

CPS TECHNOLOGIES CORP/DE/
Form 10-Q
November 10, 2016

**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 period ended October 1, 2016
or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from to

Commission file number 0-16088

CPS TECHNOLOGIES CORPORATION

(Exact Name of Registrant as Specified in its Charter)

<u>Delaware</u>	<u>04-2832509</u>
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

<u>111 South Worcester Street</u>	
<u>Norton MA</u>	<u>02766-2102</u>
(Address of principal executive offices)	(Zip Code)

(508) 222-0614
Registrants Telephone Number, including Area Code:

CPS Technologies Corporation

111 South Worcester Street

Norton, MA 02766-2102

Former Name, Former Address and Former Fiscal Year if Changed since Last Report

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 than the registrant was required to file such reports), and (2) has been subject to the filing requirements for the past 90 days. Yes No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act. (Check one):

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date. Number of shares of common stock outstanding as of October 31, 2016: 13,203,436.

PART I FINANCIAL INFORMATION

ITEM 1 FINANCIAL STATEMENTS (Unaudited)

CPS TECHNOLOGIES CORPORATION

Balance Sheets (Unaudited)

(continued on next page)

	October 1, 2016	December 26, 2015
ASSETS		
Current assets:		
Cash and cash equivalents	\$3,458,475	\$3,412,649
Accounts receivable-trade, net	2,456,181	3,572,479
Inventories, net	2,141,921	2,632,444
Prepaid expenses and other current assets	116,261	104,761
Deferred taxes	707,188	467,374
 Total current assets	 8,880,026	 10,189,707
Property and equipment:		
Production equipment	8,326,020	8,460,727
Furniture and office equipment	410,841	409,793
Leasehold improvements	854,215	854,215
 Total cost	 9,591,076	 9,724,735
Accumulated depreciation and amortization	(8,550,359)	(8,593,236)
Construction in progress	787,365	557,054
 Net property and equipment	 1,828,082	 1,688,553
Deferred taxes, non-current portion	1,683,375	1,683,375
 Total assets	 \$12,391,483	 \$13,561,635

See accompanying notes to financial statements.

CPS TECHNOLOGIES CORPORATION

Balance Sheets (Unaudited)

(concluded)

LIABILITIES AND STOCKHOLDERS' EQUITY	October 1, 2016	December 26, 2015
Current liabilities:		
Accounts payable	817,568	1,622,564
Accrued expenses	608,948	931,916

Total current liabilities	1,426,516	2,554,480
Commitments (note 9)		
Stockholders' equity:		
Common stock, \$0.01 par value, authorized 20,000,000 shares; issued 13,413,492 and 13,412,292 shares; outstanding 13,203,436 and 13,197,918 shares; at October 1, 2016 and December 26, 2015, respectively	134,235	134,123
Additional paid-in capital	35,413,125	35,245,030
Accumulated deficit	(24,065,340)	(23,864,945)
Less cost of 220,056 and 214,374 common shares repurchased at October 1, 2016 and December 26, 2015, respectively	(517,053)	(507,053)
Total stockholders' equity	10,964,967	11,007,155
Total liabilities and stockholders' equity	\$12,391,483	\$13,561,635

See accompanying notes to financial statements.

CPS TECHNOLOGIES CORPORATION

Statements of Income (Unaudited)

	First Quarter Ended		Nine month Periods ended	
	October 1, 2016	September 26, 2015	October 1, 2016	September 26, 2015
Revenues:				
Product sales	\$3,326,930	\$5,423,107	\$12,477,543	\$16,307,008
Research and development under cooperative agreement	—	—	—	42,254
Total Revenues	3,326,930	5,423,107	12,477,543	16,349,262
Cost of product sales	2,941,098	4,448,991	10,399,236	12,905,775
Cost of research and development under cooperative agreement	—	—	—	34,970
Gross Margin	385,832	974,116	2,078,307	3,408,517
Selling, general and				

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administrative expense	763,260	960,321	2,563,906	3,085,454
Operating income (loss)	(377,428)	13,795	(485,599)	323,063
Interest income (expense), net	1,742	1,454	6,980	2,305
Other income	40,000	—	41,225	—
Net income (loss) before income tax expense	(335,686)	15,249	(437,395)	325,368
Income tax (benefit) expense	(196,900)	7,000	(237,000)	129,500
Net income (loss)	\$(138,786)	\$8,249	\$(200,395)	\$195,868
Net income (loss) per basic common share	\$(0.01)	\$0.00	\$(0.02)	\$0.01
Weighted average number of basic common shares outstanding	13,203,436	13,197,827	13,200,584	13,174,598
Net income (loss) per diluted common share	\$(0.01)	\$0.00	\$(0.02)	\$0.01
Weighted average number of diluted common shares outstanding	13,203,436	13,611,956	13,200,584	13,656,888

See accompanying notes to financial statements.

CPS TECHNOLOGIES CORPORATION

Statements of Cash Flows (Unaudited)

Nine Month Periods Ended

	October 1, 2016	September 26, 2015
Cash flows from operating activities:		
Net income (loss)	\$(200,395)	\$195,868
Adjustments to reconcile net income to cash provided by (used in) operating activities		
Depreciation & amortization	380,901	406,138
Share-based compensation	153,557	226,853
Deferred taxes	(237,000)	129,500
Excess tax benefit from stock options exercised	(2,814)	(49,379)
Gain on sale of property and equipment	(40,000)	—

Changes in:		
Accounts receivable-trade, net	1,116,298	(116,503)
Inventories	490,523	(82,443)
Prepaid expenses	(11,500)	65,440
Accounts payable	(804,996)	268,798
Accrued expenses	322,968	15,043
Net cash provided by (used in) operating activities	521,606	1,059,315
Cash flows from investing activities:		
Purchases of property and equipment	(520,430)	(300,017)
Proceeds from sale of property and equipment	40,000	—
Net cash used in investing activities	(480,430)	(300,017)
Cash flows from financing activities:		
Proceeds from issuance of common stock	11,836	172,671
Excess tax benefit from stock options exercised	2,814	49,379
Repurchase of common stock	(10,000)	(172,470)
Net cash provided by financing activities	4,650	49,581
Net increase in cash and cash equivalents	45,826	808,879
Cash and cash equivalents at beginning of period	3,412,649	2,305,580
Cash and cash equivalents at end of period	\$3,458,475	\$3,114,458
Supplemental cash flow information:		
Cash paid for taxes, net of refunds	\$8,000	\$27,005
See accompanying notes to financial statements.		

CPS TECHNOLOGIES CORPORATION

Notes to Financial Statements

(Unaudited)

(1) Nature of Business

CPS Technologies Corporation (the “Company” or “CPS”) provides advanced material solutions to the electronics, power generation, automotive and other industries. The Company’s primary advanced material solution is metal-matrix composites which are a combination of metal and ceramic.

CPS also assembles housings and packages for hybrid circuits. These housings and packages may include components made of metal-matrix composites or they may include components made of more traditional materials such as aluminum, copper-tungsten, etc.

The Company sells into several end markets including the wireless communications infrastructure market, high-performance microprocessor market, motor controller market, and other microelectronic and structural markets.

(2) Interim Financial Statements

As permitted by the rules of the Securities and Exchange Commission applicable to quarterly reports on Form 10-Q, these notes are condensed and do not contain all disclosures required by generally accepted accounting principles.

The accompanying financial statements are unaudited. In the opinion of management, the unaudited financial statements of CPS reflect all normal recurring adjustments which are necessary to present fairly the financial position and results of operations for such periods.

The Company's balance sheet at December 26, 2015 has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements.

For further information, refer to the financial statements and footnotes thereto included in the Registrant's Annual Report on Form 10-K for the year ended December 26, 2015.

The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year.

(3) Net Income Per Common and Common Equivalent Share

Basic net income (loss) per common share is calculated by dividing net income (loss) by the weighted average number of common shares outstanding during the period. Diluted net income (loss) per common share is calculated by dividing net income (loss) by the sum of the weighted average number of common shares plus additional common shares that would have been outstanding if potential dilutive common shares had been issued for granted stock options and stock purchase rights. Common stock equivalents are excluded from the diluted calculations when a net loss is incurred as they would be anti-dilutive.

The following table presents the calculation of both basic and diluted EPS:

	Three Months Ended		Nine-Months Ended	
	October 1, 2016	September 26, 2015	October 1, 2016	September 26, 2015
Basic EPS Computation:				
Numerator:				
Net income (loss)	\$(138,786)	\$8,249	\$(200,395)	\$195,868
Denominator:				
Weighted average Common shares				
Outstanding	13,203,436	13,197,827	13,200,584	13,174,598
Basic EPS	\$(0.01)	\$0.00	\$(0.02)	\$0.01
Diluted EPS Computation:				
Numerator:				
Net income (loss)	\$(138,786)	\$8,249	\$(200,395)	\$195,868
Denominator:				
Weighted average Common shares				
Outstanding	13,203,436	13,197,827	13,200,584	13,174,598
Dilutive effect of stock options	—	414,129	—	482,290
Total Shares	13,203,436	13,611,956	13,200,584	13,656,888
Diluted EPS	\$(0.01)	\$0.00	\$(0.02)	\$0.01

(4) Share-Based Payments

The Company measures the cost of employee services received in exchange for an award of equity instruments based on the grant date fair value of the award. That cost is recognized over the period during which an employee is required to provide services in exchange for the award, the requisite service period (usually the vesting period). The Company provides an estimate of forfeitures at initial grant date. Reductions in compensation expense associated with the forfeited options are estimated at the date of grant, and this estimated forfeiture rate is adjusted periodically based on actual forfeiture experience. The company uses the Black-Scholes option pricing model to determine the fair value of the stock options granted.

There were no stock options granted under the Plan during the quarters ended October 1, 2016 and September 26, 2015.

During the quarter ended October 1, 2016 there were no shares issued and during the quarter ended September 26, 2015 the Company issued 6,000 shares as a result of option exercises. During the quarter ended October 1, 2016 1,200 options expired. No options expired during the quarter ended September 26, 2015.

During the quarter ended October 1, 2016 there were no shares repurchased. During the quarter ended September 26, 2015 the Company repurchased 3,923 shares from employees to facilitate their exercise of stock options.

During the three and nine months ended October 1, 2016 the Company recognized approximately \$37 thousand and \$153 thousand, respectively as share-based compensation expense related to previously granted shares under the Plan. A tax benefit of approximately \$3 thousand was recognized as additional paid in capital in the nine months ended October 1, 2016 resulting from the excess tax benefit of option exercises.

During the three and nine months ended September 26, 2015 the Company recognized approximately \$84 thousand and \$227 thousand, respectively as share-based compensation expense related to previously granted shares under the Plan. A tax benefit of approximately \$49 thousand was recognized as additional paid in capital in the nine months ended September 26, 2015 resulting from the excess tax benefit of option exercises.

(5) Inventories

Inventories consist of the following:

	October 1, 2016	December 26, 2015
Raw materials	\$515,692	\$670,318
Work in process	1,301,547	970,598
Finished goods	810,182	1,447,028
Total inventory	2,627,421	3,087,944
Reserve for obsolescence	(485,500)	(455,500)
Inventories, net	\$2,141,921	\$2,632,444

(6) Accrued Expenses

Accrued expenses consist of the following:

	October 1, 2016	December 26, 2015
Accrued legal and accounting	\$95,324	\$101,000
Accrued payroll	352,272	666,846
Accrued other	161,352	164,070

\$608,948 \$931,916

(7) Line of Credit and Equipment Lease Facility Agreements

In May 2016, the Company renewed its \$2 million revolving line of credit (“LOC”) and \$500 thousand of an equipment finance facility (“Lease Line”) with Santander Bank. Both agreements mature in May 2017. The LOC is secured by the accounts receivable and other assets of the Company, has an interest rate of prime and a one-year term. Under the terms of the agreement, the Company is required to maintain its operating accounts with Santander Bank. The LOC and the Lease Line are cross defaulted and cross collateralized. The Company is also subject to certain financial covenants within the terms of the LOC that require the Company to maintain a targeted coverage ratio as well as targeted debt to equity and current ratios. At October 1, 2016, the Company was in compliance with all existing covenants. At October 1, 2016, the Company had not utilized the equipment finance facility and therefore had \$500 thousand available. At October 1, 2016 the Company had no borrowings under this LOC and its borrowing base at the time would have permitted an additional \$1,229 thousand to have been borrowed.

(8) Income Taxes

The Company has a current and non-current deferred tax asset aggregating \$2,390,563 and \$2,150,749 on the Company’s balance sheet at October 1, 2016 and December 26, 2015, respectively. A valuation allowance is required to be established or maintained when it is "more likely than not" that all or a portion of deferred tax assets will not be realized. The Company believes that it will generate sufficient future taxable income to realize the tax benefits related to the remaining deferred tax assets and as such no valuation allowance has been provided against the deferred tax asset. At the end of 2015 the Company had utilized all of its net operating loss carryforwards.

The Company recorded a tax benefit of \$146,440 and \$177,720 for federal income taxes and a tax benefit of \$50,460 and \$59,280 for state income taxes during the three and nine months ended October 1, 2016, respectively.

The Company recorded a tax expense of \$5,000 and \$100,520 for federal income taxes and a tax expense of \$2,000 and \$28,980 for state income taxes during the three and nine months ended September 26, 2015, respectively.

(9) Commitments

The Company entered into a 10-year lease for the Norton facilities effective on March 1, 2006. The leased facilities comprise approximately 38 thousand square feet. In January 2016 this lease was amended to extend the lease to

February 28, 2017. As part of the agreement the Company obtained two, one-year options which enable the Company to continue to lease through February 28, 2019. In June 2016 the Company exercised the option to extend the lease through February 28, 2018. The lease is a triple net lease wherein the Company is responsible for payment of all real estate taxes, operating costs and utilities. The Company also has an option to buy the property and a first right of refusal during the term of the lease. Annual rental payments are \$100 thousand in year one increasing to \$152 thousand at the end of the extended term.

In February 2011, the Company entered into a lease for an additional 13.8 thousand square feet in Attleboro, MA. The lease term is for one year and has an option to extend the lease for five additional one-year periods. Monthly rent, which includes utilities, is \$6,900. The Company renewed the lease in 2013 for one additional year and also obtained two years of additional options which could extend the Company use through February 2019. In October 2015, the Company exercised its option to extend the lease through the end of February 2017.

ITEM 2 MANAGEMENTS DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of financial condition and results of operations is based upon and should be read in conjunction with the financial statements of the Company and notes thereto included in this report and the Company's Annual Report on Form 10-K for the year ended December 26, 2015.

Forward-Looking Statements