INNOVATIVE SOLUTIONS & SUPPORT INC
Form 10-Q
August 12, 2016
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2016

OR

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

[For the transition period from to]

Commission File No. 000-31157

INNOVATIVE SOLUTIONS AND SUPPORT, INC.

(Exact name of registrant as specified in its charter)

PENNSYLVANIA	**23-2507402**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
720 Pennsylvania Drive, Exton, Pennsylvania	**19341**
(Address of Principal Executive Offices)	(Zip Code)

(610) 646-9800

(Registrant s Telephone Number, Including Area Code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted 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 and post such files). Yes x No o

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 and smaller reporting company in Rule 12b-2 of the Exchange Act.

o Large accelerated filer	o Accelerated filer
o Non-accelerated filer (Do not check if a smaller reporting company)	x Smaller reporting company

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

As of July 29, 2016, there were 16,908,849 shares of the Registrant s Common Stock, with par value of $.001 per share, outstanding.

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PART I FINANCIAL INFORMATION

Item 1- Financial Statements

INNOVATIVE SOLUTIONS AND SUPPORT, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

	June 30, 2016 (unaudited)	September 30, 2015
ASSETS		
Current assets		
Cash and cash equivalents	$ 17,530,210	$ 16,282,039
Accounts receivable	5,838,818	2,394,695
Unbilled receivables, net	1,611,357	3,920,209
Inventories	4,008,114	4,597,316
Deferred income taxes	741,109	933,499
Prepaid expenses and other current assets	1,136,268	1,221,717
Total current assets	30,865,876	29,349,475
Property and equipment, net	7,014,638	7,095,330
Other assets	156,948	168,948
Total assets	$ 38,037,462	$ 36,613,753
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities		
Accounts payable	$ 1,849,274	$ 1,435,981
Accrued expenses	2,295,897	2,568,531
Deferred revenue	299,052	756,745
Total current liabilities	4,444,223	4,761,257
Non-current deferred income taxes	576,629	507,184
Other liabilities	2,930	2,826
Total liabilities	5,023,782	5,271,267
Commitments and contingencies (See Note 6)		
Shareholders equity		
Preferred stock, 10,000,000 shares authorized, $.001 par value, of which 200,000 shares are authorized as Class A Convertible stock. No shares issued and outstanding at June 30, 2016 and September 30, 2015		

Common stock, $.001 par value: 75,000,000 shares authorized, 18,812,465 and 18,756, 089 issued at June 30, 2016 and September 30, 2015, respectively		18,813		18,756
Additional paid-in capital		51,400,058		51,148,722
Retained earnings		2,408,440		818,768
Treasury stock, at cost, 1,903,616 and 1,846,451 shares at June 30, 2016 and September 30, 2015, repectively		(20,813,631)		(20,643,760)
Total shareholders equity		33,013,680		31,342,486
Total liabilities and shareholders equity	$	38,037,462	$	36,613,753

The accompanying notes are an integral part of these statements.

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INNOVATIVE SOLUTIONS AND SUPPORT, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited)

	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Nine Months Ended June 30, 2016	Nine Months Ended June 30, 2015
Net sales:				
Product	$ 6,376,042	$ 4,114,837	$ 20,771,687	$ 12,152,290
Engineering development contracts	128,550	804,852	977,465	4,777,705
Total net sales	6,504,592	4,919,689	21,749,152	16,929,995
Cost of sales:				
Product	2,490,681	2,300,470	8,461,419	6,918,457
Engineering development contracts	130,335	687,574	185,000	3,734,692
Total cost of sales	2,621,016	2,988,044	8,646,419	10,653,149
Gross profit	3,883,576	1,931,645	13,102,733	6,276,846
Operating expenses:				
Research and development	1,405,158	799,340	3,674,374	2,101,812
Selling, general and administrative	2,246,074	1,397,165	7,531,633	4,911,546
Total operating expenses	3,651,232	2,196,505	11,206,007	7,013,358
Operating income (loss)	232,344	(264,860)	1,896,726	(736,512)
Interest income	9,092	6,372	24,458	18,269
Other income	12,457	11,173	71,490	31,405
Income (loss) before income taxes	253,893	(247,315)	1,992,674	(686,838)
Income tax expense	27,096	3,284,658	403,002	2,615,484
Net income (loss)	$ 226,797	$ (3,531,973)	$ 1,589,672	$ (3,302,322)
Net income (loss) per common share:				
Basic	$ 0.01	$ (0.21)	$ 0.09	$ (0.20)
Diluted	$ 0.01	$ (0.21)	$ 0.09	$ (0.20)
Weighted average shares outstanding:				
Basic	16,941,707	16,910,475	16,925,688	16,930,522
Diluted	17,059,546	16,910,475	17,027,216	16,930,522

The accompanying notes are an integral part of these statements.

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INNOVATIVE SOLUTIONS AND SUPPORT, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

	For the Nine Months Ended June 30, 2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	$ 1,589,672	$ (3,302,322)
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	355,930	430,525
Share-based compensation expense:		
Stock options	68,172	259,582
Stock awards	183,222	149,952
Tax adjustment from share-based compensation		(54,055)
Recovery of loss on unbilled receivables		(62,159)
(Gain) loss on disposal of property and equipment	(563)	(56,824)
Excess and obsolete inventory cost		246,663
Deferred income taxes	261,835	2,837,888
(Increase) decrease in:		
Accounts receivable	(3,444,668)	516,769
Unbilled receivables, net	2,308,852	2,622,729
Inventories	589,202	1,085,418
Prepaid expenses and other current assets	85,449	97,287
Other non-current assets		(75,300)
Increase (decrease) in:		
Accounts payable	413,293	(2,043,154)
Accrued expenses	(272,634)	(1,593,150)
Income taxes payable/receivable	104	(359,491)
Deferred revenue	(457,694)	213,218
Net cash provided by operating activities	1,680,172	913,576
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(263,238)	(171,474)
Proceeds from the sale of property and equipment	1,108	57,000
Net cash (used in) investing activities	(262,130)	(114,474)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Purchase of Company s stock	(169,871)	(254,170)
Net cash (used in) financing activities	(169,871)	(254,170)
Net increase in cash and cash equivalents	1,248,171	544,932
Cash and cash equivalents, beginning of year	16,282,039	15,214,584
Cash and cash equivalents, end of period	$ 17,530,210	$ 15,759,516
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid for income tax	$ 135,000	$ 191,000

The accompanying notes are an integral part of these statements.

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INNOVATIVE SOLUTIONS AND SUPPORT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

1. Summary of Significant Accounting Policies

Description of the Company

Innovative Solutions and Support, Inc. (the Company or IS&S) was incorporated in Pennsylvania on February 12, 1988. The Company operates in one business segment as a systems integrator that designs, manufactures, sells, and services air data equipment, engine display systems, standby equipment, primary flight guidance, and cockpit display systems for retrofit applications and original equipment manufacturers (OEMs). The Company supplies integrated Flight Management Systems (FMS), Flat Panel Display Systems (FPDS), Integrated Standby Units (ISU) and advanced Global Positioning System (GPS) receivers that enable reduced carbon footprint navigation.

The Company has continued to position itself as a system integrator, which capability provides the Company with the potential to generate more substantive orders over a broader product base. The strategy, as both a manufacturer and integrator, is designed to leverage the latest technologies developed for the computer and telecommunications industries into advanced and cost-effective solutions for the general aviation, commercial air transport, United States Department of Defense (DoD)/governmental, and foreign military markets. This approach, combined with the Company s industry experience, is designed to enable IS&S to develop high-quality products and systems, to reduce product time to market, and to achieve cost advantages over products offered by its competitors. Customers include commercial air transport carriers and corporate/general aviation companies, the DoD and its commercial contractors, aircraft operators, aircraft modification centers, foreign militaries, and various OEMs.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements are presented pursuant to the rules and regulations of the United States Securities and Exchange Commission (the SEC) in accordance with the disclosure requirements for the quarterly report on Form 10-Q and, therefore, do not include all of the information and footnotes required by generally accepted accounting principles in the United States (GAAP) for complete annual financial statements. In the opinion of Company management, the unaudited condensed consolidated financial statements reflect all adjustments (consisting of normal recurring adjustments) necessary to state fairly the results for the interim periods presented. The condensed consolidated balance sheet as of September 30, 2015 is derived from the audited financial statements of the Company. Operating results for the three and nine months ended June 30, 2016 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2016. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes of the Company included in the Company s Annual Report on Form 10-K for the fiscal year ended September 30, 2015.

The Company s condensed consolidated financial statements include the accounts of its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

Preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities, as of the date of the financial statements and the reported amounts of net sales and expenses during the reporting period. Estimates are used in accounting for, among other items, long term contracts, allowance for doubtful accounts, inventory obsolescence, product warranty cost liabilities, income taxes, engineering and material costs on Engineering Development Contracts (EDC) programs, percentage-of-completion on EDC, recoverability of long-lived assets, stock-based compensation expense self-insurance reserves, and contingencies. Actual results could differ materially from those estimates.

Cash and Cash Equivalents

Highly liquid investments, purchased with an original maturity of three months or less, are classified as cash equivalents. Cash equivalents at June 30, 2016 and September 30, 2015 consist of funds invested in money market funds with financial institutions.

Property and Equipment

Property and equipment are stated at cost. Depreciation is provided using an accelerated method over the estimated useful lives of the assets (the lesser of three to seven years or over the related lease term), except for the manufacturing facility and the corporate airplane. The building is being depreciated on a straight line basis over 39 years. Major additions and improvements are capitalized. Maintenance and repairs that do not improve or extend the life of assets are charged to expense as incurred. The airplane was depreciated on a straight-line basis over its estimated useful life of ten years; however, because the airplane had been depreciated previously to its estimated salvage value, no depreciation expense was recorded for this asset during the nine months ended June 30, 2016 or 2015, respectively.

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Fair Value of Financial Instruments

The net carrying amounts of cash and cash equivalents, accounts receivable, and accounts payable approximate their fair value because of the short-term nature of these instruments. For financial assets and liabilities measured at fair value on a recurring basis, fair value is the price the Company would receive to sell an asset or pay to transfer a liability in an orderly transaction with a market participant at the measurement date. A three-level fair value hierarchy prioritizes the inputs used to measure fair value as follows:

Level 1 Unadjusted quoted prices that are available in active markets for the identical assets or liabilities at the measurement date.

Level 2 Other observable inputs available at the measurement date, other than quoted prices included in Level 1, either directly or indirectly, including:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets in non-active markets;
- Inputs other than quoted prices that are observable for the asset or liability; and
- Inputs that are derived principally from or corroborated by other observable market data.

Level 3 Unobservable inputs that cannot be corroborated by observable market data and reflect the use of significant management judgment. These values are generally determined using pricing models for which the assumptions utilize management s estimates of market participant assumptions.

The following table sets forth by level within the fair value hierarchy the Company s financial assets and liabilities that were accounted for at fair value on a recurring basis as of June 30, 2016 and September 30, 2015, according to the valuation techniques the Company used to determine their fair values.

	Fair Value Measurement on June 30, 2016		
	Quoted Price in Active Markets for Identical Assets (Level 1)	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Assets			
Cash and cash equivalents:			
Money market funds	$ 16,414,873	$	$

Fair Value Measurement on September 30, 2015

	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets			
Cash and cash equivalents:			
Money market funds	$ 14,410,806	$	$

Long-Lived Assets

The Company assesses the impairment of long-lived assets in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 360-10, *Property, Plant and Equipment* (ASC Topic 360-10). This statement requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. In addition, long-lived assets to be disposed of must be reported at the lower of the carrying amount or fair value less cost to sell. The Company considers historical performance and future estimated results in its evaluation of potential impairment and compares the carrying amount of the asset to estimated future cash flows expected from use of the asset. If the carrying amount of the asset exceeds the estimated expected undiscounted future cash flows, the Company measures the amount of the impairment by comparing the carrying amount of the asset to its fair value. The estimation of fair value is measured by discounting expected future cash flows. No impairment charges were recorded during the nine months ended June 30, 2016 or 2015.

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Revenue Recognition

The Company enters into sales arrangements with customers that, in general, provide for the Company to design, develop, manufacture, and deliver large FPDS, flight information computers and advanced monitoring systems that measure and display critical flight information, including data relative to aircraft separation, airspeed, altitude, and engine and fuel data measurements. The Company s sales arrangements include multiple deliverables as defined in FASB ASC Topic 605-25 Multiple-Element Arrangements (ASC Topic 605-25), which typically include design and engineering services, and the production and delivery of the flat panel display and related components. The Company includes any design and engineering services elements in EDC sales and any functional upgrade and product elements in product sales in the accompanying consolidated statements of operations.

To the extent that an arrangement contains software elements that are essential to the functionality of tangible products sold in the arrangement, the Company recognizes revenue for the deliverables in accordance with the guidance included in FASB Accounting Standards Update 2009-14, *Revenue Arrangements That Include Software Elements* (ASU 2009-14), FASB Accounting Standards Update 2009-13, *Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force* (ASU 2009-13), and FASB ASC Topic 605, *Revenue Recognition* (ASC Topic 605).

To the extent that an arrangement contains software components, which may include functional upgrades, that the Company sells on a standalone basis and which it has deemed outside the scope of the exception defined by ASU 2009-14, the Company recognizes software revenue in accordance with ASC Topic 985, *Software* (ASC Topic 985).

Multiple Element Arrangements -

The Company identifies all goods and/or services that are to be delivered separately under such a sales arrangement and allocates sales to each deliverable (if more than one) based on that deliverable s fair value. The Company then considers the appropriate recognition method for each deliverable. The Company s multiple element arrangements can include defined design and development activities, functional upgrades, and product sales.

The Company utilizes the selling price hierarchy that has been established by ASU 2009-13, which requires that the selling price for each deliverable be based on vendor-specific objective evidence if available, third-party evidence if vendor-specific objective evidence is not available, or estimated selling price if neither vendor-specific objective evidence nor third-party evidence is available. To the extent that an arrangement includes a deliverable for which estimated selling price is used, the Company determines the best estimate of selling price by applying the same pricing policies and methodologies that would be used to determine the price to sell the deliverable on a standalone basis.

To the extent that an arrangement contains defined design and EDC activities as identified deliverables and products (resulting in a multiple element arrangement), the Company recognizes as EDC sales amounts earned during the design and development phase of the contract following the guidance included in FASB ASC Topic 605-35, *Construction-Type and Production-Type Contracts (ASC Topic 605-35)* under the percentage-of-completion method. To the extent that multiple element arrangements include product sales, sales are generally recognized once revenue recognition criteria for the product deliverables have been met based on the provisions of ASC Topic 605. The Company includes any design and engineering services elements in EDC sales, and any functional upgrade and product elements in product

sales on the accompanying consolidated statements of operations.

Single Element Arrangements

Products

To the extent that a single element arrangement provides for product sales and repairs, the Company recognizes sales when revenue recognition criteria for the product deliverables have been met based on the provisions of ASC Topic 605. In addition, the Company receives orders for equipment and parts. Generally, revenue from the sale of such products is recognized upon shipment to the customer.

The Company offers its customers extended warranties for additional fees. These warranty sales are recorded as deferred revenue and recognized as sales on a straight-line basis over the warranty period.

Engineering Development Contracts

The Company may enter into contracts to perform specified design and EDC services related to its products. The Company recognizes revenue from these arrangements as EDC sales, following the guidance included in ASC Topic 605-35, and considers the nature of these contracts (including term, size of contract, and level of effort) when determining the appropriate accounting treatment for a particular contract. Certain of these contracts are accounted for under the percentage-of-completion method of accounting when

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the Company determines that progress toward completion is reasonable and reliably estimable, and the contract is long-term in nature. The Company uses the completed contract method for all other contracts because these contracts are short-term in nature and meet the criteria set forth in ASC Topic 605-35. Sales and profit margins under the percentage-of-completion method are recorded based on the ratio of actual costs incurred to total estimated costs expected to be incurred related to the contract under the cost-to-cost method (for development effort).

The percentage-of-completion method of accounting requires the Company to estimate the profit margin for each individual contract, and to apply that profit margin on a uniform basis as sales are recorded under the contract. The estimation of profit margin requires the Company to make projections of the total sales to be generated and the total costs that will be incurred under each contract. The projections require the Company to make numerous assumptions and estimates relating to items, such as the complexity of design and related development costs, performance of subcontractors, availability and cost of materials, engineering productivity and cost, overhead, and capital costs. Contracts sometimes include purchase options for additional quantities and customer change orders for additional or revised product functionality. Sales and costs related to profitable purchase options are included in the Company s estimates only when the options are exercised, while sales and costs related to unprofitable purchase options are included in the Company s estimates when exercise is determined to be probable. Sales related to change orders are included in profit estimates only if they can be reliably estimated and collectability is reasonably assured. Purchase options and change orders are accounted for, either as an integral part of the original contract or separately, depending upon the nature and value of the item. Anticipated losses on contracts are recognized in full in the period in which losses become probable and estimable.

The Company reviews estimates of profit margins for contracts on a quarterly basis. The percentage-of-completion method results in the profit margin being recorded evenly as revenue is recognized under the contract. Changes in these underlying estimates because of revisions in revenue and cost estimates or to the exercise of contract options may result in profit margins being recognized unevenly over a contract as such changes are accounted for on a cumulative basis in the period estimates are revised. Significant changes in estimates related to accounting for long-term contracts may have a material effect on the Company s results of operations in the period in which the revised estimate is made. Cumulative catch-up adjustments resulting from changes in estimates are disclosed in the notes to the consolidated financial statements of the Company.

Customer Service Revenue

The Company enters into sales arrangements with customers for the repair or upgrade of its various products that are not under warranty. The Company s customer service revenue and cost of sales for the three and nine months ended June 30, 2016 and 2015, respectively are as follows:

	For the Three Months Ended June 30,		For the Nine Months Ended June 30,	
	2016	**2015**	**2016**	**2015**
Customer Service Sales	$ 1,023,302	$ 772,385	$ 2,702,956	$ 1,928,966
Customer Service Cost of Sales	357,390	266,789	935,995	823,190
Gross Profit	$ 665,912	$ 505,596	$ 1,766,961	$ 1,105,776

Income Taxes

Income taxes are recorded in accordance with FASB ASC Topic 740, Income Taxes (ASC Topic 740), which utilizes a balance sheet approach to provide for income taxes. Under this method, the Company recognizes deferred tax assets and liabilities for temporary differences between

the financial reporting basis and the tax basis of the Company s assets, liabilities, and expected benefits of utilizing net operating losses (NOL) and tax credit carry-forwards. The impact on deferred taxes of changes in tax rates and laws, if any, are applied to the years during which temporary differences are expected to be settled and are reflected in the consolidated financial statements in the period of enactment. At the end of each interim reporting period, the Company prepares an estimate of the annual effective income tax rate and applies that annual effective income tax rate to ordinary year-to-date pre-tax income or loss for the interim period. Specific tax items discrete to a particular quarter are recorded in income tax expense for that quarter. The estimated annual effective tax rate used in providing for income taxes on a year-to-date basis may change in subsequent interim periods.

Deferred tax assets are reduced by valuation allowances if, based on the consideration of all available evidence, it is more likely than not that some portion of the deferred tax asset will not be realized. Significant weight is given to evidence that can be objectively verified, and significant management judgment is required in determining any valuation allowances recorded against net deferred tax assets. The Company evaluates deferred income taxes on a quarterly basis to determine if valuation allowances are required by considering available evidence. Deferred tax assets are recognized when expected future taxable income is sufficient to allow the

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related tax benefits to reduce taxes that would otherwise be payable. The sources of taxable income that may be available to realize the benefit of deferred tax assets are future reversals of existing taxable temporary differences, future taxable income exclusive of reversing temporary differences and credit carry-forwards, taxable income in carry-back years, and tax planning strategies.

In the period ended June 30, 2015, a valuation allowance was recorded on a majority of the Company s federal and state deferred tax assets, net of liabilities, due to uncertainty with respect to the Company s ability to generate sufficient future taxable income to realize such deferred tax assets. The remaining amount of the Company s recognized deferred tax assets were related to tax planning strategies and the ability to carry-back federal tax losses to claim a tax refund.

For the nine months ended June 30, 2016, the valuation allowance was reduced due to the current year profitability of the Company which represents an additional source of taxable income to realize certain federal and state deferred tax assets. However, the Company will continue to maintain a valuation allowance until the Company generates a sufficient level of profitability to warrant a conclusion that it is no longer more likely than not that the entirety of these net federal and state deferred tax assets will not be realized in future periods. The Company will also continue to assess all available evidence during future periods to evaluate any changes to the realization thereof.

The accounting for uncertainty in income taxes requires a more likely than not threshold for financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return. The Company records a liability for the difference between the (i) benefit recognized and measured for financial statement purposes and (ii) the tax position taken or expected to be taken on the Company s tax return. To the extent that the Company s assessment of such tax positions changes, the change in estimate is recorded in the period in which the determination is made. The Company has elected to record any interest or penalties associated with uncertain tax positions as income tax expense.

The Company files a consolidated United States federal income tax return. The Company prepares and files tax returns based on the interpretation of tax laws and regulations, and records estimates based on these judgments and interpretations. In the normal course of business, the tax returns are subject to examination by various taxing authorities. Such examinations may result in future tax and interest assessments by these taxing authorities, and the Company records a liability when it is probable that there will be an assessment. The Company adjusts the estimates periodically as the result of ongoing examinations by and settlements with the various taxing authorities and changes in tax laws, regulations and precedent. The consolidated tax provision of any given year includes adjustments to prior years income tax accruals that are considered appropriate and any related estimated interest. Management believes that adequate accruals have been made for income taxes. Differences between estimated and actual amounts determined upon ultimate resolution, individually or in the aggregate, are not expected to have a material adverse effect on the Company s consolidated financial position but could possibly be material to its consolidated results of operations or cash flow of any one period.

Engineering Development

The Company invests a large percentage of its sales in engineering development, both research and development (R&D) and EDC. At June 30, 2016, approximately 38% of the Company s employees were engaged in various engineering development projects. Total engineering development expense is comprised of both design and EDC charges related to specific customer contracts and R&D. EDC expense consists primarily of payroll-related expenses of employees engaged in EDC projects, engineering related product materials and equipment, and subcontracting costs. R&D charges incurred for product design, product enhancements and future product development are expensed as

incurred. EDC and design charges related to specific customer arrangements are charged to cost of sales-EDC based on the method of contract accounting (either percentage-of-completion or completed-contract) applicable to such contracts.

Treasury Stock

Treasury stock is recorded at acquisition cost. Gains and losses on disposition are recorded as increases or decreases to additional paid-in capital with losses in excess of previously recorded gains charged directly to retained earnings. When treasury shares are retired and returned to authorized but unissued status, the carrying value in excess of par is allocated to additional paid-in capital and retained earnings on a pro rata basis.

Comprehensive Income

Pursuant to FASB ASC Topic 220, *Comprehensive Income* (ASC Topic 220), the Company is required to classify items of other comprehensive income by their nature in the balance sheet and to display the accumulated balance of other comprehensive income separately from retained earnings and additional paid-in capital in the equity section of its condensed consolidated balance sheets. For the three and nine months ended June 30, 2016 and 2015, respectively, comprehensive income consisted of net income only. There were no items of other comprehensive income or accumulated other comprehensive income balances in the equity accounts for any of the periods presented.

Share-Based Compensation

The Company accounts for share-based compensation under FASB ASC Topic 505-50, *Equity-Based Payments to Non-Employees*

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(ASC Topic 505-50), and FASB ASC Topic 718, *Stock Compensation* (ASC Topic 718), which require the Company to measure the cost of employee or non-employee director services received in exchange for an award of equity instruments based on the grant-date fair value of the award using an option pricing model. That cost is recognized over the period during which an employee or non-employee director is required to provide service in exchange for the award.

Warranty

The Company offers warranties of various lengths; however the standard warranty is twenty-four months. At the time of shipment, the Company establishes a reserve for estimated costs of warranties based on its best estimate of the amounts necessary to settle future and existing claims using historical data on products sold as of the balance sheet date. The length of the warranty period, the product s failure rates, and the customer s usage affect warranty cost. If actual warranty costs are higher than the Company s estimated amounts, future results of operations could be affected adversely. Warranty cost is recorded as cost of sales, and the reserve balance is recorded as an accrued expense. Although the Company maintains product quality programs and processes, its warranty obligations are affected by product failure rates and the related corrective costs. If actual product failure rates and/or corrective costs differ from the estimates, the Company revises the estimated warranty liability accordingly.

Self-Insurance Reserves

Beginning January 1, 2014, the Company began self-insuring a significant portion of its employee medical insurance. The Company maintains a stop-loss insurance policy that limits its losses both on a per employee basis and an aggregate basis. Liabilities associated with the risks that are retained by the Company are estimated based upon actuarial assumptions including historical claim experience and demographic factors. The Company has estimated the total medical claims incurred but not reported and the Company believes that it has adequate reserves for these claims at June 30, 2016. However, the actual value of such claims could be significantly affected if future occurrences and claims differ from these assumptions. At June 30, 2016 and September 30, 2015, the estimated liability for medical claims incurred but not reported was $53,000 and $80,000, respectively. The Company has recorded the excess of funded premiums over estimated claims incurred but not reported in the amounts of $272,000 and $119,000 as a current asset in the accompanying condensed consolidated balance sheets as of June 30, 2016 and September 30, 2015, respectively.

Concentrations

Major Customers and Products

For the three months ended June 30, 2016, two customers, Sierra Nevada Corporation (Sierra Nevada) and iAccess Technologies, Inc. (iAccess), accounted for 45% and 12% of net sales, respectively. During the nine months ended June 30, 2016, three customers, Jet2.com Limited (Jet2), Sierra Nevada and DHL Aviation Services (DHL) accounted for 16%, 15% and 14% of net sales, respectively.

For the three months ended June 30, 2015, three customers, Eclipse Aerospace, Inc. (Eclipse), American Airlines, Inc. (American) and Pilatus Aircraft Limited (Pilatus), accounted for 23%, 20% and 11% of net sales, respectively. During the nine months ended June 30, 2015, three customers, Pilatus, Eclipse and the DoD accounted for 23%, 18% and 11% of net sales, respectively.

Major Suppliers

The Company buys several components from sole source suppliers. Although there are a limited number of manufacturers of particular components, the Company believes other suppliers could provide similar components on comparable terms.

For the three and nine months ended June 30, 2016, the Company had one supplier that was individually responsible for greater than 10% of the Company s total inventory related purchases.

For the three and nine months ended June 30, 2015, the Company had five and two suppliers respectively that were individually responsible for greater than 10% of the Company s total inventory related purchases.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentration of credit risk consist principally of cash balances and accounts receivable. The Company invests its excess cash where preservation of principal is the primary consideration. Cash balances are maintained with two major banks. Balances on deposit with certain money market accounts and operating accounts may exceed the Federal Deposit Insurance Corporation (FDIC) limits. The Company s customer base consists principally of companies within the aviation industry. The Company requests advance payments and/or letters of credit from customers that it considers to be credit risks.

As of June 30, 2016, the Company had allowances for doubtful accounts for unbilled receivables in the amount of $3.6 million related to the Delta contract (see Note 6, Contingencies for a description of the Delta contract). As of September 30, 2015, the Company had allowances for doubtful accounts for unbilled receivables of $1.3 million related to a certain customer contract and $3.6 million

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related to the Delta contract. In January 2016, the Company negotiated changes to its agreement with a customer whereby $1.3 million of unbilled receivables previously charged to bad debt expense in the quarter ended September 30, 2015 were cancelled. (See Unbilled Receivables below under Note 2. Supplemental Balance Sheet Disclosures).

Recent Accounting Pronouncements

In March 2016, the Financial Accounting Standards Board (FASB) issued ASU 2016-09, *Compensation - Stock Compensation - Improvements to Employee Share-Based Payment Accounting* (ASU 2016-09), which involves several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. Under the new standard, income tax benefits and deficiencies are to be recognized as income tax expense or benefit in the income statement and the tax effects of exercised or vested awards should be treated as discrete items in the reporting period in which they occur. An entity should also recognize excess tax benefits regardless of whether the benefit reduces taxes payable in the current period. Excess tax benefits should be classified along with other income tax cash flows as an operating activity. In regards to forfeitures, the entity may make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur. This ASU is effective for fiscal years beginning after December 15, 2016, including interim periods within that reporting period. Early adoption is permitted. The Company is assessing the impact the adoption of ASU 2016-09 will have on its financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases* (ASU 2016-02). The new standard establishes a right-of-use (ROU) model that requires a lessee to record an ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. The Company is assessing the impact the adoption of ASU 2016-02 will have on its financial statements.

In November 2015, the FASB issued guidance regarding Balance Sheet Classification of Deferred Taxes. Current guidance requires an entity to separate deferred income tax liabilities and assets into current and noncurrent amounts in a classified statement of financial position. However, the new guidance requires that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The guidance is effective for the Company beginning October 1, 2017. Early adoption is permitted. The Company is currently assessing the impact of this guidance on its financial statements disclosure.

In July 2015, the FASB issued guidance regarding Simplifying the Measurement of Inventory. This guidance requires entities to measure most inventory at the lower of cost and net realizable value, thereby simplifying the current guidance under which an entity must measure inventory at the lower of cost or market (market in this context is defined as one of three different measures). The guidance will not apply to inventories that are measured by using either the last-in, first-out (LIFO) method or the retail inventory method (RIM). The guidance is effective for the Company beginning October 1, 2017. Early adoption is permitted. The Company is currently assessing the impact of this guidance on its financial statements disclosure.

In August 2014, the FASB issued ASU No. 2014-15, *Presentation of Financial Statements - Going Concern (Subtopic 205-40)* (ASU 2014-15). The objective of ASU 2014-15 is to define management s responsibility to evaluate whether there is substantial doubt about an organization s ability to continue as a going concern and provide related disclosures. Currently, GAAP does not provide guidance to evaluate whether there is substantial doubt regarding an organization s ability to continue as a going concern. ASU 2014-15 provides guidance to an

organization s management, with principles and definitions to reduce diversity in the timing and content of financial statement disclosures commonly provided by organizations. ASU 2014-15 is effective for periods ending after December 15, 2016 and interim periods within annual periods beginning after December 15, 2016. Early adoption is permitted. The Company does not believe that ASG 2014-15 will have a material effect on the accompanying financial statements.

In June 2014, the FASB issued ASU No. 2014-12, *Compensation - Stock Compensation (ASC Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period* (ASU 2014-12). The amendments in ASU 2014-12 require that a performance target that affects vesting and that could be achieved after the requisite service period to be treated as a performance condition. As such, the performance target should not be reflected in estimating the grant date fair value of the award. This ASU further clarifies that compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the requisite service has already been rendered. The amendments in ASU 2014-12 are effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. Early adoption is permitted. The Company does not believe that ASG 2014-12 will have a material effect on the accompanying financial statements.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (ASC Topic 606)* (ASU 2014-09). ASU 2014-09 will supersede existing revenue recognition guidance and require revenue to be recognized when promised goods or services are transferred to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. The new standard was scheduled to be effective for reporting periods beginning after December 15, 2016,

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and early adoption is not permitted. However, on July 9, 2015, the FASB decided to delay the effective date of the new revenue standard by one year, but reporting entities may choose to adopt the standard as of the original effective date. Adoption of the new rules could affect the timing of revenue recognition for certain transactions. The guidance permits two implementation approaches, one requiring retrospective application of the new standard with restatement of prior years and one requiring retrospective application of the new standard with the cumulative effect of applying the new standard as of the date of initial application recognized and disclosure of results under old standards. The FASB has recently issued an Exposure Draft of a proposed ASU that would delay by one year the effective date of this standard. The Company is currently evaluating the impacts of adoption and the implementation approach to be used.

As new accounting pronouncements are issued, the Company will adopt those that are applicable under the circumstances.

2. Supplemental Balance Sheet Disclosures

Unbilled Receivables

Unbilled receivables principally represent sales recorded under the percentage-of-completion method of accounting that, in accordance with applicable contract terms, have not been billed to customers. Unbilled receivables, net of progress payments and an impairment of $3.6 million related to the Delta contract at June 30, 2016 were $1.6 million. Unbilled receivables, net of progress payments and an impairment of $1.3 million related to a certain customer and an impairment of $3.6 million related to the Delta contract, at September 30, 2015 were $3.9 million. The Company negotiated changes to its agreement with a customer in January 2016 whereby the $1.3 million of unbilled receivables previously charged to bad debt expense in the quarter ended September 30, 2015 were cancelled.

Significant changes in estimates related to accounting for long-term contracts under the percentage-of-completion method may have a material effect on the Company s results of operations in the period in which the revised estimates are made. Cumulative catch-up adjustments resulting from changes in estimates decreased operating income by $120,000 for the three months ended June 30, 2016 and increased operating income by $232,000 for the nine months ended June 30, 2016. These increases to operating income are primarily related to reversals of loss accruals due to the cancellation of certain product deliverables as negotiated with a certain customer in January, 2016. Cumulative catch-up adjustments resulting from changes in estimates decreased operating income by $125,000 for the three months ended June 30, 2015 and increased operating income by $595,000 for the nine months ended June 30, 2015.

Inventories

Inventories are stated at the lower of cost (first-in, first-out) or market, net of reserve for excess and obsolete inventory, and consist of the following:

	June 30, 2016	September 30, 2015

Raw materials	$	3,151,301	$	3,346,778
Work-in-process		474,767		745,311
Finished goods		382,046		505,227
	$	4,008,114	$	4,597,316

Prepaid expenses and other current assets

Prepaid expenses and other current assets consist of the following:

		June 30, 2016		September 30, 2015
Prepaid insurance	$	434,017	$	290,543
Income tax refund receivable		380,806		386,869
Other		321,445		544,305
	$	1,136,268	$	1,221,717

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Property and equipment

Property and equipment, net consists of the following:

		June 30, 2016		September 30, 2015
Land	$	1,021,245	$	1,021,245
Computer equipment		2,260,506		2,270,799
Corporate airplane		3,194,571		3,128,504
Furniture and office equipment		1,052,284		1,056,486
Manufacturing facility		5,733,313		5,733,313
Equipment		5,358,315		5,165,190
		18,620,234		18,375,537
Less: accumulated depreciation and amortization		(11,605,596)		(11,280,207)
	$	7,014,638	$	7,095,330

Depreciation related to property and equipment was approximately $117,000 and $138,000 for the three months ended June 30, 2016 and 2015, respectively. The corporate airplane is utilized primarily in support of product development and has been depreciated to its estimated salvage value.

Depreciation related to property and equipment was approximately $344,000 and $413,000 for the nine months ended June 30, 2016 and 2015, respectively.

Other assets

Other assets consist of the following:

		June 30, 2016		September 30, 2015
Intangible assets, net of accumulated amortization of $529,037 and $517,037 at June 30, 2016 and September 30, 2015	$	71,200	$	83,200
Other non-current assets		85,748		85,748
	$	156,948	$	168,948

Intangible assets consist of licensing and certification rights which are amortized over a defined number of units. No impairment charges were recorded in the nine months ended June 30, 2016 and 2015.

Total amortization expense was approximately $7,200 and $5,000 for the three months ended June 30, 2016 and 2015, respectively. Total amortization expense was approximately $12,000 and $17,000 for the nine months ended June 30, 2016 and 2015, respectively.

Accrued expenses

Accrued expenses consist of the following:

	June 30, 2016	September 30, 2015
Warranty	$ 950,432	$ 878,901
Salary, benefits and payroll taxes	451,910	537,451
Professional fees	689,453	353,012
Other, including losses on contracts	204,102	799,167
	$ 2,295,897	$ 2,568,531

Other accrued expense at June 30, 2016 and September 30, 2015 includes $0 and $0.6 million of EDC program costs, respectively.

Warranty cost and accrual information for the three and nine months ended June 30, 2016 is highlighted below:

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	Three Months Ending June 30, 2016	Nine Months Ending June 30, 2016
Warranty accrual, beginning of period	$ 996,660	$ 878,901
Accrued expense	35,890	308,200
Warranty cost	(82,118)	(236,669)
Warranty accrual, end of period	$ 950,432	$ 950,432

3. Income Taxes

The income tax expense for the three and nine months ended June 30, 2016 was $27,000 and $403,000, respectively, as compared to an income tax expense of $3.3 million and $2.6 million respectively, for the three and nine months ended June 30, 2015.

The effective tax rate for the three months ended June 30, 2016 was 10.7%. The effective tax rate for the three months ended June 30, 2016 differs from the statutory rate primarily due to a reduction in the valuation allowance of approximately $150,000 included in our current year estimated annual effective tax rate that is attributable to the anticipated profitability in the current year.

The effective tax rate for the three months ended June 30, 2015 was (1,328.1%). The effective tax rate for the three months ended June 30, 2015 differs from the statutory rate primarily because of the Company recorded a valuation allowance against the deferred tax assets of $3.3 million reflecting only those deferred tax assets that could be realized.

The effective tax rate for the nine months ended June 30, 2016 was 20.2%. The effective tax rate for the nine months ended June 30, 2016 differs from the statutory rate primarily due to a reduction in the valuation allowance of approximately $150,000 included in our current year estimated annual effective tax rate that is attributable to the anticipated profitability in the current year.

The effective tax benefit rate for the nine months ended June 30, 2015 was (380.8%). The effective tax rate for the nine months ended June 30, 2015 differs from the statutory rate primarily because of the $3.3 million valuation allowance recorded against the deferred tax assets in the three months ended June 30, 2015.

On December 18, 2015, the Protecting Americans from Tax Hikes (PATH) Act of 2015 was enacted. This legislation retroactively extended various temporary tax provisions which expired on December 31, 2014, including the permanent extension of the R&D Tax Credit. No income tax benefit was recorded in the period on the retroactive benefit for the period from January 1, 2015 to September 30, 2015 due to the uncertainty on the Company s ability to generate future taxable income.

In the period ended June 30, 2015, a valuation allowance was recorded on a majority of the Company s federal and state deferred tax assets, net of liabilities, due to the uncertainty on the Company s ability to generate sufficient future taxable income to realize such deferred tax assets. The remaining amount of the deferred tax assets recognized were attributable to tax planning strategies and the ability to carry-back federal tax losses to claim a tax refund.

For the nine months ended June 30, 2016, the valuation allowance was reduced due to the current year profitability of the Company which represented an additional source of taxable income to realize certain federal and state deferred tax assets. However the Company will continue to maintain a valuation allowance until the Company generates a sufficient level of profitability to warrant a conclusion that it no longer is more likely than not that these net federal and state deferred tax assets will not be realized in future periods.

On September 13, 2014, the U.S. Treasury Department and the IRS issued final regulations that addressed cost incurred in acquiring, producing, or improving tangible property (the tangible property regulations). The tangible property regulations were generally effective for tax years beginning on or after January 1, 2014 and required the Company to make additional tax accounting method changes as of October 1, 2014. However, the impact of these changes to the Company s consolidated financial statements was immaterial as of and for the three and nine months ended June 30, 2016 and 2015.

4. Shareholders Equity and Share-based Payments

At June 30, 2016, the Company s Amended and Restated Articles of Incorporation provides the Company authority to issue 75,000,000 shares of common stock and 10,000,000 shares of preferred stock.

Share-based compensation

The Company accounts for share-based compensation under the provisions of ASC Topic 505-50 and ASC Topic 718 by using the fair value method for expensing stock options and stock awards.

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Total share-based compensation expense was approximately $0 and $59,000 for the three months ended June 30, 2016 and 2015, respectively. The income tax effect recognized as a (charge) to additional paid-in capital related to share-based compensation arrangements was ($0) and ($7,000) for the three months ended June 30, 2016 and 2015, respectively.

Total share-based compensation expense was approximately $68,000 and $409,000 for the nine months ended June 30, 2016 and 2015, respectively. The income tax effect recognized as a (charge) to additional paid-in capital related to share-based compensation arrangements was approximately ($0) and ($54,000) for the nine months ended June 30, 2016 and 2015, respectively. Compensation expense related to share-based awards is recorded as a component of general and administrative expense.

The Company maintains three share-based compensation plans; the 1998 Stock Option Plan (the 1998 Plan), the 2003 Restricted Stock Plan (the Restricted Plan), and the 2009 Stock-Based Incentive Compensation Plan (the 2009 Plan). The Company s shareholders approved each of these plans. The 1998 Plan expired on November 13, 2008. The last awards under the Restricted Plan were made in 2010, and no further shares remain to be awarded under the Restricted Plan.

1998 Stock Option Plan

The 1998 Plan authorized the grant of incentive and nonqualified stock options to employees, officers, directors, and independent contractors and consultants. No stock options were granted to independent contractors or consultants under this Plan. There was no compensation expense associated with awards under the 1998 Plan for the nine months ended June 30, 2016 and 2015.

Incentive stock options granted under the 1998 Plan have exercise prices that must be at least equal to the fair value of the common stock on the grant date. Nonqualified stock options granted under the 1998 Plan have exercise prices that may be less than, equal to, or greater than the fair value of the common stock on the date of grant. The Company reserved 3,389,000 shares of common stock for awards under the 1998 Plan. On November 13, 2008, the 1998 Plan expired, and no additional shares were granted under the Plan after that date.

2003 Restricted Stock Plan

The Restricted Plan for non-employee directors was approved by shareholders at the Company s February 26, 2004 Annual Meeting of Shareholders. It provided for an annual award of non-vested shares of common stock having a fair market value of $40,000 at close of business on October 1 of each year for each eligible non-employee director. The shares of common stock were awarded in four quarterly installments during the fiscal year if the director was still serving on the board on the quarterly issue date. The last awards under the Restricted Plan were made in 2010, and the Company has awarded all available shares under the Restricted Plan. However, the Company has continued to make an annual grant of shares to eligible non-employee directors under the 2009 Plan.

There was no compensation expense under the Restricted Plan for the nine months ended June 30, 2016 and 2015.

2009 Stock-Based Incentive Compensation Plan

The 2009 Plan authorizes the grant of Stock Appreciation Rights (SARs), Restricted Stock, Options, and other equity-based awards (collectively referred to as Awards). Options granted under the 2009 Plan may be either Incentive Stock Options as defined in section 422 of the Internal Revenue Code of 1986, as amended (the Code), or Nonqualified Stock Options as determined by the Compensation Committee of the Company s Board of Directors (the Compensation Committee).

Subject to an adjustment required because of a stock dividend, recapitalization, forward split or reverse split, reorganization, merger, consolidation, spin-off, combination, repurchase or share exchange, extraordinary or unusual cash distribution, or other similar corporate transaction or event, the maximum number of shares of common stock available for Awards under the 2009 Plan is 1,200,000, all of which may be issued pursuant to Awards of Incentive Stock Options. In addition, the 2009 Plan provides that no more than 300,000 shares of common stock per year may be awarded to any employee as a performance-based Award under Section 162(m) of the Code. At June 30, 2016, there were 268,439 shares of common stock available for Awards under the 2009 Plan.

If any Award is forfeited, or if any Option terminates, expires, or lapses without being exercised, the shares of common stock subject to such Award will again be available for future grant. Any shares tendered by a participant in payment of the exercise price of an Option or the tax liability with respect to an Award (including, in any case, shares withheld from any such Award) will not be available for future grant under the 2009 Plan. If there is any change in the Company s corporate capitalization, the Compensation Committee must adjust proportionately and equitably the number and kind of shares of common stock which may be issued in connection with future Awards, the number and type of shares of common stock covered by Awards then outstanding under the 2009 Plan, the number and type of shares of common stock available under the 2009 Plan, the exercise or grant price of any Award, or, if deemed appropriate, make provision for a cash payment with respect to any outstanding Award, provided that no adjustment may be made that would affect adversely the status of any Award that is intended to be a performance-based Award under Section 162(m) of

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the Code, unless otherwise determined by the Compensation Committee. In addition, the Compensation Committee may make adjustments in the terms and conditions of any Awards, including any performance goals, in recognition of unusual or nonrecurring events affecting the Company or any subsidiary, or in response to changes in applicable laws, regulations or accounting principles, provided that no adjustment may be made that would affect adversely the status of any Award that is intended to be a performance-based Award under Section 162(m) of the Code, unless otherwise determined by the Compensation Committee.

On April 17, 2014, the Board of Directors resolved to revise the valuation date and the timing of the issuance of the awards of non-vested shares of common stock to each eligible non-employee director under the 2009 Plan. Effective January 1, 2015, the awards had a fair market value of $40,000 each at the close of business on the first business day after January 1 of each calendar year and will be issued on the first business day after January 1 of the following year. If any non-employee director resigns from the Board of Directors prior to December 31 of such calendar year, the Company will issue to such non-employee director a pro-rata number of shares through the date of resignation. On November 12, 2015, the Board of Directors resolved that effective January 1, 2016, such awards would be in the form of restricted stock units (RSUs) with a fair market value of 40,000 each at the close of business on the first business day after January 1 of the calendar year of service, which RSU s shall vest in full on the first business day of the calendar year following the year of service.

Total compensation expense related to Options issued to employees under the 2009 Plan was approximately $0 and $59,000 for the three months ended June 30, 2016 and 2015, respectively; and $68,000 and $259,000 for the nine months ended June 30, 2016 and 2015, respectively. The expense under the 2009 Plan related to shares issued to non-employee members of the Company s Board of Directors as compensation was $0 for the three months ended June 30, 2016 and 2015, respectively, and $183,000 and $150,000 for each of the nine months ended June 30, 2016 and 2015, respectively. Total compensation expense associated with the 2009 Plan was $0 and $59,000 for the three months ended June 30, 2016 and 2015, respectively; and $251,000 and $409,000 for the nine months ended June 30, 2016 and 2015, respectively.

Stock repurchase program

On April 14, 2016, the Company s Board of Directors approved the extension of the current share repurchase program (originally approved on April 29, 2013 and previously extended in each of April 2014 and April 2015) which allows the Company to acquire up to 250,000 shares of its outstanding common stock for one year beginning May 1, 2016. Under the share repurchase program, the Company may purchase shares of its common stock through open market transactions, in privately negotiated block purchases, or in other private transactions (either solicited or unsolicited). The timing and amount of repurchase transactions under this program will depend on market conditions, and corporate and regulatory considerations. The program may be discontinued or suspended at any time. The Company anticipates funding for this program to come from available corporate funds, including cash on hand and future cash flow. During the three months ended June 30, 2016, the Company purchased 57,165 shares of its common stock under the program. The aggregate cost of the shares purchased in the three months ended June 30, 2016 was $169,871 at an average cost per share of $2.97. As of June 30, 2016, the number of shares that may yet be purchased under the current share repurchase program was 192,835 shares.

5. Earnings Per Share

	Three Months Ended June 30,	**Nine Months Ended June 30,**