

KOSS CORP
Form 10-K
August 27, 2012

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

FORM 10-K

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

For the fiscal year ended June 30, 2012

OR

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

COMMISSION FILE NUMBER 0-3295

KOSS CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	39-1168275
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

4129 North Port Washington Avenue, Milwaukee, Wisconsin	53212
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (414) 964-5000

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock \$0.005 par value	The Nasdaq Stock Market LLC

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

NONE

(Title of class)

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 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 ☐

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Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

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.

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting company ☒

(Do not check if a 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

☐ No ☒

The aggregate market value of the common voting stock held by nonaffiliates of the registrant as of December 31, 2011 was approximately \$11,497,395 (based on the \$5.00 per share closing price of the Company's common stock as reported on the NASDAQ Stock Market on December 30, 2011).

On August 17, 2012, 7,382,706 shares of voting common stock were outstanding.

Documents Incorporated by Reference

Part III of this Form 10-K incorporates by reference information from Koss Corporation's Proxy Statement for its 2012 Annual Meeting of Stockholders filed with the Commission under Regulation 14A within 120 days of the end of the fiscal year covered by this Form 10-K.

KOSS CORPORATION
FORM 10-K
June 30, 2012

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains forward-looking statements within the meaning of that term in the Private Securities Litigation Reform Act of 1995 (the “Act”) (Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934). Additional written or oral forward-looking statements may be made by the Company from time to time in filings with the Securities Exchange Commission, press releases, or otherwise. Statements contained in this Form 10-K that are not historical facts are forward-looking statements made pursuant to the safe harbor provisions of the Act. Forward-looking statements may include, but are not limited to, projections of revenue, income or loss and capital expenditures, statements regarding future operations, anticipated financing needs, compliance with financial covenants in loan agreements, plans for acquisitions or sales of assets or businesses, plans relating to products or services of the Company, assessments of materiality, predictions of future events, the effects of pending and possible litigation and assumptions relating to the foregoing. In addition, when used in this Form 10-K, the words “anticipates,” “believes,” “estimates,” “expects,” “intends,” “plans” and variations thereof and similar expressions are intended to identify forward-looking statements.

Forward-looking statements are inherently subject to risks and uncertainties, some of which cannot be predicted or quantified based on current expectations. Consequently, future events and actual results could differ materially from those set forth in, contemplated by, or underlying the forward-looking statements contained in this Form 10-K, or in other Company filings, press releases, or otherwise. In addition to the factors discussed in this Form 10-K, other factors that could contribute to or cause such differences include, but are not limited to, developments in any one or more of the following areas: future fluctuations in economic conditions, the receptivity of consumers to new consumer electronics technologies, the rate and consumer acceptance of new product introductions, competition, pricing, the number and nature of customers and their product orders, production by third party vendors, foreign manufacturing, sourcing, and sales (including foreign government regulation, trade and importation concerns), borrowing costs, changes in tax rates, pending or threatened litigation and investigations, and other risk factors which may be detailed from time to time in the Company’s Securities and Exchange Commission filings.

Readers are cautioned not to place undue reliance on any forward-looking statements contained herein, which speak only as of the date hereof. The Company undertakes no obligation to publicly release the result of any revisions to these forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unexpected events.

PART I

ITEM 1. BUSINESS.

GENERAL

As used herein unless the context otherwise requires, the term “Company” means Koss Corporation and its former consolidated wholly-owned subsidiary, Koss Classics Ltd. (“Koss Classics”), which was dissolved in the three months ended September 30, 2011. The Company was incorporated in Delaware in 1971.

The Company operates in the audio/video industry segment of the home entertainment industry through its design, manufacture and sale of stereo headphones and related accessory products. The Company reports its results as a single reporting segment, as the Company’s principal business line is the design, manufacture and sale of stereo headphones and related accessories.

The Company’s products are sold through national retailers, international distributors, audio specialty stores, the internet, direct mail catalogs, regional department store chains, discount department stores, military exchanges and prisons under the “Koss” name. The Company also sells products to distributors for resale to school systems, and directly to other manufacturers for inclusion with their own products. The Company has more than 300 domestic dealers and its products are carried in approximately 17,000 domestic retail outlets and numerous retailers worldwide. International markets are served by domestic sales representatives and a sales office in Switzerland which utilizes independent distributors in several foreign countries.

Ninety-nine percent of the Company’s products are stereo headphones for listening to music. The products are not significantly differentiated by their retail sales channel or application with the exception of products sold to school systems and prisons. There are no other product line differentiations other than the quality of the sound produced by the stereo headphone itself, which is highly subjective. The business could also be classified by distribution channel.

In fiscal year 2012, the Company launched the Striva products which allow the consumer to listen to the stereo headphones directly from the World Wide Web using Wi-Fi. These products are sold through the Koss website.

The Company sources complete stereo headphones manufactured to its specifications from various manufacturers in Asia as well as raw materials used to produce stereo headphones at its plant in Milwaukee, Wisconsin. Management believes that it has sources of complete stereo headphones and raw materials that are adequate for its needs.

There are no employment or compensation commitments between the Company and its dealers. The Company has several independent manufacturers’ representatives as part of its distribution efforts. The Company typically signs one year contracts with these manufacturers’ representatives. The arrangements with foreign distributors do not contemplate that the Company pays any compensation other than any profit the distributors make upon their sale of the Company’s products.

INTELLECTUAL PROPERTY

John C. Koss is recognized for creating the stereo headphone industry with the first SP3 stereo headphone in 1958. The Company regularly applies for registration of its trademarks in many countries around the world, and over the years the Company has had numerous trademarks registered and patents issued in North America, South America, Asia, Europe, Africa, and Australia. The Company currently has approximately 441 trademarks registered in 90 countries around the world and patents in 31 countries. The Company has trademarks to protect the brand name,

Koss, and its logo on its products. These trademarks are maintained throughout the countries in which the Company sells its products. The Company also holds many design patents that protect the unique visual appearance of some of its products. These trademarks and patents are important to differentiate the Company from its competitors. Certain of the Company's trademarks are of material value and importance to the conduct of its business. The Company considers protection of its proprietary developments important; however, the Company's business is not, in the opinion of management, materially dependent upon any single trademark or patent. During the year ended June 30, 2012, the Company took steps to update and monitor its patents and trademarks to protect its intellectual property around the world.

SEASONALITY

Although retail sales of consumer electronics have typically been higher during the holiday season, stereo headphones have also seen increased interest as gift items throughout the year. Management of the Company believes that its business and industry segment are no longer seasonal as evidenced by the fact that net sales for the year ended June 30, 2012 were almost

equally split between the first and second halves of the year. Management believes that the reason for this level performance of sales to retailers and distributors is related to the fact that stereo headphones have become replacement items for portable electronic products. Therefore, upgrades and replacements appear to have as much interest over the course of the year as gifts of stereo headphones during the holiday season.

WORKING CAPITAL AND BACKLOG

The Company's working capital needs do not differ substantially from those of its competitors in the industry and generally reflect the need to carry significant amounts of inventory to meet delivery requirements of its customers. From time to time, although rarely, the Company may extend payment terms to its dealers for a special promotion. For instance, the Company has in the past offered a 90-120 day payment period for certain customers, such as computer retailers and office supply stores. Based on historical trends, management does not expect these practices to have a material effect on net sales or net income. The Company's backlog of orders as of June 30, 2012 is not significant in relation to net sales during fiscal year 2012 or projected fiscal year 2013 net sales.

CUSTOMERS

The Company markets a line of products used by consumers to listen to music, DVD's in vehicles, sound bytes on computer systems, and other audio related media. The Company distributes these products through retail channels in the U.S. and independent distributors throughout the rest of the world. The Company markets its products to approximately 17,000 domestic retailers and numerous retailers worldwide. During fiscal year 2012, the Company's sales to its largest single customer, Tura Scandinavia AB, were approximately 25% of net sales and sales to Walmart accounted for 11% of fiscal year 2012 net sales. In fiscal year 2011, net sales to Tura Scandinavia AB and Walmart, accounted for 25% and 17% of net sales, respectively. The Company is dependent upon its ability to retain a base of retailers and distributors to sell the Company's line of products. Loss of retailers and distributors means loss of product placement. The Company has broad distribution across many channels including specialty stores, mass merchants, and electronics stores. Management believes that any loss of revenues would be partially offset by a corresponding decrease, on a percentage basis, in expenses; thereby partially reducing the impact on the Company's income from operations. The five largest customers of the Company (including Tura Scandinavia AB and Walmart) accounted for approximately 48% and 53% of total net sales in fiscal years 2012 and 2011, respectively.

The recently launched Striva product line is sold directly to consumers through the Koss website. This product line was launched late in fiscal year 2012 and sales of these products were not significant in fiscal year 2012.

COMPETITION

The Company focuses on the stereo headphone industry. In the stereo headphone market, the Company competes directly with approximately five major competitors, several of which are large and diversified and have greater total assets and resources than the Company. The extent to which retailers and consumers view the Company as an innovative vendor of high quality stereo headphone products, and a provider of excellent after sales customer service, is the extent to which the Company maintains a competitive advantage. The Company relies upon its unique sound, quality workmanship, brand identification, engineering skills, and customer service to maintain its competitive position.

RESEARCH AND DEVELOPMENT

The amount expensed on engineering and research activities relating to the development of new products or the improvement of existing products was approximately \$1,306,000 during fiscal year 2012 as compared with approximately \$900,000 during fiscal year 2011. These activities were conducted by both Company personnel and

outside consultants. The Company expects that research and development costs will continue and it is planning to introduce a several new product offerings during fiscal year 2013.

ENVIRONMENTAL MATTERS

The Company believes that it has materially complied with all currently existing federal, state and local statutes and regulations regarding environmental standards and occupational safety and health matters to which it is subject. During the fiscal years 2012 and 2011, the amounts incurred in complying with federal, state and local statutes and regulations pertaining to environmental standards and occupational safety and health laws and regulations did not materially affect the Company's operating results or financial condition.

EMPLOYEES

As of June 30, 2012, the Company employed 60 people, who are all non-union. The Company also engages temporary personnel.

FOREIGN SALES

The Company's competitive position and risks relating to its business in foreign markets are comparable to those in the domestic market. In addition, the governments of foreign nations may elect to erect trade barriers on imports. The creation of additional barriers would reduce the Company's net sales and net income. In addition, any fluctuations in currency exchange rates could affect the pricing of the Company's products and divert customers who might choose to purchase lower-priced, less profitable products, and could affect overall demand for the Company's products. For further information, see Part II, Item 7 and Note 18 to the consolidated financial statements.

The Company has a small sales office in Switzerland to service the international export marketplace. The Company is not aware of any material risks in maintaining this operation. Loss of this office would result in a transfer of sales and marketing responsibility. The Company sells its products to independent distributors in countries and regions outside the United States including Europe, the Middle East, Africa, Asia, South America, Latin America, the Caribbean, Canada and Mexico. During the last two fiscal years, net sales of all Koss products, were distributed as follows:

	2012	2011
United States	\$ 17,155,135	\$ 19,532,323
Sweden	9,361,346	10,450,895
Cyprus	1,901,601	1,119,701
Russia	1,430,949	2,139,521
Canada	1,220,109	1,079,081
Czech Republic	1,200,374	1,237,034
All other countries	5,596,253	5,959,580
Net sales	\$ 37,865,767	\$ 41,518,135

In addition to a manufacturing facility in Milwaukee, Wisconsin, the Company uses contract manufacturing facilities in the People's Republic of China, Taiwan and South Korea. These independent suppliers are distant from the Company, which means that we are at risk of business interruptions due to natural disasters, war, disease and government intervention through tariffs or trade restrictions that are of less concern domestically. The Company maintains finished goods inventory in its U.S. facility to mitigate this risk. The Company's goal is to stock finished goods inventory at an average of approximately 90 days demand per item. Recovery of a single facility through replacement of a supplier in the event of a disaster or suspension of supply could take 120 days. The Company believes that it could restore production of its top ten selling models (which represent approximately 57% of the Company's 2012 net sales) within one year. The Company is also at risk if the trade restrictions are introduced on its products based upon country of origin. In addition, the Company may not be able to pass along most increases in tariffs and freight charges to the Company's customers, which would directly affect profits.

AVAILABLE INFORMATION

The Company's internet website is <http://www.koss.com>. The Company makes available free of charge through its internet website the Company's annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements and all amendments to those reports as soon as reasonably practicable after they are

electronically filed with (or furnished to) the Securities and Exchange Commission. These reports and other information regarding the Company are also available on the SEC's internet website at <http://www.sec.gov>.

ITEM 2.

PROPERTIES.

The Company leases its facility in Milwaukee, Wisconsin from its Board Chairman. On May 15, 2012, the lease was renewed extending the expiration to June 30, 2018. The lease extension maintained the rent at a fixed rate of \$380,000 per year and it is being accounted for as an operating lease. The Company is responsible for all property maintenance, insurance, taxes, and other normal expenses related to ownership. All facilities are in good repair and, in the opinion of management, are suitable and adequate for the Company's business purposes.

ITEM 3.

LEGAL PROCEEDINGS.

As of June 30, 2012, the Company is involved in several legal matters and has initiated certain actions against third parties related to the unauthorized transactions as previously reported. A description of these legal matters is included at Note 20 of the Notes to Consolidated Financial Statements included herein, which description is incorporated herein by reference.

PART II

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

MARKET INFORMATION ON COMMON STOCK

The Company's common stock is traded on The NASDAQ Stock Market under the trading symbol KOSS. There were approximately 1,420 record holders of the Company's common stock as of August 1, 2012. This number does not include individual participants in security position listings. The quarterly high and low sale prices of the Company's common stock for the last two fiscal years as well as dividends declared are shown below.

Quarter Ended	High	Low	Per Share Dividend
September 30, 2010	\$5.90	\$5.15	\$0.06
December 31, 2010	\$5.75	\$4.60	\$0.06
March 31, 2011	\$7.81	\$4.90	\$0.06
June 30, 2011	\$7.54	\$5.25	\$0.06
September 30, 2011	\$6.75	\$5.25	\$0.06
December 31, 2011	\$6.27	\$4.92	\$0.06
March 31, 2012	\$5.95	\$5.00	\$0.06
June 30, 2012	\$5.68	\$4.91	\$0.06

The Company's stockholders are entitled to receive dividends as may be declared by the Board of Directors and paid out of funds legally available therefore. The Company began paying dividends for the quarter ended September 30, 2002 and has paid a dividend for each quarter since, including the last fiscal quarter ended June 30, 2012. On April 26, 2012 the Company announced its quarterly dividend of \$0.06 per share for stockholders of record on June 29, 2012. The dividend was paid on July 16, 2012. Although the Company anticipates it will continue to pay a quarterly dividend, the decision to pay dividends and the amount of such dividends are within the sole discretion of the Board of Directors, who meet quarterly. The decision to pay dividends will depend on the Company's operating results, financial condition, tax considerations, alternative uses for such funds, and other factors the Board of Directors deem relevant, and there can be no assurance that dividends will be paid in the future.

COMPANY REPURCHASES OF EQUITY SECURITIES

Period (2012)	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan (1)	Approximate Dollar Value of Shares Available under Repurchase Plan
April 1-April 30	—	\$—	—	\$2,139,753
May 1-May 31	—	\$—	—	\$2,139,753
June 1-June 30	—			