

NORTECH SYSTEMS INC  
Form 10-Q  
August 14, 2018  
[Table of Contents](#)

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D. C. 20549

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended June 30, 2018

OR

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

For the transition period from            to

**NORTECH SYSTEMS INCORPORATED**

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Commission file number **0-13257**

State of Incorporation: **Minnesota**

IRS Employer Identification No. **41-1681094**

Executive Offices: **7550 Meridian Circle N., Suite # 150, Maple Grove, MN 55369**

Telephone number: **(952) 345-2244**

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulations 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  No

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

Large Accelerated Filer   
Non-accelerated Filer   
Emerging growth company

Accelerated Filer   
Smaller Reporting 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

Number of shares of \$.01 par value common stock outstanding at August 9, 2018 was 2,684,051



Table of Contents

## TABLE OF CONTENTS

	PAGE
<b><u>PART I - FINANCIAL INFORMATION</u></b>	
<u>Item 1</u> :	<u>Financial Statements</u>
	<u>Condensed Consolidated Statements of Operations and Comprehensive Income (Loss)</u> 3
	<u>Condensed Consolidated Balance Sheets</u> 4
	<u>Condensed Consolidated Statements of Cash Flows</u> 5
	<u>Condensed Notes to Consolidated Financial Statements</u> 6-17
<u>Item 2</u> :	<u>Management's Discussion and Analysis of Financial Condition And Results of Operations</u> 18-24
<u>Item 3</u> :	<u>Quantitative and Qualitative Disclosures About Market Risk</u> 24
<u>Item 4</u> :	<u>Controls and Procedures</u> 24
<b><u>PART II - OTHER INFORMATION</u></b>	
<u>Item 1</u> :	<u>Legal Proceedings</u> 25
<u>Item 1A</u> :	<u>Risk Factors</u> 25
<u>Item 2</u> :	<u>Unregistered Sales of Equity Securities, Use of Proceeds</u> 25
<u>Item 3</u> :	<u>Defaults on Senior Securities</u> 26
<u>Item 4</u> :	<u>Mine Safety Disclosures</u> 26
<u>Item 5</u> :	<u>Other Information</u> 26
<u>Item 6</u> :	<u>Exhibits</u> 26
<u>SIGNATURES</u>	27

Table of Contents**PART****ITEM 1. FINANCIAL STATEMENTS****NORTECH SYSTEMS INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)****(UNAUDITED)****(IN THOUSANDS, EXCEPT SHARE DATA)**

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2018	2017	2018	2017
Net Sales	\$ 28,538	\$ 30,134	\$ 54,985	\$ 58,452
Cost of Goods Sold	24,721	26,769	48,140	51,995
Gross Profit	3,817	3,365	6,845	6,457
Operating Expenses				
Selling Expenses	1,037	1,327	2,075	2,532
General and Administrative Expenses	2,046	1,944	4,155	4,065
Gain on Sale of Property and Equipment		(1)		(355)
Total Operating Expenses	3,083	3,270	6,230	6,242
Income From Operations	734	95	615	215
Other Expense				
Loss on Extinguishment of Debt		(175)		(175)
Interest Expense	(209)	(142)	(382)	(281)
Income (Loss) Before Income Taxes	525	(222)	233	(241)
Income Tax Expense (Benefit)	135	(206)	235	(211)
Net Income (Loss)	\$ 390	\$ (16)	\$ (2)	\$ (30)
Net Income (Loss) Per Common Share - Basic and Diluted	\$ 0.14	\$ (0.01)	\$ (0.00)	\$ (0.01)
Weighted Average Number of Common Shares Outstanding - Basic and Diluted	2,695,994	2,747,831	2,708,234	2,747,831
Other comprehensive income (loss)				
Foreign currency translation	(126)	1	(54)	(3)
Comprehensive income (loss), net of tax	\$ 264	\$ (15)	\$ (56)	\$ (33)

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*See Accompanying Condensed Notes to Condensed Consolidated Financial Statements*

Table of Contents

## NORTECH SYSTEMS INCORPORATED AND SUBSIDIARIES

## CONDENSED CONSOLIDATED BALANCE SHEETS

(IN THOUSANDS, EXCEPT SHARE DATA)

	JUNE 30, 2018 (Unaudited)	DECEMBER 31, 2017(1)
<b>ASSETS</b>		
Current Assets		
Cash	\$ 437	\$ 473
Restricted Cash	234	306
Accounts Receivable, less allowances of \$204 and \$209	19,309	17,417
Inventories	13,969	18,527
Contract Assets	6,547	
Prepaid Expenses and Other Current Assets	1,259	1,044
Total Current Assets	41,755	37,767
Property and Equipment, Net	10,110	10,176
Goodwill	2,375	2,375
Other Intangible Assets, Net	1,633	1,739
Other Non Current Assets	28	28
Total Assets	\$ 55,901	\$ 52,085
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
Current Liabilities		
Current Maturities of Long-Term Debt	\$ 1,014	\$ 1,003
Current Portion of Capital Lease Obligation	346	295
Accounts Payable	15,676	11,699
Accrued Payroll and Commissions	3,275	2,900
Other Accrued Liabilities	2,340	2,148
Total Current Liabilities	22,651	18,045
Long-Term Liabilities		
Long Term Line of Credit	7,142	8,503
Long-Term Debt, Net	3,843	4,353
Long-Term Capital Lease Obligation, Net	1,105	1,222
Other Long-Term Liabilities	151	137
Total Long-Term Liabilities	12,241	14,215
Total Liabilities	34,892	32,260
Commitments and Contingencies		
Shareholders Equity		
Preferred Stock, \$1 par value; 1,000,000 Shares Authorized: 250,000 Shares Issued and Outstanding	250	250
Common Stock - \$0.01 par value; 9,000,000 Shares Authorized: 2,686,328 and 2,739,250 Shares Issued and Outstanding, respectively	27	27
Additional Paid-In Capital	15,619	15,760
Accumulated Other Comprehensive Loss	(155)	(101)
Retained Earnings	5,268	3,889
Total Shareholders Equity	21,009	19,825

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Total Liabilities and Shareholders	Equity	\$	55,901	\$	52,085
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(1) The balance sheet at December 31, 2017 has been derived from the audited financial statements at that date

*See Accompanying Condensed Notes to Condensed Consolidated Financial Statements*



Table of Contents

**NORTECH SYSTEMS INCORPORATED AND SUBSIDIARIES**

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

**(UNAUDITED)**

**(IN THOUSANDS)**

	SIX MONTHS ENDED	
	2018	2017
	JUNE 30,	
Cash Flows From Operating Activities		
Net Loss	\$ (2)	\$ (30)
Adjustments to Reconcile Net Loss to Net Cash Provided by Operating Activities		
Depreciation and Amortization	1,108	1,233
Compensation on Stock-Based Awards and Equity Appreciation Rights	45	10
Loss on Extinguishment of Debt		17
Change in Contingent Consideration		(87)
Change in Accounts Receivable Allowance	(5)	(739)
Change in Inventory Reserves	73	229
Gain on Disposal of Property and Equipment		(355)
Changes in Current Operating Items		
Accounts Receivable	(1,886)	961
Inventories	(594)	(1,169)
Contract Assets	(88)	
Prepaid Expenses and Other Current Assets	(130)	(143)
Accounts Payable	3,722	1,288
Accrued Payroll and Commissions	374	(16)
Other Accrued Liabilities	124	94
Net Cash Provided by Operating Activities	2,741	1,293
Cash Flows from Investing Activities		
Proceeds from Sale of Property and Equipment		669
Purchase of Intangible Asset	(4)	(100)
Purchases of Property and Equipment	(557)	(359)
Net Cash (Used in) Provided by Investing Activities	(561)	210
Cash Flows from Financing Activities		
Net Change in Line of Credit	(1,361)	(672)
Proceeds from Long-Term Debt		5,123
Principal Payments on Long-Term Debt	(545)	(5,234)
Principal Payments on Capital Leases	(150)	
Loss on Extinguishment of Debt		(158)
Debt Issuance Costs		(268)
Share Repurchases	(186)	
Net Cash Used in Financing Activities	(2,242)	(1,209)
Effect of Exchange Rate Changes on Cash	(46)	(25)
Net Change in Cash	(108)	269
Cash - Beginning of Period	779	268
Cash - Ending of Period	\$ 671	\$ 537

Reconciliation of cash and restricted cash reported within the condensed consolidated balance sheets

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Cash	\$	437	\$	191
Restricted Cash		234		346
Total cash and restricted cash reported in the condensed consolidated statements of cash flows	\$	671	\$	537
<b>Supplemental Disclosure of Cash Flow Information:</b>				
Cash Paid During the Period for Interest	\$	317	\$	263
Cash Refunded During the Period for Income Taxes		167		23
<b>Supplemental Noncash Investing and Financing Activities:</b>				
Property and Equipment Purchases in Accounts Payable		284		244
Equipment Acquired under Capital Lease		83		

*See Accompanying Condensed Notes to Condensed Consolidated Financial Statements*

Table of Contents

**CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)  
(UNAUDITED)**

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Basis of Presentation*

The accompanying unaudited condensed consolidated financial statements for the interim periods have been prepared in accordance with Generally Accepted Accounting Principles in the United States of America ( GAAP ) for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the financial information and footnotes required by GAAP for complete financial statements, although we believe the disclosures are adequate to make the information presented not misleading. It is suggested that these condensed consolidated financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2017. The operating results for the interim periods presented are not necessarily indicative of the results expected for the full year or for any other interim period. In our opinion, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included.

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. In preparing these condensed consolidated financial statements, we have made our best estimates and judgments of certain amounts included in the condensed consolidated financial statements, giving due consideration to materiality. Changes in the estimates and assumptions used by us could have a significant impact on our financial results, since actual results could differ from those estimates.

*Principles of Consolidation*

The condensed consolidated financial statements include the accounts of Nortech Systems Incorporated and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated.

*Revenue Recognition*

Our revenue is comprised of product, engineering services and repair services. All revenue is recognized when the Company satisfies its performance obligation(s) under the contract by transferring the promised product or service to our customer either when (or as) our customer obtains control of the product or service, with the majority of our revenue being recognized over time including goods produced under contract manufacturing agreements and services revenue. A performance obligation is a promise in a contract to transfer a distinct product or service to a customer. A contract's transaction price is allocated to each distinct performance obligation. The majority of our contracts have a single

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performance obligation. Revenue is recorded net of returns, allowances and customer discounts. Our net sales for services were less than 10% of our total sales for all periods presented, and accordingly, are included in net sales in the Condensed Consolidated Statements of Operations and Comprehensive Income (Loss). Sales, value add, and other taxes collected from customers and remitted to governmental authorities are accounted for on a net (excluded from revenues) basis. Shipping and handling costs charged to our customers are included in net sales, while the corresponding shipping expenses are included in cost of goods sold.

Effective January 1, 2018, we adopted the FASB issued Accounting Standards Update ( ASU ) 2014-09, Revenue from Contracts with Customers (Topic 606) ( ASU 2014-09 ), which supersedes the revenue recognition requirements in ASC 605, Revenue Recognition. ASU 2014-09 is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. It also requires additional disclosure about the nature, amount, timing, and uncertainty of revenue, cash flows arising from

Table of Contents

customer contracts, including significant judgments and changes in judgments, and assets recognized from costs incurred to obtain or fulfill a contract. ASU 2014-09 is effective for fiscal years beginning after December 15, 2017, including interim periods within that reporting period. The Company adopted the provisions of ASU 2014-09 using the modified retrospective approach with application to contracts that were not completed as of January 1, 2018. The adoption of ASU 2014-09 had a significant impact to the Company's results of operations, cash flow and financial position, and as a result we now recognize the majority of our revenue over time rather than upon shipment resulting in an adjustment to retained earnings of \$1,381 on January 1, 2018. The Company has presented the disclosures required by this new standard, refer to Note 3.

*Stock-Based Awards*

Following is the status of all stock options as of June 30, 2018:

	Shares	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding - January 1, 2018	187,750	\$ 3.70		
Granted	134,000	3.77		
Exercised				
Cancelled				
Outstanding - June 30, 2018	321,750	\$ 3.56	8.53	\$ 18
Exercisable - June 30, 2018	87,750	\$ 4.00	6.21	\$ 3

The 2005 Plan has not been renewed, and therefore no further grants may be made under the 2005 Plan. In May 2017, the shareholders approved the 2017 Stock Incentive Plan which authorized the issuance of 350,000 shares. There were 114,000 and 134,000 stock options granted during the three and six months ended June 30, 2018, respectively.

Total compensation expense related to stock options for the three months ended June 30, 2018 and 2017 was \$25 and \$9, respectively and \$45 and \$9 for the six months ended June 30, 2018 and 2017, respectively. As of June 30, 2018, there was \$315 of unrecognized compensation which will vest over the next 3.44 years.

In November 2010, the Board of Directors adopted the Nortech Systems Incorporated Equity Appreciation Rights Plan ( 2010 Plan ). The total number of Equity Appreciation Right Units ( Units ) that can be issued under the 2010 Plan shall not exceed an aggregate of 1,000,000 Units as amended and restated on March 11, 2015. The 2010 Plan provides that Units issued shall fully vest three years from the base date as defined in the agreement unless terminated earlier. Units give the holder a right to receive a cash payment equal to the appreciation in book value per share of common stock from the base date, as defined, to the redemption date. Unit redemption payments under the 2010 Plan shall be paid in cash within 90 days after we determine the book value of the Units as of the calendar year immediately preceding the redemption date. The Units are adjusted to market value for each reporting period.

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During the three and six months ended June 30, 2018, no additional Units were granted. During the three and six months ended June 30, 2017, a total of 100,000 Units were granted.

Table of Contents

Total compensation expense (income) related to the vested outstanding Units based on the estimated appreciation over their remaining terms was \$0 and (\$7) for the three months ended June 30, 2018 and 2017, respectively and \$0 and \$1 for the six months ended June 30, 2018 and 2017, respectively.

As of both June 30, 2018 and December 31, 2017, no amounts were accrued under this plan.

***Net Income (Loss) per Common Share***

For both the three months and six months ended June 30, 2018 and 2017 all stock options are deemed to be antidilutive and, therefore, were not included in the computation of loss per common share amount.

***Share Repurchase Program***

As of June 30, 2018, we have a \$250 share repurchase program which was authorized by our Board of Directors in August 2017. Under this repurchase program, we repurchased 18,495 and 52,922 shares in the open market transactions totaling \$61 and \$186 for the three and six months ended June 30, 2018, respectively. As of June 30, 2018, we had \$27 remaining under this authorization. The par value of repurchased shares is deducted from common stock and the excess repurchase price over par value is deducted from additional paid-in capital.

***Segment Reporting Information***

All of our operations fall under the contract manufacturing segment within the electronic manufacturing Services industry. We strategically direct production between our various manufacturing facilities based on a number of considerations to best meet our customers' requirements. We share resources for sales, marketing, engineering, supply chain, information services, human resources, payroll, and all corporate accounting functions. Consolidated financial information is available that is evaluated regularly by the chief operating decision maker in assessing performance and allocating resources.

***Restricted Cash***

Cash and cash equivalents classified as restricted cash on our condensed consolidated balance sheets are restricted as to withdrawal or use under the terms of certain contractual agreements. The June 30, 2018 balance included lockbox deposits that are temporarily restricted due to timing at the period end. The lockbox deposits are applied against our line of credit the next business day. As of June 30, 2018, we had no outstanding letters of credit.

*Accounts Receivable and Allowance for Doubtful Accounts*

Credit is extended based upon an evaluation of the customer's financial condition and, while collateral is not required, the Company periodically receives surety bonds that guarantee payment. Credit terms are consistent with industry standards and practices. The amounts of trade accounts receivable have been reduced by an allowance for doubtful accounts of \$204 at June 30, 2018 and \$209 at December 31, 2017.

*Inventories*

Inventories are stated at the lower of cost (first-in, first-out method) or net realizable value. Costs include material, labor, and overhead required in the warehousing and production of our products. Inventory reserves are maintained for the estimated value of the inventories that may have a lower value than stated or quantities in excess of future production needs.



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Table of Contents

Inventories are as follows (in thousands):

	<b>June 30, 2018</b>	<b>December 31, 2017</b>
Raw Materials	\$ 14,397	\$ 13,870
Work in Process	307	3,112
Finished Goods	182	2,389
Reserves	(917)	(844)
<b>Total</b>	<b>\$ 13,969</b>	<b>\$ 18,527</b>

The primary decrease in work in process and finished goods inventory as of June 30, 2018 as compared to December 31, 2017 primarily relates to the adoption of ASU 2014-09 and the recognition of revenue over time rather than upon shipment of inventory. Refer to Note 3 for further information.

***Other Intangible Assets***

Other intangible assets at June 30, 2018 and December 31, 2017 are as follows (in thousands):

		<b>Gross Carrying Amount</b>	<b>June 30, 2018</b>	
	<b>Years</b>		<b>Accumulated Amortization</b>	<b>Net Book Value</b>
Customer Relationships	9	\$ 1,302	\$ 434	\$ 868
Trade Names	3	100	44	56
Intellectual Property	20	814	122	692
Patents	7	17		17
<b>Totals</b>		<b>\$ 2,233</b>	<b>\$ 600</b>	<b>\$ 1,633</b>

		<b>Gross Carrying Amount</b>	<b>December 31, 2017</b>	
	<b>Years</b>		<b>Accumulated Amortization</b>	<b>Net Book Value</b>
Customer Relationships	9	\$ 1,302	\$ 361	\$ 941
Intellectual Property	3	100	28	72
Trade Names	20	814	102	712
Patents	7	14		14
<b>Totals</b>		<b>\$ 2,230</b>	<b>\$ 491</b>	<b>\$ 1,739</b>

Amortization expense for the three and six months ended June 30, 2018 was \$55 and \$109, respectively. Amortization expense for the three and six months ended June 30, 2017 was \$56 and \$106, respectively. Estimated future annual amortization expense (not including projects in process) related to these assets is approximately as follows (in thousands):



Table of Contents

Year	Amount
Remainder of 2018	\$ 110
2019	219
2020	191
2021	185
2022	185
Thereafter	726
Total	\$ 1,616

***Impairment of Goodwill and Other Intangible Assets***

In accordance with ASC 350, *Goodwill and Other Intangible Assets*, goodwill is not amortized but is required to be reviewed for impairment at least annually or when events or circumstances indicate that carrying value may exceed fair value. We test impairment annually as of October 1st. No events were identified during the six months ended June 30, 2018 that would require us to test for impairment. In testing goodwill for impairment we perform a quantitative impairment test, including computing the fair value of the reporting unit and comparing that value to its carrying value. If the fair value is less than its carrying value, then the goodwill is determined to be impaired. In the event that goodwill is impaired, an impairment charge to earnings would become necessary.

***Impairment Analysis***

We evaluate long-lived assets, primarily property and equipment and intangible assets, as well as the related depreciation periods, whenever current events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable. Recoverability for assets to be held and used is based on our projection of the undiscounted future operating cash flows of the underlying assets. To the extent such projections indicate that future undiscounted cash flows are not sufficient to recover the carrying amounts of related assets, a charge might be required to reduce the carrying amount to equal estimated fair value. No impairment expense was recorded during the three and six months ended June 30, 2018 and 2017, respectively.

***Recently Issued Accounting Standards***

During February 2016, the FASB issued ASU 2016-02, *Leases*. ASU 2016-02 was issued to increase transparency and comparability among organizations by recognizing all lease transactions (with terms in excess of 12 months) on the balance sheet as a lease liability and a right-of-use asset (as defined). ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, with earlier application permitted. Upon adoption, the lessee will apply the new standard on a modified retrospective basis to all periods presented. We are currently assessing the effect that ASU 2016-02 will have on our consolidated financial statements.

In March 2018, we adopted FASB ASU 2018-05, *Income Taxes (Topic 740): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118*, which updates the income tax accounting in U.S. GAAP to reflect the Securities and Exchange Commission (SEC) interpretive guidance released on December 22, 2017, when the Tax Cuts and Jobs Act (the Tax Act) was signed into law. Additional information regarding the adoption of this standard is contained in Note 5, *Income Taxes*.

**NOTE 2. CONCENTRATION OF CREDIT RISK AND MAJOR CUSTOMERS**

Financial instruments that potentially subject us to concentrations of credit risk consist principally of cash and accounts receivable. With regard to cash, we maintain our excess cash balances in checking accounts at primarily two financial institutions, one in the United States and one in China. The account in the United States may at times exceed federally insured limits. Of the \$671 in cash at June 30, 2018, approximately \$436 was held at banks located in China. We grant credit to customers in the normal course of business and do not require collateral on our accounts receivable.

Table of Contents

Our largest customer has two divisions that together accounted for 10% or more of our net sales during the three and six months ended June 30, 2018 and 2017. One division accounted for approximately 21% and 20% of net sales for the three and six months ended June 30, 2018, respectively, and approximately 25% for both the three and six months ended June 30, 2017. The other division accounted for approximately 1% and 1% of net sales for the three months and six ended June 30, 2018, respectively, and approximately 1% and 2% of net sales for the three and six months ended June 30, 2017, respectively. Together they accounted for approximately 22% and 21% of net sales for the three and six months ended June 30, 2018, respectively, and approximately 27% of both the three and six months ended June 30, 2017. Accounts receivable from the customer at June 30, 2018 and December 31, 2017 represented approximately 19% and 16% of our total accounts receivable, respectively.

Export sales represented approximately 21% and 17% of net sales for the three months ended June 30, 2018 and 2017, respectively. Export sales represented 20% and 16% of net sales for the six months ended June 30, 2018 and 2017, respectively.

**NOTE 3. REVENUE**

**Revenue recognition**

Our revenue is comprised of product, engineering services and repair services. All revenue is recognized when the Company satisfies its performance obligation(s) under the contract by transferring the promised product or service to our customer either when (or as) our customer obtains control of the product or service, with the majority of our revenue being recognized over time including goods produced under contract manufacturing agreements and services revenue. A performance obligation is a promise in a contract to transfer a distinct product or service to a customer. A contract's transaction price is allocated to each distinct performance obligation. The majority of our contracts have a single performance obligation, as the promise to transfer products or services is not separately identifiable from other promises in the contract and, therefore, not distinct.

Revenue is measured as the amount of consideration we expect to receive in exchange for transferring products or providing services. As such, revenue is recorded net of returns, allowances and customer discounts. Sales, value add, and other taxes collected from customers and remitted to governmental authorities are accounted for on a net (excluded from revenues) basis. Shipping and handling costs are included in cost of goods sold.

The majority of our revenue is derived from the transfer of goods produced under contract manufacturing agreements which have no alternative use and we have an enforceable right to payment for our performance completed to date. Our performance obligations within our contract manufacturing agreements are generally satisfied over time as the goods are produced based on customer specifications and we have an enforceable right to payment for the goods produced. If these requirements are not met, the revenue is recognized at a point in time, generally upon shipment. Revenue under contract manufacturing agreements that was recognized over time accounted for approximately 91% of our revenue for both the three and six months ended June 30, 2018. Revenues under these agreements are generally recognized over time using an input measure based upon the proportion of actual costs incurred.

Accounting for contract manufacturing agreements involves the use of various techniques to estimate total revenue and costs. We estimate profit on these agreements as the difference between total estimated revenue and expected costs to complete the performance obligation within the terms of the agreement and recognize the respective profit as the goods are produced. The estimates to determine the profit earned on the

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performance obligation are based on anticipated selling prices and historical cost of goods sold and represent our best judgement at the time. Changes in judgements on these above estimates could impact the timing and amount of revenue recognized with a resulting impact on the timing and amount of associated profit.

On occasion our customers provide materials to be used in the manufacturing process and the fair value of the materials is included in revenue as noncash consideration at the point in time when the manufacturing process

Table of Contents

commences along with the same corresponding amount recorded as cost of goods sold. The inclusion of noncash consideration has no impact on overall profitability.

**Contract Assets**

Contract assets, recorded as such in the Condensed Consolidated Balance Sheet, consist of unbilled amounts related to revenue recognized over time. Significant changes in the contract assets balance during the three and six months ended June 30, 2018 was as follows (in thousands):

**Six Months Ended June 30, 2018**

Outstanding at January 1, 2018	\$	6,459
Increase (decrease) attributed to:		
Transferred to receivables from contract assets recognized		(5,648)
Product transferred over time		5,736
Outstanding at June 30, 2018	\$	6,547

We expect substantially all of the remaining performance obligations for the contract assets recorded as of June 30, 2018, to be transferred to receivables within 90 days, with any remaining amounts to be transferred within 180 days. We bill our customers upon shipment with payment terms of up to 120 days.

The following tables summarize our net sales by market for the three and six months ended June 30, 2018 (in thousands):

	Product/ Service Transferred Over Time	Three Months Ended June 30, 2018			Total Net Sales by Market
		Product Transferred at Point in Time	Noncash Consideration		
Aerospace and Defense	\$ 4,001	\$ 72	\$ 196	\$ 4,269	
Medical	11,934	87	544	12,565	
Industrial	10,023	1,206	475	11,704	
Total net sales	\$ 25,958	\$ 1,365	\$ 1,215	\$ 28,538	

	Product/ Service Transferred Over Time	Six Months Ended June 30, 2018			Total Net Sales by Market
		Product Transferred at Point in Time	Noncash Consideration		
Aerospace and Defense	\$ 8,717	\$ 120	\$ 393	\$ 9,230	
Medical	21,201	569	945	22,715	
Industrial	20,089	2,049	902	23,040	
Total net sales	\$ 50,007	\$ 2,738	\$ 2,240	\$ 54,985	

**Impact of New Revenue Guidance on Financial Statement Line Items**

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The following table compares the reported condensed consolidated statement of operations and comprehensive loss, balance sheet and cash flows, as of and for the three and six months ended June 30, 2018, to the pro-forma amounts had the previous guidance been in effect (in thousands):



Table of Contents

	Three Months Ended June 30, 2018		Six Months Ended June 30, 2018	
	As Reported	Pro forma as if the previous accounting guidance was in effect	As Reported	Pro forma as if the previous accounting guidance was in effect
<b>Condensed Consolidated Statement of Operations</b>				
Net Sales	\$ 28,538	\$ 26,928	\$ 54,985	\$ 52,658
Cost of Goods Sold	24,721	23,106	48,140	45,836
Gross Profit	3,817	3,822	6,845	6,822
Income from Operations	734	739	615	592
Income Before Income Taxes	525	530	233	210
Income Tax Expense	135	135	235	235
Net Income (Loss)	\$ 390	\$ 395	\$ (2)	\$ (25)
Net Income (Loss) Per Common Share - Basic and Diluted	\$ 0.14	\$ 0.15	\$	\$ (0.01)

	As of June 30, 2018	
	As Reported	Pro forma as if the previous accounting guidance was in effect
<b>Condensed Consolidated Balance Sheet</b>		
Assets		