements. Variable lease payments for which we are typically responsible for include real estate taxes, insurance and common area maintenance expenses based on the Company's pro-rata share, which are excluded from the measurement of the lease liability. Additionally, one of the Company's real estate leases has lease payments that adjust based on annual changes in the Consumer Price Index ("CPI"). The leases that are dependent upon CPI are initially measured using the index or rate at the commencement date and are included in the measurement of the lease liability. Incremental payments due to changes in the index are treated as variable lease costs and expensed as incurred.

These operating leases are included in "Operating lease right-of-use assets" on the Company's consolidated balance sheets as of December 31, 2019, and represent the Company's right to use the underlying asset for the lease term. The Company's obligations to make lease payments are included in "Operating lease liabilities, current portion" and "Operating lease liabilities, net of current portion" on the Company's consolidated balance sheets as of December 31, 2019. Based on the present value of the lease payments for the remaining lease term of the Company's existing leases, the Company recognized right-of-use assets of approximately \$7,664,000 and lease liabilities for operating leases of approximately \$8,549,000 on January 1, 2019, and included adjustments for any unamortized lease incentives and prepaid and accrued rent. Operating lease right-of-use assets and liabilities commencing after January 1, 2019 are recognized at the commencement date based on the present value of lease payments over the lease term. As of December 31, 2019, total right-of-use assets and operating lease liabilities were approximately \$7,014,000 and \$7,747,000, respectively.

We primarily use our incremental borrowing rate, which is updated quarterly, based on the information available at commencement date, in determining the present value of lease payments. If readily available, we would use the implicit rate in a new lease to determine the present value of lease payments. The Company has certain contracts for real estate which may contain lease and non-lease components which it has elected to treat as a single lease component.

The Company has entered into various short-term operating leases, primarily for office equipment with an initial term of twelve months or less. Lease payments associated with short-term leases are expensed as incurred and are not recorded on the Company's balance sheet. The related lease expense for short-term leases was not material for the year ended December 31, 2019.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

The following table presents information related to lease expense for the year ended December 31, 2019 (in thousands):

Finance lease expense:	
Amortization expense .....	\$ 481
Interest expense .....	348
Operating lease expense .....	1,406
Variable lease expense .....	<u>272</u>
Total lease expense .....	<u>\$ 2,507</u>

The following table presents supplemental cash flow information related to leases for the year ended December 31, 2019 (in thousands):

Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash flows from operating leases .....	\$ 1,436
Operating cash flows from finance leases.....	348
Financing cash flows from finance leases.....	632

The annual future minimum lease payments as of December 31, 2019 are as follows (in thousands):

	<u>Operating Leases</u>	<u>Finance Leases</u>
Next 12 months .....	\$ 1,424	\$ 945
12 to 24 months .....	1,476	644
24 to 36 months .....	1,492	612
36 to 48 months .....	1,509	612
48 to 60 months .....	1,318	559
Thereafter .....	<u>2,931</u>	<u>595</u>
Total lease payments .....	10,150	3,967
Less imputed interest.....	<u>(2,403)</u>	<u>(932)</u>
Total.....	<u>\$ 7,747</u>	<u>\$ 3,035</u>

For the year ended December 31, 2018, and under legacy lease accounting (ASC 840), future minimum lease payments under non-cancellable leases as of December 31, 2018 were expected to be as follows:

	<u>Operating Leases</u>	<u>Finance Leases</u>
2019.....	\$ 1,453	\$ 927
2020.....	1,387	881
2021.....	1,430	580
2022.....	1,443	548
2023.....	1,459	548
Thereafter .....	<u>4,101</u>	<u>1,143</u>
Total lease payments .....	<u>\$ 11,273</u>	4,627
Less imputed interest.....		<u>(1,230)</u>
Total.....		<u>\$ 3,397</u>

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

The following table presents certain information related to lease terms and discount rates for leases as of December 31, 2019:

	<u>Operating Leases</u>	<u>Finance Leases</u>
Weighted-average remaining lease term (years) .....	7.1	5.3
Weighted-average discount rate (percentage) .....	8.0	10.3

**(3) Revenue from Contracts with Customers**

The Company recognizes revenue when it satisfies a performance obligation by transferring control of a promised product or rendering a service to a customer. The amount of revenue recognized reflects the consideration the Company expects to be entitled to in exchange for the product or service (the “transaction price”). The Company’s transaction price in its contracts with customers is generally fixed; no payment discounts, rebates or refunds are included within its contracts. The Company also does not provide service-type warranties nor does it allow customer returns. In connection with the sale of various parts to customers, the Company is subject to typical assurance warranty obligations covering the compliance of the electronics parts produced to agreed-upon specifications (See Note 1). Customer returns, when they occur, relate to quality rework issues and are not connected to any repurchase obligation of the Company.

A performance obligation is a promise in a contract to transfer a distinct product or render a service to a customer and is the unit of account to which the transaction price is allocated under ASC 606. When a contract contains multiple performance obligations, we allocate the transaction price to the individual performance obligations using the price at which the promised goods or services would be sold to customers on a standalone basis. For most sales within our Sypris Technologies segment and a portion of sales within Sypris Electronics, control transfers to the customer at a point in time. Indicators that control has transferred to the customer include the Company having a present right to payment, the customer obtaining legal title and the customer having the significant risks and rewards of ownership. The Company’s principal terms of sale are FOB Shipping Point, or equivalent, and, as such, the Company primarily transfers control and records revenue for product sales upon shipment.

For contracts where Sypris Electronics serves as a contractor for aerospace and defense companies under federally funded programs, we generally recognize revenue over time as we perform because of continuous transfer of control to the customer. This continuous transfer of control to the customer is supported by clauses in the contracts that allow the customer to unilaterally terminate the contract for convenience, pay us for costs incurred plus a reasonable profit and take control of any work in process. Because control is transferred over time, revenue is recognized based on the extent of progress towards completion of the performance obligation. We use labor hours incurred as a measure of progress for these contracts because it best depicts the Company’s performance of the obligation to the customer, which occurs as we incur labor on our contracts. Under this measure of progress, the extent of progress towards completion is measured based on the ratio of labor hours incurred to date to the total estimated labor hours at completion of the performance obligation.

Our contract profit margins may include estimates of revenues for goods or services on which the customer and the Company have not reached final agreements, such as contract changes, settlements of disputed claims, and the final amounts of requested equitable adjustments permitted under the contract. These estimates are based upon management’s best assessment of the totality of the circumstances and are included in our contract profit based upon contractual provisions and our relationships with each customer.

The majority of Sypris Electronics’ contractual arrangements with customers are for one year or less. For the remaining population of non-cancellable contracts greater than one year we had \$8,769,000 of remaining performance obligations as of December 31, 2019, all of which were long-term Sypris Electronics’ contracts. We expect to recognize approximately 41% of our remaining performance obligations as revenue in 2020 and the balance in 2021.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

*Disaggregation of Revenue*

The following table summarizes revenue from contracts with customers for the years ended December 31, 2019 and 2018:

	December 31,	
	2019	2018
Sypris Technologies – transferred point in time.....	\$ 61,683	\$ 59,816
Sypris Electronics – transferred point in time .....	6,201	5,800
Sypris Electronics – transferred over time .....	20,007	22,353
Net revenue.....	\$ 87,891	\$ 87,969

Differences in the timing of revenue recognition, billings and cash collections results in billed accounts receivable, unbilled receivables (contract assets) and deferred revenue, customer deposits and billings in excess of revenue recognized (contract liabilities) on the consolidated balance sheets.

*Contract assets* – Contract assets include unbilled amounts typically resulting from sales under contracts where revenue is recognized over time and revenue recognized exceeds the amount billed to the customer, and the right to payment is subject to conditions other than the passage of time. Contract assets are generally classified as current assets in the consolidated balance sheet. The balance of contract assets as of December 31, 2019 and 2018 were \$906,000 and \$839,000, respectively, and are included within other current assets in the accompanying consolidated balance sheets.

*Contract liabilities* – Some of the Company’s contracts within Sypris Electronics are billed as work progresses in accordance with the contract terms and conditions, either at periodic intervals or upon achievement of certain milestones. Often this results in billing occurring prior to revenue recognition resulting in contract liabilities. Additionally, the Company occasionally receives cash payments from customers in advance of the Company’s performance resulting in contract liabilities. These contract liabilities are classified as either current or long-term in the consolidated balance sheet based on the timing of when the Company expects to recognize revenue. As of December 31, 2019, the contract liabilities balance was \$7,504,000, of which \$5,769,000 was included within accrued liabilities and \$1,735,000 was included within other liabilities in the accompanying consolidated balance sheets. As of December 31, 2018, the contract liabilities balance was \$8,369,000, which was included within accrued liabilities in the accompanying consolidated balance sheets. Payments received from customers in advance of revenue recognition are not considered to be significant financing components because they are used to meet working capital demands that can be higher in the early stages of a contract.

The Company recognized revenue from contract liabilities of \$5,109,000 and \$1,121,000 during the years ended December 31, 2019 and 2018, respectively.

*Practical expedients and exemptions*

Sales commissions are expensed when incurred because the amortization period would have been one year or less. These costs are recorded in selling, general and administrative expense in the consolidated statements of operations.

We do not disclose the value of unsatisfied performance obligations for contracts with original expected lengths of one year or less.

**(4) Exit and Disposal Activities**

During 2016, the continued strength of the U.S. dollar, the tightening of margins in certain sectors of the commercial vehicle markets and the generally softening of certain key market segments led the Company to reevaluate the strategic importance of each of its customers to the Company’s long-term success. The Company has reduced its reliance on certain of its traditional Tier 1 customers that represent the primary suppliers to the original equipment manufacturers (“OEMs”) in the commercial vehicle markets, while targeting to replace these customers with more diversified, longer-term relationships, especially among the OEMs, Tier 1 suppliers and others who place a higher value on the Company’s innovation, flexibility and core commitment to lean manufacturing principles. Among the customer programs not being renewed were (i) a supply agreement with Meritor that expired on January 1, 2017 and (ii) the Company’s business with Eaton, both of which utilized production at the Company’s Broadway Plant.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

On February 21, 2017, the Board of Directors approved a modified exit or disposal plan with respect to the Broadway Plant, which included the relocation of production to other Company facilities, as needed, and/or the closure of the plant. The relocation of production was complete as of the end of 2017. The Company has relocated certain assets from the Broadway Plant to other manufacturing facilities, as needed, to serve its existing and target customer base and identified underutilized or non-core assets, including the Broadway Plant real estate, for disposal.

As a result of these initiatives, the Company recorded charges of \$509,000, or \$0.02 per share, and \$1,394,000, or \$0.07 per share, during 2019 and 2018, respectively, related to the transition of production from the Broadway Plant, which is included in severance, relocation and other costs in the consolidated statement of operations. All amounts incurred were recorded within Sypris Technologies. The charges for 2019 were primarily related to mothball costs associated with the closed facility. The charges for 2018 included \$361,000 for equipment relocation costs and \$1,033,000 primarily related to mothball costs associated with the closed facility. A summary of the total pre-tax charges is as follows (in thousands):

	<u>Total Program</u>	<u>Costs Incurred</u>		<u>Remaining Costs to be Recognized</u>
		<u>Year Ended Dec. 31, 2019</u>	<u>Total Recognized to date</u>	
Severance and benefit related costs .....	\$ 1,350	\$ —	\$ 1,350	\$ —
Asset impairments .....	188	—	188	—
Equipment relocation costs .....	1,826	38	1,826	—
Other.....	<u>1,609</u>	<u>471</u>	<u>1,546</u>	<u>63</u>
	<u>\$ 4,973</u>	<u>\$ 509</u>	<u>\$ 4,910</u>	<u>\$ 63</u>

The Company expects to incur additional pre-tax costs of approximately \$63,000 within Sypris Technologies, all of which is expected to be cash expenditures.

As noted above, management expects to apply proceeds from the sale of underutilized or non-core assets to help fund the costs to transfer additional equipment from the Broadway Plant and the transition of the related production. The following assets have been segregated and included in assets held for sale in the consolidated balance sheets (in thousands):

	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Property, plant and equipment.....	\$ 13,346	\$ 11,207
Accumulated depreciation .....	<u>(11,113)</u>	<u>(9,733)</u>
Property, plant and equipment, net .....	<u>\$ 2,233</u>	<u>\$ 1,474</u>

**(5) Other Income, Net**

The Company recognized other income of \$1,256,000 during the year ended December 31, 2019. During 2019, the Company recognized a gain of \$1,500,000 as a result of a settlement agreement with one of its customers to resolve various outstanding disputes between the two parties. As a result of the agreement, the customer paid the Company \$1,500,000 in compensation during 2019. Additionally, the Company recognized a net gain of \$654,000 in the year ended December 31, 2019 related to the sale of idle assets and foreign currency related gains of \$152,000 related to the net U.S. dollar denominated monetary asset position of our Mexican subsidiaries for which the Mexican peso is the functional currency. This was offset by pension expense of \$970,000.

The Company recognized other income of \$1,436,000 during the year ended December 31, 2018. Subsequent to the transfer of production from the Broadway Plant, the primary water supply and sprinkler pipes within the facility suffered freeze damage during an extended period of extreme cold temperatures. The Company and its insurer reached a full and final settlement agreement with respect to the claim during the second quarter of 2018. During the year ended December 31, 2018, the Company received insurance proceeds of \$2,447,000 and recognized an insurance recovery gain of \$2,275,000, net of expenses incurred for claim related expenses. Additionally, the Company recognized foreign currency related gains of \$21,000, a net loss of \$249,000 related to the sale of certain idle assets, and pension expense of \$584,000.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

**(6) Accounts Receivable**

Accounts receivable consists of the following (in thousands):

	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Commercial .....	\$ 7,494	\$ 9,962
Allowance for doubtful accounts.....	(50)	(81)
Net .....	<u>\$ 7,444</u>	<u>\$ 9,881</u>

**(7) Inventory**

Inventory consists of the following (in thousands):

	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Raw materials.....	\$ 15,139	\$ 12,354
Work in process.....	5,889	6,331
Finished goods.....	1,675	1,313
Reserve for excess and obsolete inventory.....	(1,919)	(1,414)
Total .....	<u>\$ 20,784</u>	<u>\$ 18,584</u>

**(8) Other Current Assets**

Other current assets consist of the following (in thousands):

	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Prepaid expenses .....	\$ 835	\$ 576
Contract assets.....	906	839
Other.....	2,541	3,340
Total .....	<u>\$ 4,282</u>	<u>\$ 4,755</u>

Included in other current assets are income and VAT taxes refundable, tools, spare parts and other items, none of which exceed 5% of total current assets.

**(9) Property, Plant and Equipment**

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

	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Land and land improvements .....	\$ 50	\$ 219
Buildings and building improvements.....	8,108	11,178
Machinery, equipment, furniture and fixtures .....	55,520	59,179
Construction in progress.....	371	2,141
	64,049	72,717
Accumulated depreciation .....	(52,374)	(58,062)
	<u>\$ 11,675</u>	<u>\$ 14,655</u>

Depreciation expense, including amortization of assets recorded under finance leases, totaled approximately \$2,671,000 and \$2,648,000 for the years ended December 31, 2019 and 2018, respectively. Capital expenditures included in accounts payable or accrued liabilities were not material at December 31, 2019 and 2018, respectively.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

Included within property, plant and equipment were assets under finance leases as follows (in thousands):

	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Buildings and building improvements.....	\$ 3,128	\$ 2,995
Machinery, equipment, furniture and fixtures .....	<u>1,546</u>	<u>1,277</u>
	4,674	4,272
Accumulated depreciation .....	<u>(1,495)</u>	<u>(976)</u>
	<u>\$ 3,179</u>	<u>\$ 3,296</u>

**(10) Other Assets**

Other assets consist of the following (in thousands):

	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Long term spare parts .....	\$ 183	\$ 646
Long term deposits .....	396	507
Pension asset .....	607	138
Other.....	<u>343</u>	<u>224</u>
Total .....	<u>\$ 1,529</u>	<u>\$ 1,515</u>

**(11) Accrued Liabilities**

Accrued liabilities consist of the following (in thousands):

	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Salaries, wages, employment taxes and withholdings.....	\$ 2,416	\$ 2,019
Employee benefit plans .....	1,517	1,050
Accrued professional fees .....	966	821
Income, property and other taxes .....	355	453
Contract liabilities .....	5,769	8,369
Deferred gain from sale-leaseback.....	313	500
Other.....	<u>1,159</u>	<u>1,753</u>
Total .....	<u>\$ 12,495</u>	<u>\$ 14,965</u>

Included in other accrued liabilities are accrued operating expenses, accrued warranty expenses, accrued interest, and other items, none of which exceed 5% of total current liabilities.

**(12) Other Liabilities**

Other liabilities consist of the following (in thousands):

	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Noncurrent pension liability .....	\$ 4,026	\$ 4,272
Deferred gain from sale leaseback .....	1,616	3,093
Other.....	<u>1,879</u>	<u>1,131</u>
Total .....	<u>\$ 7,539</u>	<u>\$ 8,496</u>

Upon the adoption of Topic 842 on January 1, 2019, the remaining deferred gain is related to the finance lease portion on a 2016 sale lease-back related and is recognized in proportion to the amortization of the finance lease right-of-use asset. Included in other liabilities are long-term contract liabilities, deferred rent expenses and other items, none of which exceed 5% of total liabilities.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

**(13) Debt**

Long-term obligations consists of the following (in thousands):

	December 31,	
	2019	2018
Current:		
Current portion of finance lease obligations.....	\$ 684	\$ 593
Long Term:		
Note payable – related party .....	\$ 6,500	\$ 6,500
Finance lease obligations .....	2,351	2,804
Less unamortized debt issuance and modification costs.....	(37)	(51)
Long term debt and finance lease obligations, net of unamortized debt costs .....	\$ 8,813	\$ 9,253

The weighted average interest rate for outstanding borrowings at December 31, 2019 and 2018 was 8.0%. The Company had no capitalized interest in 2019 or 2018. Interest paid during the years ended December 31, 2019 and 2018 totaled approximately \$526,000 and \$526,000, respectively.

*Note Payable – Related Party*

The Company has received the benefit of cash infusions from GFCM in the form of secured promissory note obligations totaling \$6,500,000 in principal as of December 31, 2019 and 2018. GFCM is an entity controlled by the Company’s chairman, president and chief executive officer, Jeffrey T. Gill and one of our directors, R. Scott Gill. GFCM, Jeffrey T. Gill and R. Scott Gill are significant beneficial stockholders of the Company. The promissory note bears interest at a rate of 8.0% per year through March 31, 2019 and, thereafter is reset on April 1<sup>st</sup> of each year, at the greater of 8.0% or 500 basis points above the five-year Treasury note average during the preceding 90-day period, in each case, payable quarterly. The maturity dates for the obligation are as follows: \$2,500,000 of the obligation on April 1, 2021, \$2,000,000 on April 1, 2023, and the balance on April 1, 2025. The note allows for up to an 18-month deferral of payment for up to 60% of the interest due on the portion of the notes maturing in April of 2021 and 2023.

Obligations under the promissory note are guaranteed by all of the subsidiaries and are secured by a first priority lien on substantially all assets of the Company.

*Finance Lease Obligations*

On March 9, 2016, the Company completed the sale of its 24-acre Toluca property for 215,000,000 Mexican Pesos, or approximately \$12,182,000 in U.S. dollars. Simultaneously, the Company entered into a ten-year lease of the 9 acres and buildings currently occupied by the Company and needed for its ongoing business in Toluca. As a result of the Toluca Sale-Leaseback, the Company has a finance lease obligation of \$2,421,000 for the building as of December 31, 2019.

In January 2018, the Company entered into a 36-month capital lease for \$1,277,000 for new production equipment installed at its Sypris Electronics facility during 2018. The balance of the finance lease obligation as of December 31, 2019 was \$384,000.

In February 2019, the Company entered into a 60-month capital lease for \$269,000 for new machinery at its Sypris Technologies facility in the U.S. The balance of the finance lease obligation as of December 31, 2019 was \$230,000.

**(14) Fair Value of Financial Instruments**

Cash, accounts receivable, accounts payable and accrued liabilities are reflected in the consolidated financial statements at their carrying amount which approximates fair value because of the short-term maturity of those instruments. The carrying amount of debt outstanding at December 31, 2019 approximates fair value, and is based upon a market approach (Level 2).

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

**(15) Employee Benefit Plans**

Sypris Technologies sponsors noncontributory defined benefit pension plans (the “Pension Plans”) covering certain of its employees. The Pension Plans covering salaried and management employees provide pension benefits that are based on the employees’ highest five-year average compensation within ten years before retirement. The Pension Plans covering hourly employees and union members generally provide benefits at stated amounts for each year of service. All of the Company’s pension plans are frozen to new participants and certain plans are frozen to additional benefit accruals. The Company’s funding policy is to make the minimum annual contributions required by the applicable regulations. The Pension Plans’ assets are primarily invested in equity securities and fixed income securities.

The following table details the components of pension (income) expense (in thousands):

	<u>Year ended December 31.</u>	
	<u>2019</u>	<u>2018</u>
Service cost .....	\$ 4	\$ 4
Interest cost on projected benefit obligation.....	1,407	1,315
Net amortization of actuarial loss.....	666	632
Expected return on plan assets .....	<u>(1,103)</u>	<u>(1,363)</u>
Net periodic benefit cost.....	<u>\$ 974</u>	<u>\$ 588</u>

The following are summaries of the changes in the benefit obligations and plan assets and of the funded status of the Pension Plans (in thousands):

	<u>December 31.</u>	
	<u>2019</u>	<u>2018</u>
Change in benefit obligation:		
Benefit obligation at beginning of year .....	\$ 34,690	\$ 39,179
Service cost.....	4	4
Interest cost.....	1,407	1,315
Actuarial (gain) loss.....	2,835	(2,913)
Benefits paid.....	<u>(2,886)</u>	<u>(2,895)</u>
Benefit obligation at end of year .....	<u>\$ 36,050</u>	<u>\$ 34,690</u>
Change in plan assets:		
Fair value of plan assets at beginning of year .....	\$ 30,199	\$ 34,398
Actual return on plan assets .....	4,043	(1,381)
Company contributions.....	382	77
Benefits paid.....	<u>(2,886)</u>	<u>(2,895)</u>
Fair value of plan assets at end of year .....	<u>\$ 31,738</u>	<u>\$ 30,199</u>
Underfunded status of the plans .....	<u>\$ (4,312)</u>	<u>\$ (4,491)</u>
Balance sheet assets (liabilities):		
Other assets.....	\$ 607	\$ 138
Accrued liabilities.....	(893)	(357)
Other liabilities .....	<u>(4,026)</u>	<u>(4,272)</u>
Net amount recognized.....	<u>\$ (4,312)</u>	<u>\$ (4,491)</u>
Pension plans with accumulated benefit obligation in excess of plan assets:		
Projected benefit obligation .....	\$ 24,843	\$ 23,466
Accumulated benefit obligation.....	24,843	23,466
Fair value of plan assets.....	19,924	18,838

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Projected benefit obligation and net periodic pension cost assumptions:		
Discount rate – projected benefit obligation .....	3.15%	4.25%
Discount rate – net periodic pension cost .....	4.25	3.55
Rate of compensation increase .....	4.00	4.00
Expected long-term rate of return on plan assets.....	3.65 – 3.90	3.95 – 4.30
Weighted average asset allocation:		
Equity securities.....	18%	16%
Debt securities .....	78	80
Other.....	<u>4</u>	<u>4</u>
Total.....	<u>100%</u>	<u>100%</u>

The fair values of our pension plan assets as of December 31, 2019 are as follows (in thousands):

	<b>Quoted Prices In Active Markets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>
Asset categories:		
Cash and cash equivalents .....	\$ 2,228	\$ —
Equity securities:		
U.S. Large Cap.....	1,935	—
U.S. Mid Cap .....	1,067	—
U.S. Small Cap.....	609	—
World Equity.....	2,214	—
Real Estate.....	546	—
Other .....	757	—
Fixed income securities .....	<u>3,394</u>	<u>18,988</u>
Total Plan Assets .....	<u>\$ 12,750</u>	<u>\$ 18,988</u>

The fair values of our pension plan assets as of December 31, 2018 are as follows (in thousands):

	<b>Quoted Prices In Active Markets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>
Asset categories:		
Cash and cash equivalents .....	\$ 1,415	\$ —
Equity securities:		
U.S. Large Cap.....	1,590	—
U.S. Mid Cap .....	967	—
U.S. Small Cap.....	489	—
World Equity.....	1,886	—
Real Estate.....	458	—
Other .....	690	—
Fixed income securities .....	<u>5,237</u>	<u>17,467</u>
Total Plan Assets .....	<u>\$ 12,732</u>	<u>\$ 17,467</u>

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

Investments in our defined benefit plans are stated at fair value. The following valuation methods were used to value our pension assets:

- Equity securities.....The fair value of equity securities is determined by either direct or indirect quoted market prices. When the value of assets held in separate accounts is not published, the value is based on the underlying holdings, which are primarily direct quoted market prices on regulated financial exchanges.
- Fixed income securities.....The fair value of fixed income securities is determined by either direct or indirect quoted market prices. When the value of assets held in separate accounts is not published, the value is based on the underlying holdings, which are primarily direct quoted market prices on regulated financial exchanges.
- Cash and cash equivalents.....The fair value of cash and cash equivalents is set equal to its cost.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Company believes the valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The Company uses December 31 as the measurement date for the Pension Plans. Total estimated contributions expected to be paid to the plans during 2020 is \$893,000, which represents the minimum funding amounts required by federal law. The expected long-term rates of return on plan assets for determining net periodic pension cost for 2019 and 2018 were chosen by the Company from a best estimate range determined by applying anticipated long-term returns and long-term volatility for various assets categories to the target asset allocation of the plan. The target asset allocation of plan assets is equity securities ranging 0-55%, fixed income securities ranging 35-100% and non-traditional/other of 0-10% of total investments.

When establishing the expected long-term rate of return on our U.S. pension plan assets, the Company considered historical performance and forward looking return estimates reflective of our portfolio mix and investment strategy. Based on the most recent analysis of projected portfolio returns, the Company concluded that the use of 3.90% for the Louisville Hourly Plan, 3.85% for the Marion Plan and 3.65% for the Louisville Salaried Plan as the expected return on our U.S. pension plan assets for 2019 was appropriate.

Actuarial gains and losses, which are primarily the result of changes in the discount rate and other assumptions and differences between actual and expected asset returns, are deferred in Accumulated other comprehensive loss and amortized to expense following the corridor approach. We use the average remaining service period of active participants unless almost all of the plan’s participants are inactive, in which case we use the average remaining life expectancy for all active and inactive participants. Accumulated other comprehensive loss at December 31, 2019 includes \$13,007,000 of unrecognized actuarial losses that have not yet been recognized in net periodic pension cost. The actuarial loss included in accumulated other comprehensive loss and expected to be recognized in net periodic pension cost during the fiscal year ending December 31, 2020 is \$635,000. The actual loss reclassified from accumulated other comprehensive loss for 2019 and 2018 was \$666,000 and \$632,000, respectively.

At December 31, 2019, the benefits expected to be paid in each of the next five fiscal years, and in aggregate for the five fiscal years thereafter are as follows (in thousands):

2020.....	\$ 2,839
2021.....	2,782
2022.....	2,715
2023.....	2,638
2024.....	2,571
2025-2029 .....	<u>11,582</u>
Total .....	<u>\$ 25,127</u>

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

The Company sponsors a defined contribution plan (the “Defined Contribution Plan”) for substantially all domestic employees of the Company. The Defined Contribution Plan is intended to meet the requirements of Section 401(k) of the Internal Revenue Code. The Defined Contribution Plan allows the Company to match participant contributions up to 3% and provide discretionary contributions. In connection with the matching contributions, the Company recognized compensation expense of approximately \$392,000 and \$376,000 in 2019 and 2018, respectively.

In addition, certain of the Company’s non-U.S. employees are covered by various defined benefit and defined contribution plans. The Company’s expenses for these plans totaled approximately \$40,000 and \$41,000 in 2019 and 2018, respectively. The aggregate benefit plan assets and accumulated benefit obligation of these plans are not significant.

**(16) Commitments and Contingencies**

As of December 31, 2019, the Company had outstanding purchase commitments of approximately \$8,792,000 primarily for the acquisition of inventory. These commitments are for goods and services to be acquired in the ordinary course of business and are fulfilled by our vendors within a short period of time.

The Company bears insurance risk as a member of a group captive insurance entity for certain general liability, automobile and workers’ compensation insurance programs and a self-insured employee health program. The Company records estimated liabilities for its insurance programs based on information provided by the third-party plan administrators, historical claims experience, expected costs of claims incurred but not paid, and expected costs to settle unpaid claims. The Company monitors its estimated insurance-related liabilities on a quarterly basis. As facts change, it may become necessary to make adjustments that could be material to the Company’s consolidated results of operations and financial condition.

The Company is involved in certain litigation and contract issues arising in the normal course of business. While the outcome of these matters cannot, at this time, be predicted in light of the uncertainties inherent therein, management does not expect that these matters will have a material adverse effect on the consolidated financial position or results of operations of the Company. Additionally, the Company believes its product liability insurance is adequate to cover all potential product liability claims.

The Company accounts for loss contingencies in accordance with U.S. generally accepted accounting principles (GAAP). Estimated loss contingencies are accrued only if the loss is probable and the amount of the loss can be reasonably estimated. With respect to a particular loss contingency, it may be probable that a loss has occurred but the estimate of the loss is within a range or undeterminable. If the Company deems an amount within the range to be a better estimate than any other amount within the range, that amount will be accrued. However, if no amount within the range is a better estimate than any other amount, the minimum amount of the range is accrued.

The Company has various current and previously-owned facilities subject to a variety of environmental regulations. The Company has received certain indemnifications from either companies previously owning these facilities or from purchasers of those facilities. As of December 31, 2019 and 2018, no amounts were accrued for any environmental matters. See “Legal Proceedings” in Part I, Item 3 of this Annual Report on Form 10-K.

On December 27, 2017, the U.S. Department of Labor (the “DOL”) filed a lawsuit alleging that the Company had misinterpreted the language of its Company’s 401(k) Plans (collectively, the “Plan”). The DOL does not appear to dispute that the Company reached such interpretation in good faith and after consulting with independent ERISA counsel. If the DOL’s allegations were upheld by a court, the Company could be required to make additional contributions into the accounts of its Plan participants. The Company regards the DOL’s allegations to be without merit and is continuing to vigorously defend the matter.

During the fourth quarter of 2018, the Company resolved an outstanding disputed legal fee for an amount less than originally charged. The resolution of the disputed legal fee resulted in a decrease in selling, general and administrative expense of \$1,890,000 for the year ended December 31, 2018.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

**(17) Stock Option and Purchase Plans**

The Company's stock compensation program provides for the grant of restricted stock (including performance-based restricted stock), unrestricted stock, stock options and stock appreciation rights. A total of 3,655,088 shares of common stock were registered for issuance under the 2010 Omnibus Plan. On May 19, 2015, the 2010 Omnibus Plan was replaced with the 2015 Omnibus Plan. A total of 3,476,021 shares were registered for issuance under the 2015 Omnibus Plan. Additionally, awards under the 2010 Omnibus Plan that are cancelled without having been fully exercised or vested are available again for new awards under the 2015 Omnibus Plan. The aggregate number of shares available for future grant as of December 31, 2019 and 2018 was 1,153,271 and 1,444,771, respectively.

The 2010 and 2015 Omnibus Plans provide for restrictions which lapse after three years. During the restricted period, which is commensurate with each vesting period, the recipient has the right to receive dividends and voting rights for the shares. Generally, if a recipient leaves the Company before the end of the restricted period or if performance requirements, if any, are not met, the shares will be forfeited.

Under the plans, the Company may grant options to purchase common stock to officers, key employees and non-employee directors. Options may be granted at not less than the market price on the date of grant. Stock option grants under the 2010 and 2015 Omnibus Plans include a five year life along with vesting after three years of service.

Compensation expense is measured based on the fair value at the date of grant and is recognized on a straight-line basis over the vesting period. Fair value for restricted shares is equal to the stock price on the date of grant, while the fair value of each stock option grant is estimated on the date of grant using the Black-Scholes option-pricing method. The Company uses historical Company and industry data to estimate the expected price volatility, the expected option life and the expected dividend yield. The risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant for the estimated life of the option. Forfeitures are recorded as they occur. Stock based compensation expense of \$469,000 and \$637,000 has been recorded in selling, general and administrative expense in the consolidated statements of operations for the years ended December 31, 2019 and 2018, respectively.

The following weighted average assumptions were used to estimate the fair value of options granted using the Black-Scholes option-pricing model:

	<u>Year ended December 31,</u>	
	<u>2019</u>	<u>2018</u>
Expected life (years).....	4.0	4.0
Expected volatility.....	53.9%	51.8%
Risk-free interest rates.....	2.30%	2.65%
Expected dividend yield .....	0.0%	0.0%

A summary of the restricted stock activity is as follows:

	<u>Number of Shares</u>	<u>Weighted- average Grant Date Fair Value</u>	<u>Weighted- average Remaining Term</u>	<u>Aggregate Intrinsic Value</u>
Nonvested shares at January 1, 2019.....	843,000	\$ 1.01		
Granted .....	—	—		
Vested.....	(508,500)	0.99		
Forfeited .....	<u>(10,000)</u>	<u>1.06</u>		
Nonvested shares at December 31, 2019.....	<u>324,500</u>	<u>\$ 1.03</u>	0.61	<u>\$ 253,000</u>

The total fair value of shares vested during 2019 and 2018 was \$533,000 and \$381,000, respectively.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

The following table summarizes option activity for the year ended December 31, 2019:

	<u>Number of Shares</u>	<u>Weighted- average Exercise Price Per Share</u>	<u>Weighted- average Remaining Term</u>	<u>Aggregate Intrinsic Value</u>
Outstanding at January 1, 2019 .....	2,326,250	\$ 1.47		
Granted .....	706,000	1.06		
Exercised .....	—	—		
Forfeited.....	(160,000)	1.48		
Expired.....	<u>(304,500)</u>	<u>2.33</u>		
Outstanding at December 31, 2019 .....	<u>2,567,750</u>	<u>\$ 1.26</u>	2.31	<u>\$ —</u>
Exercisable at December 31, 2019 .....	<u>1,010,500</u>	<u>\$ 1.21</u>	0.41	<u>\$ —</u>

The weighted average grant date fair value based on the Black-Scholes option pricing model for options granted in the years ended December 31, 2019 and 2018 was \$0.46 and \$0.69 per share, respectively. There were no options exercised in 2019 or 2018.

As of December 31, 2019, there was \$478,000 of total unrecognized compensation cost related to unvested share-based compensation granted under the plans. That cost is expected to be recognized over a weighted-average period of 1.0 year. The total fair value of option shares vested during the years ended December 31, 2019 and 2018 was \$318,000 and \$184,000, respectively.

**(18) Stockholders' Equity**

As of December 31, 2019 and 2018, 24,850 shares of the Company's preferred stock were designated as Series A Preferred Stock in accordance with the terms of our stockholder rights plan, which expired in October 2011. There are no shares of Series A Preferred Stock currently outstanding, and there are no current plans to issue any such shares.

The holders of our common stock were not entitled to any payment as a result of the expiration of the rights plan and the rights issued thereunder.

The Company's accumulated other comprehensive loss consists of employee benefit related adjustments and foreign currency translation adjustments.

Accumulated other comprehensive loss consisted of the following (in thousands):

	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Foreign currency translation adjustments, net of tax.....	\$ (10,623)	\$ (10,967)
Employee benefit related adjustments – U.S, net of tax.....	(13,544)	(14,177)
Employee benefit related adjustments – Mexico, net of tax.....	<u>116</u>	<u>302</u>
Accumulated other comprehensive loss .....	<u>\$ (24,051)</u>	<u>\$ (24,842)</u>

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

Changes in each component of accumulated other comprehensive loss consisted of the following:

	<u>Foreign Currency Translation</u>	<u>Defined Benefit Plans</u>	<u>Accumulated Other Comprehensive Loss</u>
Balance at January 1, 2018.....	\$ (10,915)	\$ (14,636)	\$ (25,551)
Currency translation adjustments, net of tax.....	(52)	—	(52)
Net actuarial gain for the year, net of tax.....	—	276	276
Amortization for the year, net of tax.....	<u>—</u>	<u>485</u>	<u>485</u>
Balance at December 31, 2018.....	\$ (10,967)	\$ (13,875)	\$ (24,842)
Currency translation adjustments, net of tax.....	344	—	344
Net actuarial loss for the year, net of tax .....	—	(64)	(64)
Amortization for the year, net of tax.....	<u>—</u>	<u>511</u>	<u>511</u>
Balance at December 31, 2019.....	<u>\$ (10,623)</u>	<u>\$ (13,428)</u>	<u>\$ (24,051)</u>

**(19) Income Taxes**

The Company accounts for income taxes under the liability method. Accordingly, deferred income taxes have been provided for temporary differences between the recognition of revenue and expenses for financial and income tax reporting purposes and between the tax basis of assets and liabilities and their reported amounts in the consolidated financial statements.

The components of income (loss) before taxes are as follows (in thousands):

	<u>Year ended December 31,</u>	
	<u>2019</u>	<u>2018</u>
Domestic .....	\$ (5,337)	\$ (5,331)
Foreign .....	<u>1,384</u>	<u>1,621</u>
Total .....	<u>\$ (3,953)</u>	<u>\$ (3,710)</u>

The components of income tax (benefit) expense are as follows (in thousands):

	<u>Year ended December 31,</u>	
	<u>2019</u>	<u>2018</u>
Current:		
Federal.....	\$ —	\$ —
State.....	(14)	2
Foreign.....	<u>270</u>	<u>302</u>
Total current income tax expense.....	256	304
Deferred:		
Federal.....	(217)	(191)
State.....	(23)	(21)
Foreign.....	<u>(20)</u>	<u>(297)</u>
Total deferred income tax (benefit) expense .....	<u>(260)</u>	<u>(509)</u>
Income tax (benefit) expense, net.....	<u>\$ (4)</u>	<u>\$ (205)</u>

Income tax (benefit) expense for each year is allocated to continuing operations, discontinued operations, extraordinary items, other comprehensive income, the cumulative effects of accounting changes, and other charges or credits recorded directly to shareholders' equity. ASC 740-20-45 *Income Taxes, Intra-period Tax Allocation, Other Presentation Matters* includes an exception to the general principle of intra-period tax allocations. The codification source states that the tax effect of pretax income or loss from continuing operations generally should be determined by a computation that considers only the tax effects of items that are included in continuing operations. The exception to that incremental approach is that all items (i.e. other comprehensive income, discontinued operations, etc.) be considered in determining the amount of tax benefit that results from a loss from continuing operations and that benefit

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

should be allocated to continuing operations. That is, when a company has a current period loss from continuing operations, management must consider income recorded in other categories in determining the tax benefit that is allocated to continuing operations. This includes situations in which a company has recorded a full valuation allowance at the beginning and end of the period, and the overall tax provision for the year is zero. The intraperiod tax allocation is performed once the overall tax provision has been computed and allocates that provision to various income statement (continuing operations, discontinued operations), other comprehensive income and balance sheet captions. While the intraperiod tax allocation does not change the overall tax provision, it results in a gross-up of the individual components. Additionally, tax jurisdictions must be considered separately; therefore the allocation to the U.S. and Mexico must be looked at separately.

As the Company experienced a net loss from operations in the U.S. for the years ended December 31, 2019 and 2018 and other comprehensive income from employee benefit adjustments, the Company has allocated income tax expense against the components of other comprehensive income in 2019 and 2018 using a 23.3% effective tax rate. Income tax benefit for the years ended December 31, 2019 and 2018 includes a benefit of \$240,000 and \$212,000, respectively due to the required intraperiod tax allocation. Conversely, other comprehensive income for the years ended December 31, 2019 and 2018 includes income tax expense of \$240,000 and \$212,000, respectively.

On December 22, 2017, the U.S. bill commonly referred to as the Tax Cuts and Jobs Act (“Tax Reform Act”) was enacted, which significantly changed U.S. tax law by, among other things, lowering corporate income tax rates, implementing a territorial tax system and imposing a one-time repatriation tax on deemed repatriated earnings of foreign subsidiaries. The Tax Reform Act reduced the U.S. corporate income tax rate from a maximum of 35% to a flat 21% rate, effective January 1, 2018. The Tax Reform Act also provided for a one-time deemed repatriation of post-1986 undistributed foreign subsidiary earnings and profits (“E&P”) through the year ended December 31, 2017. The Global Intangible Low-Taxed Income (“GILTI”) provisions of the Tax Reform Act require the Company to include in its U.S. income tax return foreign subsidiary earnings in excess of an allowable return on the foreign subsidiary’s tangible assets. The Company is subject to incremental U.S. tax on GILTI income due to expense allocations required by the U.S. foreign tax credit rules. The Company has elected to account for the GILTI tax in the period in which it is incurred, and therefore has not provided any deferred tax impacts of GILTI in its consolidated financial statements.

The Company files a consolidated federal income tax return which includes all domestic subsidiaries. State income taxes paid in the U.S. during 2019 and 2018 totaled \$37,000 and \$33,000, respectively. State income tax refunds received in the U.S. during 2019 and 2018 totaled \$51,000 and \$12,000, respectively. Foreign income taxes paid during 2019 and 2018 totaled \$293,000 and \$109,000, respectively. There were no foreign refunds received in 2019 and 2018. There were no federal taxes paid in 2019 and 2018. The Company received federal refunds of \$92,000 in 2019 and there were no federal refunds received in 2018. At December 31, 2019, the Company had \$136,127,000 of federal net operating loss carryforwards available to offset future federal taxable income. The pre-2018 federal net operating loss carryforwards expire in various amounts from 2026 to 2037. Federal net operating loss carryforwards generated in 2018 and forward will have an unlimited carryforward period as part of the Tax Act. The indefinite lived net operating loss carryforwards as of December 31, 2019 are approximately \$1,769,000.

At December 31, 2019, the Company had \$2,537,000 of state net operating loss carryforwards available to offset future state taxable income, the majority of which relates to Florida and Kentucky. The pre-2018 state net operating loss carryforwards totaling approximately \$2,431,000 expire in various amounts from 2026 to 2037. State net operating loss carryforwards generated in 2018 and forward will have an unlimited carryforward. The indefinite lived state net operating loss carryforwards as of December 31, 2019 are approximately \$106,000.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

The following is a reconciliation of income tax (benefit) expense to that computed by applying the federal statutory rate to income (loss) before income taxes (in thousands):

	<u>Year ended December 31,</u>	
	<u>2019</u>	<u>2018</u>
Federal tax expense at the statutory rate.....	\$ (830)	\$ (779)
Current year permanent differences .....	257	82
State income taxes, net of federal tax impact .....	(131)	(118)
Effect of tax rates of foreign subsidiaries .....	125	154
Currency translation effect on temporary differences .....	312	189
Change in valuation allowance.....	(2,377)	358
Intraperiod tax allocation.....	(240)	(212)
State NOL carryforwards .....	3,326	320
Other items .....	(446)	(199)
Income tax (benefit) expense, net.....	<u>\$ (4)</u>	<u>\$ (205)</u>

ASC 740, *Income Taxes*, requires that a valuation allowance be established when it is more likely than not that all or a portion of a deferred tax asset will not be realized. The net cumulative domestic and foreign losses for the current and prior two years represents negative evidence under the provisions of ASC 740 requiring the Company to establish a valuation allowance against all U.S. deferred tax assets and a portion of its non-U.S. deferred tax assets. Until an appropriate level and characterization of profitability is attained, the Company expects to continue to maintain a valuation allowance on its net deferred tax assets related to future U.S. and a portion of its non-U.S. tax benefits.

The gross deferred tax asset for the Company's Mexican subsidiaries was \$4,054,000 and \$4,434,000 as of December 31, 2019 and 2018, respectively.

Deferred income tax assets and liabilities are as follows (in thousands):

	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Deferred tax assets:		
Compensation and benefit accruals .....	\$ 359	\$ 450
Inventory valuation.....	866	759
Federal and state net operating loss carryforwards.....	30,591	33,567
Deferred revenue .....	975	90
Accounts receivable allowance .....	8	11
Depreciation .....	85	39
Defined benefit pension plan.....	591	573
Lease liabilities.....	1,334	—
Foreign deferred revenue and other provisions .....	4,054	4,434
Other .....	661	874
Total .....	39,524	40,797
Domestic valuation allowance.....	(34,338)	(36,363)
Foreign valuation allowance.....	(3,717)	(4,137)
Total deferred tax assets.....	1,469	297
Deferred tax liabilities:		
Right-of-use assets, net.....	(1,132)	—
Total deferred tax liabilities .....	(1,132)	—
Net deferred tax asset .....	<u>\$ 337</u>	<u>\$ 297</u>

The ASC Income Tax topic includes guidance for the accounting for uncertainty in income taxes recognized in an enterprise's financials. Specifically, the guidance prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The total amount of gross unrecognized tax benefits as of December 31, 2019 and 2018 was \$200,000. There were no changes to the unrecognized tax benefit balance during the years ended December 31, 2019 and 2018.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

If the Company's positions are sustained by the taxing authority, the entire balance at December 31, 2019 would reduce the Company's effective tax rate. The Company does not expect its unrecognized tax benefits to change significantly over the next 12 months. The Company recognizes accrued interest and penalties related to uncertain tax positions in income tax expense. As of December 31, 2019 and 2018, the Company does not have an accrual for the payment of tax-related interest and penalties.

The Company files income tax returns in the U.S. federal jurisdiction, and various state and foreign jurisdictions. The Internal Revenue Service (IRS) is not currently examining the Company's U.S. income tax returns for 2016 through 2018, for which the statute has yet to expire. In addition, open tax years related to state and foreign jurisdictions remain subject to examination.

**(20) Loss Per Common Share**

The Company computes earnings per share using the two-class method, which is an earnings allocation formula that determines earnings per share for common stock and participating securities. Restricted stock granted by the Company is considered a participating security since it contains a non-forfeitable right to dividends.

Our potentially dilutive securities include potential common shares related to our stock options and restricted stock. Diluted earnings per share considers the impact of potentially dilutive securities except in periods in which there is a loss because the inclusion of the potential common shares would have an anti-dilutive effect. Diluted earnings per share excludes the impact of common shares related to our stock options in periods in which the option exercise price is greater than the average market price of our common stock for the period. All potential common shares were excluded from diluted earnings per share for the years ended December 31, 2019 and 2018 because the effect of inclusion would be anti-dilutive.

A reconciliation of the weighted average shares outstanding used in the calculation of basic and diluted loss per common share is as follows (in thousands):

	<u>Year ended December 31,</u>	
	<u>2019</u>	<u>2018</u>
Loss attributable to stockholders:		
Net loss as reported.....	\$ (3,949)	\$ (3,505)
Less distributed and undistributed earnings allocable to restricted award holders .....	<u>—</u>	<u>—</u>
Net loss allocable to common stockholders.....	<u>\$ (3,949)</u>	<u>\$ (3,505)</u>
Loss per common share attributable to stockholders:		
Basic.....	<u>\$ (0.19)</u>	<u>\$ (0.17)</u>
Diluted .....	<u>\$ (0.19)</u>	<u>\$ (0.17)</u>
Weighted average shares outstanding – basic .....	20,865	20,512
Weighted average additional shares assuming conversion of potential common shares .....	<u>—</u>	<u>—</u>
Weighted average shares outstanding – diluted .....	<u>20,865</u>	<u>20,512</u>

**(21) Segment Information**

The Company is organized into two business segments, Sypris Technologies and Sypris Electronics. The segments are each managed separately because of the distinctions between the products, markets, customers, technologies, and workforce skills of the segments. Sypris Technologies generates revenue primarily from the sale of forged, machined, welded and heat-treated steel components primarily for the heavy commercial vehicle and high-pressure energy pipeline applications. Sypris Electronics provides circuit card and box build manufacturing, high reliability manufacturing, systems assembly and integration, design for manufacturability and design to specification work to customers in the market for aerospace and defense electronics. There was no intersegment net revenue recognized for any year presented.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

The Company includes the unallocated costs of its corporate office, including the employment costs of its senior management team and other corporate personnel, administrative costs and net corporate interest expense incurred at the corporate level under the caption “General, corporate and other” in the table below. Such unallocated costs include those for centralized information technology, finance, legal and human resources support teams, certain professional fees, director fees, corporate office rent, certain self-insurance costs and recoveries, software license fees and various other administrative expenses that are not allocated to our reportable segments. The unallocated assets include cash and cash equivalents maintained in its domestic treasury accounts and the net book value of corporate facilities and related information systems. The unallocated liabilities consist primarily of the related party notes payable. Domestic income taxes are calculated at an entity level and are not allocated to our reportable segments. Corporate capital expenditures and depreciation and amortization include items attributable to the unallocated fixed assets of the corporate office and related information systems.

The following table presents financial information for the reportable segments of the Company (in thousands):

	<u>Year ended December 31,</u>	
	<u>2019</u>	<u>2018</u>
Net revenue from unaffiliated customers:		
Sypris Technologies.....	\$ 61,683	\$ 59,816
Sypris Electronics.....	<u>26,208</u>	<u>28,153</u>
	<u>\$ 87,891</u>	<u>\$ 87,969</u>
Gross profit:		
Sypris Technologies .....	\$ 9,785	\$ 7,523
Sypris Electronics.....	<u>98</u>	<u>49</u>
	<u>\$ 9,883</u>	<u>\$ 7,572</u>
Operating income (loss):		
Sypris Technologies .....	\$ 4,257	\$ 3,207
Sypris Electronics.....	(2,999)	(2,555)
General, corporate and other.....	<u>(5,564)</u>	<u>(4,948)</u>
	<u>\$ (4,306)</u>	<u>\$ (4,296)</u>
Interest expense, net:		
Sypris Technologies .....	\$ 377	\$ 293
Sypris Electronics.....	63	117
General, corporate and other.....	<u>463</u>	<u>440</u>
	<u>\$ 903</u>	<u>\$ 850</u>
Other (income) expense, net:		
Sypris Technologies .....	\$ 272	\$ (1,434)
Sypris Electronics.....	(33)	—
General, corporate and other.....	<u>(1,495)</u>	<u>(2)</u>
	<u>\$ (1,256)</u>	<u>\$ (1,436)</u>
Income (loss) before income taxes:		
Sypris Technologies .....	\$ 3,609	\$ 4,349
Sypris Electronics.....	(3,029)	(2,672)
General, corporate and other.....	<u>(4,533)</u>	<u>(5,387)</u>
	<u>\$ (3,953)</u>	<u>\$ (3,710)</u>
Income tax expense (benefit), net:		
Sypris Technologies .....	\$ 250	\$ 5
Sypris Electronics.....	—	—
General, corporate and other.....	<u>(254)</u>	<u>(210)</u>
	<u>\$ (4)</u>	<u>\$ (205)</u>

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

	<u>Year ended December 31,</u>	
	<u>2019</u>	<u>2018</u>
Depreciation and amortization:		
Sypris Technologies .....	\$ 1,927	\$ 2,029
Sypris Electronics .....	506	515
General, corporate and other.....	<u>238</u>	<u>104</u>
	<u>\$ 2,671</u>	<u>\$ 2,648</u>
Capital expenditures:		
Sypris Technologies .....	\$ 693	\$ 1,311
Sypris Electronics .....	97	173
General, corporate and other.....	<u>69</u>	<u>567</u>
	<u>\$ 859</u>	<u>\$ 2,051</u>
	<u>December 31,</u>	
	<u>2019</u>	<u>2018</u>
Total assets:		
Sypris Technologies .....	\$ 29,694	\$ 31,312
Sypris Electronics .....	24,985	19,208
General, corporate and other.....	<u>5,377</u>	<u>11,048</u>
	<u>\$ 60,056</u>	<u>\$ 61,568</u>
Total liabilities:		
Sypris Technologies .....	\$ 19,989	\$ 23,644
Sypris Electronics .....	17,416	15,180
General, corporate and other.....	<u>9,220</u>	<u>7,910</u>
	<u>\$ 46,625</u>	<u>\$ 46,734</u>

The Company's export sales from the U.S. totaled \$7,239,000 and \$4,155,000 in 2019 and 2018, respectively. Approximately \$40,536,000 and \$39,744,000 of net revenue in 2019 and 2018, respectively, and \$6,669,000 and \$7,162,000 of long lived assets at December 31, 2019 and 2018, respectively, and net assets of \$9,899,000 and \$6,495,000 at December 31, 2019 and 2018 relate to the Company's international operations.

## **Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure**

None.

### **Item 9A. Controls and Procedures**

#### **Evaluation of Disclosure Controls and Procedures**

An evaluation was performed under the supervision and with the participation of the Company's management, including the President and Chief Executive Officer (the CEO) and the Chief Financial Officer (the CFO), of the effectiveness of the design and operation of the Company's disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934. Based on that evaluation, the Company's management, including the CEO and CFO, concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report.

#### **Remediation of Previously Disclosed Material Weakness**

The Company identified misstatements in the previously-reported quarter ended March 31, 2019. The misstatements were the result of improperly designed controls around the implementation of a new enterprise resource planning system ("ERP system") at our Sypris Electronics segment effective January 1, 2019. Due to data entry processing errors that were made following this transition to the new ERP system, certain vendor invoices related to raw material inventory receipts in the first quarter of 2019 for the Sypris Electronics segment were incorrectly recorded in the second quarter of 2019. These errors resulted in an understatement of accounts payable and cost of sales as of and for the quarter ended March 31, 2019.

In connection with the restatement of Company's financial statements for the quarter ended March 31, 2019, the Company identified two material weaknesses in internal controls over financial reporting that arose from the new ERP system implementation. The two material weaknesses were:

- The ineffective design and implementation of effective controls with respect to the ERP system transition. Specifically, we did not maintain adequate control over user access within the ERP system to restrict access to accounting period changes in the financial reporting modules. Additionally, we did not exercise sufficient oversight over the ERP system transition, design effective controls over the ERP implementation to ensure appropriate data conversion and data integrity, or provide sufficient end user training to our employees to ensure that our employees could effectively operate the new ERP system and carry out their responsibilities.
- Inadequate process level and monitoring controls in the area of accounting close and financial reporting. Specifically, we did not have appropriate controls around the review of account reconciliations, and related cut-off, and monitoring of the accounting close cycle.

The Audit Committee, the Board of Directors, and management are committed to maintaining a strong internal control environment. As a result, the Company took immediate action in developing and implementing remediation plans to address the material weaknesses outlined above. The remediation efforts included the following:

- User Access – We have restricted the ability of accounting personnel to modify data entry fields that relate to previously closed accounting periods for accounts payable processing.
- Oversight – We have established a plan to address the control deficiencies arising from our ERP system conversions, including additional training for accounting personnel and a more formal review and documentation process around financial reporting.
- Accounting Close and Financial Reporting – We have implemented additional analysis and review procedures related to the cost of goods sold variance accounts on a monthly basis and additional controls over the closing of accounting periods within the ERP system. We have hired additional qualified personnel to assist management with its financial statement close process and to provide additional oversight of our financial reporting.

During the fourth quarter of 2019, we completed our testing of the operating effectiveness of the implemented controls and found them to be effective. As a result we have concluded the material weakness has been fully remediated and no longer exists as of December 31, 2019.

**SYPRIS SOLUTIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – CONTINUED**

**Changes in Internal Control Over Financial Reporting**

Other than the updates and remediation efforts described above, there were no changes in our internal control over financial reporting that occurred during the quarter ended December 31, 2019 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. We did, however, implement certain changes to our internal control over financial reporting in connection with the implementation of the lease accounting standard and disclosure requirements of Accounting Standards Codification Topic 842. The changes primarily related to the design and implementation of controls related to the preparation and review of the new measurement and disclosure requirements of this new accounting standard.

**Management’s Report on Internal Control over Financial Reporting**

The management of Sypris Solutions, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). Our internal control system was designed to provide reasonable assurance to Sypris management and its Board of Directors regarding the preparation and fair presentation of published consolidated financial statements.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can only provide reasonable assurance with respect to the accuracy of consolidated financial statement preparation and presentation.

Under the supervision and with participation of our management, including the Chief Executive Officer and Chief Financial Officer, we assessed the effectiveness of Sypris Solutions, Inc.’s internal control over financial reporting as of December 31, 2019. In making our assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control – Integrated Framework (2013). Based on our assessment, we concluded that as of December 31, 2019, Sypris’ internal control over financial reporting is effective based on these criteria.

This annual report does not include an attestation report of the Company’s 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 temporary rules of the Securities and Exchange Commission that permit the Company (non-accelerated filer) to provide only management’s report in this annual report.

**Item 9B. Other Information**

None.

## PART III

### Item 10. Directors, Executive Officers and Corporate Governance

The information required herein is incorporated by reference from sections of the Company’s Proxy Statement titled “Section 16(a) Beneficial Ownership Reporting Compliance,” “Governance of the Company – Committees of the Board of Directors,” “Governance of the Company – Audit and Finance Committee,” “Proposal One, Election of Directors,” and “Executive Officers,” which Proxy Statement will be filed with the Securities and Exchange Commission pursuant to instruction G(3) of the General Instructions to Form 10-K.

The Company has adopted a Code of Conduct that applies to all of its directors, officers (including its chief executive officer, chief financial officer, chief accounting officer and any person performing similar functions) and employees. The Company has made the Code of Conduct, and will make any amendments and waivers thereto, available on its website at [www.sypris.com](http://www.sypris.com).

### Item 11. Executive Compensation

The information required herein is incorporated by reference from sections of the Company’s Proxy Statement titled “2019 Director Compensation,” “Governance of the Company,” “Summary Compensation Table,” and “Outstanding Equity Awards at Fiscal Year-End 2019,” which Proxy Statement will be filed with the Securities and Exchange Commission pursuant to instruction G(3) of the General Instructions to Form 10-K.

### Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required herein is incorporated by reference from the section of the Company’s Proxy Statement titled “Stock Ownership of Certain Beneficial Owners and Management,” which Proxy Statement will be filed with the Securities and Exchange Commission pursuant to instruction G(3) of the General Instructions to Form 10-K.

### Equity Compensation Plan Information

The following table provides information as of December 31, 2019 with respect to shares of Sypris common stock that may be issued under our equity compensation plans.

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 Under Equity Compensation Plans (Excluding Securities Reflected in Column (a)) (c)
Equity Compensation Plans Approved by Stockholders .....	2,567,750 (1)	\$ 1.26	1,153,271 (2)
Equity Compensation Plans Not Approved by Stockholders .....	—	—	—
Total .....	2,567,750	\$ 1.26	1,153,271

(1) Consists of (a) 220,000 outstanding options under the 2010 Omnibus Plan, which plan expired on May 11, 2015 and (b) 2,347,750 under the 2015 Omnibus Plan.

(2) Shares remaining available for issuance under the 2015 Omnibus Plan.

**Item 13. Certain Relationships and Related Transactions, and Director Independence**

The information required herein is incorporated by reference from the sections of the Company's Proxy Statement titled "Governance of the Company – Transactions with Related Persons" and "Governance of the Company – Independence," which Proxy Statement will be filed with the Securities and Exchange Commission pursuant to instruction G(3) of the General Instructions to Form 10-K.

**Item 14. Principal Accounting Fees and Services**

The information required herein is incorporated by reference from the section of the Company's Proxy Statement titled "Relationship with Independent Public Accountants," which Proxy Statement will be filed with the Securities and Exchange Commission pursuant to instruction G(3) of the General Instructions to Form 10-K.

## PART IV

### Item 15. Exhibits and Financial Statement Schedules

(a) The following documents are filed as part of this Annual Report on Form 10-K:

1. Financial Statements

The financial statements as set forth under Item 8 of this Annual Report on Form 10-K are included.

2. Exhibits

<u>Exhibit Number</u>	<u>Description</u>
3.1	Certificate of Incorporation of the Company (incorporated by reference to Exhibit 3.1 to the Company's Form 10-Q for the quarterly period ended June 30, 2004 filed on August 3, 2004 (Commission File No. 000-24020)).
3.2	Amended and Restated Bylaws of the Company (incorporated by reference to Exhibit 3.1 to the Company's Form 8-K filed October 31, 2011 (Commission File No. 000-24020)).
4.1	Specimen common stock certificate (incorporated by reference to Exhibit 4.1 to the Company's Form 10-K for the fiscal year ended December 31, 1998 filed on March 5, 1999 (Commission File No. 000-24020)).
4.2	Description of the Company's Securities Registered under Section 12 of the Securities Exchange Act of 1934.
10.1	Promissory Note between Gill Family Capital Management, Inc., Sypris Solutions, Inc., Sypris Technologies, Inc., Sypris Electronics, LLC, Sypris Data Systems, Inc., Sypris Technologies Marion, LLC, Sypris Technologies Kenton, Inc., Sypris Technologies Mexican Holdings, LLC, Sypris Technologies Northern, Inc., Sypris Technologies Southern, Inc. and Sypris Technologies International, Inc. dated as of March 12, 2015 (incorporated by reference to Exhibit 10.2 to the Company's Form 10-K filed on March 31, 2015 (Commission File No. 000-24020)).
10.1.1	Amended Promissory Note between Gill Family Capital Management, Inc., Sypris Solutions, Inc., Sypris Technologies, Inc., Sypris Electronics, LLC, Sypris Data Systems, Inc., Sypris Technologies Marion, LLC, Sypris Technologies Kenton, Inc., Sypris Technologies Mexican Holdings, LLC, Sypris Technologies Northern, Inc., Sypris Technologies Southern, Inc. and Sypris Technologies International, Inc. dated as of June 11, 2015 (incorporated by reference to Exhibit 10.1 to the Company's Form 10-Q filed on August 18, 2015 (Commission File No. 000-24020)).
10.1.2	Amended and Restated Promissory Note between Gill Family Capital Management, Inc., Sypris Solutions, Inc., Sypris Technologies, Inc., Sypris Electronics, LLC, Sypris Data Systems, Inc., Sypris Technologies Marion, LLC, Sypris Technologies Kenton, Inc., Sypris Technologies Mexican Holdings, LLC, Sypris Technologies Northern, Inc., Sypris Technologies Southern, Inc. and Sypris Technologies International, Inc. dated as of October 30, 2015 (incorporated by reference to Exhibit 10.2.2 to the Company's Form 10-K filed on March 30, 2016 (Commission File No. 000-24020)).
10.1.3	Amended and Restated Promissory Note in favor of Gill Family Capital Management, Inc. dated as of February 25, 2016 (incorporated by reference to Exhibit 10.3 to the Company's Form 10-Q filed on May 18, 2016 (Commission File No. 000-24020)).
10.1.4	Amended Promissory Note between Gill Family Capital Management, Inc., Sypris Solutions, Inc., Sypris Technologies, Inc., Sypris Electronics, LLC, Sypris Data Systems, Inc., Sypris Technologies Marion, LLC, Sypris Technologies Kenton, Inc., Sypris Technologies Mexican Holdings, LLC, Sypris Technologies Northern, Inc., Sypris Technologies Southern, Inc. and Sypris Technologies International, Inc. dated as of September 30, 2016 (incorporated by reference to Exhibit 10.2 to the Company's Form 10-Q filed on November 16, 2016 (Commission File No. 000-24020)).

<b><u>Number</u></b>	<b><u>Exhibit Description</u></b>
10.1.5	Amended and Restated Promissory Note between Gill Family Capital Management, Inc., Sypris Solutions, Inc., Sypris Technologies, Inc., Sypris Electronics, LLC, Sypris Data Systems, Inc., Sypris Technologies Marion, LLC, Sypris Technologies Kenton, Inc., Sypris Technologies Mexican Holdings, LLC, Sypris Technologies Northern, Inc., Sypris Technologies Southern, Inc. and Sypris Technologies International, Inc. dated as of November 10, 2017 (incorporated by reference to Exhibit 10.1.5 to the Company's Form 10-K filed on March, 20, 2018 (Commission File No. 000-24020)).
10.1.6	Security Agreement between Sypris Solutions, Inc., Sypris Technologies, Inc., Sypris Electronics, LLC, Sypris Data Systems, Inc., Sypris Technologies Marion, LLC, Sypris Technologies Kenton, Inc., Sypris Technologies Mexican Holdings, LLC, Sypris Technologies Northern, Inc., Sypris Technologies Southern, Inc. and Sypris Technologies International, Inc. and Gill Family Capital Management, Inc., dated as of March 12, 2015 (incorporated by reference to Exhibit 10.2.1 to the Company's Form 10-K filed on March, 31, 2015 (Commission File No. 000-24020)).
10.2	Asset Purchase Agreement between Analog Devices, Inc. and Sypris Electronics, LLC dated as of August 16, 2016 (incorporated by reference to Exhibit 10.1 to the Company's Form 10-Q filed on November 16, 2016 (Commission File No. 000-24020)).
10.3	Lease agreement between Promotora y Desarrolladora Pulso Inmobiliario, S.C. and Sypris Technologies Mexico, S. de R.L. de C.V dated January 29, 2016 (incorporated by reference to Exhibit 10.4 to the Company's Form 10-Q filed on May 18, 2016 (Commission File No. 000-24020)).
10.4	Lease between Sypris Electronics, LLC and University Business Center I, LLC dated May 3, 2016 regarding 10421 University Center Drive, Tampa, FL property. (incorporated by reference to Exhibit 10.1 to the Company's Form 10-Q filed on August 17, 2016 (Commission File No. 000-24020)).
10.5*	Sypris Solutions, Inc., Directors Compensation Program adopted on September 1, 1995 Amended and Restated on January 21, 2016 (incorporated by reference to Exhibit 10.9 to the Company's Form 10-K filed on March 30, 2016 (Commission File No. 000-24020)).
10.6*	Form of Discretionary Director Restricted Stock Award Agreement (incorporated by reference to Exhibit 10.10 to the Company's Form 10-K filed on March 30, 2016 (Commission File No. 000-24020)).
10.7*	Form of Four Year Discretionary Director Restricted Stock Award Agreement (incorporated by reference to Exhibit 10.5 to the Company's Form 10-Q filed on November 16, 2016 (Commission File No. 000-24020)).
10.8*	2010 Sypris Omnibus Plan effective as of May 11, 2010 (incorporated by reference to Exhibit 10.1 to the Company's Registration Statement on Form S-8 filed on May 19, 2010 (Commission File No. 333-166951)).
10.9*	2015 Sypris Omnibus Plan effective as of May 5, 2015 (incorporated by reference to Exhibit 10.1 to the Company's Registration Statement on Form S-8 filed on May 19, 2015 (Commission File No. 333-204299)).
10.10*	Form of Three Year Restricted Stock Award Agreement (incorporated by reference to Exhibit 10.15 to the Company's Form 10-K filed on March 30, 2016 (Commission File No. 000-24020)).
10.11*	Form of Four Year Non-Qualified Stock Option Award Agreement (incorporated by reference to Exhibit 10.16 to the Company's Form 10-K filed on March 30, 2016 (Commission File No. 000-24020)).
10.12*	Form of Five Year Non-Qualified Stock Option Award Agreement (incorporated by reference to Exhibit 10.17 to the Company's Form 10-K filed on March 30, 2016 (Commission File No. 000-24020)).
10.13*	Form of Four Year Restricted Stock Award Agreement (incorporated by reference to Exhibit 10.6 to the Company's Form 10-Q filed on November 16, 2016 (Commission File No. 000-24020)).
10.14*	Form of Executive Long-Term Incentive Award Agreement for Grants of Restricted Stock to Executive Officers (incorporated by reference to Exhibit 10.3 to the Company's Form 10-Q filed on November 16, 2016 (Commission File No. 000-24020)).

<b><u>Exhibit Number</u></b>	<b><u>Description</u></b>
10.15*	Form of Executive Long-Term Incentive Award Agreement for Grants of Non-Qualified Stock Options to Executive Officers (incorporated by reference to Exhibit 10.4 to the Company's Form 10-Q filed on November 16, 2016 (Commission File No. 000-24020)).
10.16*	Sypris Solutions, Inc., Directors Compensation Program adopted on September 1, 1995, Amended and Restated on March 14, 2017 (incorporated by reference to Exhibit 10.26 to the Company's Form 10-K filed on March 28, 2017 (Commission File No. 000-24020)).
10.17*	Form of Five Year Non-Qualified Stock Option Award Agreement (incorporated by reference to Exhibit 10.1 to the Company's Form 10-Q filed on May 15, 2018 (Commission File No. 000-24020)).
21	Subsidiaries of the Company
23	Consent of Crowe LLP
31.1	CEO certification pursuant to Section 302 of Sarbanes - Oxley Act of 2002.
31.2	CFO certification pursuant to Section 302 of Sarbanes - Oxley Act of 2002.
32	CEO and CFO certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes - Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
* Management contract or compensatory plan or arrangement.	

**Item 16. Form 10-K Summary**

None.





