

MICROPAC INDUSTRIES INC  
Form 10-K  
February 16, 2016

United States Securities and Exchange Commission  
WASHINGTON, D.C.20549

FORM 10-K

(Mark One)

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended November 30, 2015

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 000-5109

Micropac Industries, Inc.  
(Exact name of registrant as specified in charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

75-1225149  
(I.R.S. Employer Identification  
No.)

905 E. Walnut Street, Garland,  
TX  
(Address of principal executive  
offices)

75040  
(Zip Code)

972/272-3571  
(Telephone No.)

Securities Registered Pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
None	N/A

Securities Registered Pursuant to Section 12(g) of the Act:

Common stock, par value \$0.10 per share  
(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 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 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, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" 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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant as of May 30, 2015 representing the last business day of the registrant's most recently completed second fiscal quarter, was approximately \$5,360,000, The number of shares of the registrant's common stock, \$0.10 par value, outstanding as of February 15, 2016 was 2,578,315.

#### DOCUMENTS INCORPORATED BY REFERENCE

The definitive proxy statement to be filed with the Securities and Exchange Commission relating to the registrant's Annual Meeting of Shareholders, to be held March 11, 2016 is incorporated by reference in Part III to the extent described therein.

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## PART I

### Item 1. Business

#### INTRODUCTION

Micropac Industries, Inc. (the “Company”), a Delaware corporation, manufactures and distributes various types of hybrid microelectronic circuits, solid state relays, power controllers, and optoelectronic components and assemblies. The Company’s products are used as components in a broad range of military, space and industrial systems, including aircraft instrumentation and navigation systems, power supplies, electronic controls, computers, medical devices, and high-temperature (200o C) products.

The Company’s facilities are certified and qualified by the Defense Logistics Agency (DLA) to MIL-PRF-38534 (class K-space level), MIL-PRF-19500 JANS (space level), and MIL-PRF-28750 (class K-space level) and is certified to ISO 9001-2002. Micropac is a National Aeronautics and Space Administration (NASA) core supplier, and is registered to AS9100-Aerospace Industry standard for supplier certification. The Company has UL approval on our industrial power controllers.

The Company’s core technology is the packaging and interconnecting of multi-chip microelectronics modules. Other technologies include light emitting and light sensitive materials and products, including light emitting diodes and silicon phototransistors used in the Company’s optoelectronic components and assemblies.

The business of the Company was started in 1963 as a sole proprietorship. On March 3, 1969, the Company was incorporated under the name of “Micropac Industries, Inc.” in the state of Delaware. The stock was publicly held by 470 shareholders on November 30, 2015.

#### PRODUCTS AND TECHNOLOGIES

The Company’s products are either custom (being application-specific circuits designed and manufactured to meet the particular requirements of a single customer) or standard proprietary components. Custom-designed components accounted for approximately 42% of the Company’s sales for the fiscal year ended November 30, 2015, and were 44% for fiscal 2014. Standard components accounted for approximately 58% of the Company’s sales for the fiscal year ended November 30, 2015, and were 56% for fiscal 2014.

The Company provides power management and controls, sensors and displays, and optocouplers products, components and assemblies and offers a wide range of products sold to the industrial, medical, military, aerospace and space markets.

The power management and controls technologies, including custom microcircuits, solid state relays, power operational amplifiers, and regulators accounted for 32% of the Company’s business in 2015 compared to 30% in 2014. Sensors and displays accounted for 33% of the Company’s business and the optocouplers product accounted for 35% of the Company’s business in 2015, compared to 41% and 29% in 2014, respectively.

The Company’s basic products and technologies include:

- Custom design hybrid microelectronic circuits
- Solid state relays and power controllers
- Custom optoelectronic assemblies and components
- Optocouplers

- Light-emitting diodes
- Hall-Effect sensors
- Displays
- Power operational amplifiers
- Fiber optic components and assemblies
- High temperature (200° C) products
- Radiation tolerant electronics

Micropac's products are primarily sold to original equipment manufacturers (OEM's) who serve the following major markets:

- Military/Aerospace – aircraft instrumentation, guidance and navigations systems, control circuitry, power supplies, laser positioning
- Space – control circuitry, power monitoring and sensing
- Industrial – power control equipment, robotics

The Company has two provisional patents. The Company has no licenses, franchises or labor contracts. The Company's trademark "Mii" is registered with the U.S. Patent and Trademark Office.

Sales of our products internationally are subject to government regulations, including export control regulations of the U.S. Department of State and Department of Commerce. Violation of these regulations by the Company could result in monetary penalties and denial of export privileges. The Company is not aware of any violations of export control regulations or any other applicable government regulations.

Five of the Company's principal product families require government approval. Further, a significant portion of our business is military and is dependent on maintaining our facility certifications to MIL-PRF-38534, MIL-PRF-19500 and MIL-PRF-28750. In addition, several customers require the Company maintain ISO 9001-2002 certifications. We expect to maintain these certifications and qualifications; however, the loss of any of these certifications would have a significant negative impact on our business.

Government regulations impose certain controls on chemicals used in electronics and semiconductor manufacturing. Micropac has obtained all the necessary environmental permits, and routinely monitors and reports the wastewater stream results to the local governing agency. Micropac is classified as a small generator of hazardous waste, and the annual cost of complying with the regulations is minimal.

In 2015, the Company's investment in technology through research and development, which was expensed, totaled approximately \$1,707,000 (\$1,856,000 in 2014). The Company's research and development expenditures were directed primarily toward standard proprietary power management products, including industrial power controllers and DC-DC converters, fiber optic transceivers, high voltage optocouplers and continued product development and improvement associated with the Company's space level and other high reliability products.

In addition to the Company's investment in research and development, various customers paid the Company approximately \$650,000 in non-recurring engineering revenue with costs recorded within cost of goods sold associated with the development of custom products for specific applications.

The Company provides a one year warranty from the date of shipment to the original purchaser. The Company is obligated under this warranty to either replace or repair defective goods or refund the purchase price paid by the buyer.

## CUSTOMERS

The Company's products are marketed throughout the United States and in Western Europe, through a direct technical sales staff, independent representatives and independent stocking distributors. Approximately 23% of the sales for fiscal year 2015 (17% in 2014) were to international customers. Sales to Western European customers are made by independent representatives under the coordination of the Company's office in Bremen, Germany.

Sales through the Company's distribution channels were \$6,535,000 in 2015 compared to \$4,452,000 in 2014, or 33% and 23% of sales, respectively.

The Company's major customers include contractors to the United States government. Sales to these customers for the Department of Defense (DOD) and NASA contracts accounted for approximately 57% of the Company's revenues in 2015 compared to 57% in 2014.

The Company's major customers are Lockheed Martin, Northrop Grumman, Rockwell, Goodrich, Raytheon, and L-3. One customer accounted for 12% of the Company's sales during 2015 and no customer accounted for 10% or more of the Company's sales in 2014.

#### BACKLOG

At November 30, 2015, the Company had a backlog of unfilled orders totaling approximately \$18,925,000 compared to approximately \$21,175,000 at November 30, 2014. The Company expects to complete and ship the majority of its November 30, 2015 backlog during fiscal 2016.

## EMPLOYEES

At November 30, 2015, the Company had 124 full-time employees (compared to 116 at November 30, 2014), of which 22 were executive and managerial employees, 31 were engineers and quality-control personnel, 9 were clerical and administrative employees, and 62 were production personnel. None of the Company's employees are covered by collective bargaining agreements.

The Company is an equal opportunity employer. It is the Company's policy to recruit, hire, train and promote personnel in all job classifications, without regard to race, religion, color, national origin, sex or age. Above and beyond non-discrimination, we are committed to an Affirmative Action Program, dedicated to the hiring, training, and advancement within the Company of minority group members, women, veterans, and handicapped individuals.

## COMPETITION

The Company competes with two or more companies with respect to each of its major products. Some of these competitors are larger and have greater capital resources than the Company. Management believes the Company's competitive position is favorable with regard to our product reliability and integrity, past performance, customer service and responsiveness, timely delivery and pricing; however, no assurance can be given that the Company can compete successfully in the future.

There are approximately 51 independent manufacturing companies who are certified to supply microcircuits to MIL-PRF-38534 or supply semiconductors to MIL-PRF-19500, in addition to OEM's, who manufacture hybrid microcircuits for their internal needs. Micropac may compete with all of these for hybrid microcircuit, power management and optoelectronics business. Some of the Company's primary competitors are MS Kennedy, Avago, Isolink, and International Rectifier.

## SUPPLY CHAIN

The parts and raw materials for the Company's products are generally available from more than one source. Except for certain optoelectronic products, the Company does not manufacture the basic parts or materials used in production of its products. From time to time, the Company has experienced difficulty in obtaining certain materials when needed. The Company's inability to secure materials for any reason could have adverse effects on the Company's ability to deliver products on a timely basis and could result in loss of customers or sales. However, the Company has not been materially affected by such shortages. The Company uses capacitors, active semiconductor devices (primarily in chip form), hermetic packages, ceramic substrates, resistor inks, conductor pastes, precious metals and other materials in its manufacturing operations. The Company's delivery commitments to customers allow for adequate lead times for production of the products including lead time for order and receipt from the supply chain.

Some of the Company's primary suppliers are NTK Technologies, Electrovac, Schott Glass, Semi-Dice, Micross Components, Cobhanm Rad Solutions, and Materion Advanced Materials.

### Item Risk Factors 1A.

This annual report on Form 10-K contains forward-looking statements that are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Actual results could differ materially. Investors are warned that forward-looking statements involve risks and unknown factors including, but not limited to, customer cancellation or rescheduling of orders, problems affecting delivery of vendor-supplied raw materials and components,



unanticipated manufacturing problems and availability of direct labor resources.

The Company produces silicon phototransistors and light emitting diode die for use in certain military, standard and custom products. Fabrication efforts sometimes may not result in successful results, limiting the availability of these components. Competitors offer commercial level alternatives and our customers may purchase our competitors' products if the Company is not able to manufacture the products using these technologies to meet the customer demands.

The Company disclaims any responsibility to update the forward-looking statements contained herein, except as may be required by law.

#### Majority shareholder ability to control the election of the Board of Directors

The Company's majority shareholder, Mr. Heinz-Werner Hempel, established a partnership organized under the laws of Germany, which owns 1,952,577 shares or 75.7% of the outstanding voting shares. Mr. Hempel, through the partnership, has the ability to control the election of the Company's Board of Directors and elect individuals who may be more sympathetic to such majority shareholder's desires and not necessarily sympathetic to the desires of minority shareholders as to the policies and directions of the Company. However, the ability to control the election of the Board of Directors does not modify the fiduciary duties of the Board of Directors to represent the interests of all shareholders.

#### Availability of public shares for purchase and sale

A small number of shares are available for public purchase and sale. As a result, the Company's reported share price may be subject to extreme fluctuations due in part to the small number of shares traded at any time.

#### Pricing pressures from customers for reduction in selling prices

The Company continues to experience pricing pressures from some of its OEM customers. In some cases, the Company's customers request the review of pricing for possible reduction in selling price on future orders. This requires the Company to improve its productivity and to request similar price reductions from its supplier chain. If one or both of the approaches by the Company does not succeed, the Company could be required to reduce the selling price on future orders, reducing the product gross margins and affecting the Company's net earnings in order to receive future orders from the customer. However, the Company has no agreement that requires a reduction in the selling price on any current customer order. All contracts are firm fixed pricing.

#### Insurance coverage and exposure to substantial claims or liabilities

The Company operates manufacturing facilities in Garland, Texas and subcontracts portions of the Company's manufacturing to a contract manufacturer in Juarez, Mexico. These facilities use industrial machines and chemicals that could provide risks of personal injury and/or property damage. There is no assurance that accidents will not occur. If accidents do occur, the Company could be exposed to substantial liability. The Company maintains worker's compensation insurance and general liability insurance for protection of its employees and for protection of the Company's assets in Garland, Texas and for equipment and inventory located at the contract manufacturer in Juarez, Mexico. In addition to the basic policies mentioned, the Company maintains an umbrella insurance policy. The Company reviews all insurance coverage on an annual basis, and makes any necessary adjustments based on risk assessment and changes in its business. In the opinion of the Company's management, and its insurance advisors, the Company is adequately insured; however, the Company's financial position could be materially affected by claims not covered or exceeding coverage currently carried by the Company.

#### The Company is subject to numerous environmental regulations and changes in government policy

The Company is subject to governmental regulations pertaining to the use, storage, handling and disposal of hazardous substances used in connection with its manufacturing activities. Failure of the Company to control all activities dealing with hazardous chemicals could subject the Company to significant liabilities or could cause the Company to cease its manufacturing activities.

The Company could be adversely affected by changes in laws and regulations made by U.S. and non U.S. governments and agencies dealing with foreign shipments. Changes by regulatory agencies dealing with environmental issues could affect the cost of the Company's products and make it hard for the Company to be

competitive with larger companies.

Sales of our products internationally are subject to government regulations, including export control regulations of the U.S. Department of State and Department of Commerce. Violation of these regulations by the Company could result in monetary penalties and denial of export privileges. The Company is not aware of any violations of export control regulations or any other applicable government regulations.

The Company is subject to the Foreign Corrupt Practices Act (the "FCPA"), which generally prohibits U.S. companies and their intermediaries from making improper payments to foreign officials for the purpose of obtaining or retaining business. Any violation of the FCPA or similar laws and regulations could result in significant expenses, divert management attention, have a material adverse effect on our business, our financial condition and our results of operations and otherwise have a negative impact on the Company and its reputation.

#### Product liability claims

The use of the Company's products in commercial or government applications may subject the Company to product liability claims. Although the Company has not experienced any product liability claims, the sale of any product may provide risk of such claims. Product liability claims brought against the Company could have a material adverse effect on the Company's operating results and financial condition.

#### Component shortages from suppliers could affect ability to manufacture products or delay shipments to customers

The Company relies on suppliers to deliver quality raw materials in a timely and cost effective manner. Most of the materials and components are generally available from multiple sources; however, from time to time vendors do not deliver the product as needed due to manufacturing problems or a decision to discontinue that product. Such interruption of supply or price increases could have a material adverse effect on the Company's operations; however, the Company is not currently impacted by materials shortages.

#### The ability to develop new products and technologies used in the military, space or aerospace markets

The Company's base products and technologies generally have long life cycles. The Company's products are primarily used in military, space or aerospace applications, which also have long life cycles. There can be no assurance that the Company will be able to define, develop and market new products and technologies on a timely and cost effective basis. Failure to respond to our customers' requirements and to our competitors' progress in technological changes could have a material adverse effect on the Company's business.

#### General economic downturn

The Company cannot assure you that our business will not be adversely affected as a result of an industry or general economic downturn. If the Company's supply chain is adversely affected by the current economic downturn, this could result in the Company's inability to secure materials and could have adverse effects on the Company's ability to deliver products on a timely basis.

#### The Company has potential warranty obligations

The Company provides a one year warranty from the date of shipment to the original purchaser. The Company is obligated under this warranty to either replace or repair defective goods or refund the purchase price paid by the buyer. An unexpected number of warranty claims could negatively impact the profitability of the Company.

#### The Company may default on its line of credit

The Company currently has an existing line of credit with a Texas banking institution. In connection therewith, the Company is obligated to maintain certain minimum financial requirements in order to receive advances therefrom. The Company is currently in compliance with such financial requirements, but there is no guarantee that the Company will remain in compliance. If the Company does not maintain compliance with each of the requirements, its ability to receive advances from the line of credit will be impaired.

#### The Company is heavily dependent on a few major customers

The Company's major customers include contractors to the United States government. Sales to these customers for the Department of Defense (DOD) and NASA contracts accounted for approximately 57% of the Company's revenues in 2015 compared to 57% in 2014. The Company's major customers are Lockheed Martin, Northrop Grumman,

Rockwell, Goodrich, Raytheon, and L-3. The Company's top 10 customers accounted for 41% of the Company's sales during 2015 and 47% of the Company's sales during 2014.

Item Unresolved Staff Comments  
1B.

Not applicable.

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Item 2. Properties

The Company occupies approximately 37,000 square feet of manufacturing, engineering and office space in Garland, Texas. The Company owns 31,200 square feet of that space and leases an additional 4,800 square feet. The Company considers its facilities adequate for its current level of operations.

The Company also subcontracts some manufacturing to Inmobiliaria San Jose De Ciudad Juarez S.A. DE C.V., a maquila contract manufacturer in Juarez, Mexico. The Company owns all equipment and inventory with temporary importation into Mexico under the maquila rules of Mexico. The Company does not lease or own any real property in Mexico.

The Company employs a sales team in Bremen, Germany who coordinates sales to Western European customers made by independent representatives. The sales manager maintains an office in a private residence. The Company does not lease or own any real property in Germany, or any other foreign country.

Item 3. Legal Proceedings

The Company is not involved in any material current or pending legal proceedings.

Item 4. Mine Safety Disclosure

None

PART II

Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information, Holders and Dividends

On February 15, 2016, there were 470 shareholders of record of the Company’s common stock. The stock of the Company is closely held; and, therefore, certain shareholders have the ability to significantly influence decisions. The Company’s common stock is quoted on the OTC Bulletin Board under the symbol “MPAD.OB”. The following sets forth the high and low sell price for each quarter during the last two fiscal years:

	HIGH	LOW
Fiscal Year Ended November 30, 2015	PRICE	PRICE
Fourth Quarter	\$10.25	\$8.75
Third Quarter	\$10.25	\$8.61
Second Quarter	\$10.50	\$8.55
First Quarter	\$9.25	\$8.01
Fiscal Year Ended November 30, 2014		
Fourth Quarter	\$9.00	\$8.00

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Third Quarter	\$9.20	\$8.35
Second Quarter	\$9.95	\$7.80
First Quarter	\$8.35	\$7.00

During the three month period ended November 30, 2015, approximately 10,000 shares of the Company's common stock were traded in the over-the-counter market at a price range of \$10.25 to \$8.75 per share. For the two year period ending November 30, 2015, approximately 241,300 shares of the Company's common stock were traded in the over-the-counter market at prices ranging from a low of \$7.00 to a high of \$10.50. Due to this average monthly volume of approximately 10,000 shares of common stock being publicly bought and sold during this two year period, the Company does not believe this share trading volume results in prices which represent the market value of the Company's common stock held by non-affiliates.

On December 17, 2013, the Board of Directors of Micropac Industries, Inc. approved the payment of a special dividend of \$0.10 per share for shareholders of record as of January 15, 2014. The dividend was paid to shareholders on February 12, 2014.

On December 16, 2014, the Board of Directors of Micropac Industries, Inc. approved the payment of a special dividend of \$0.10 per share for shareholders of record as of January 12, 2015. The dividend was paid to shareholders on February 10, 2015.

On December 15, 2015, the Board of Directors of Micropac Industries, Inc. approved the payment of a \$0.10 per share special dividend to all shareholders of record as of January 12, 2016. The dividend was paid to shareholders on February 11, 2016.

Securities Issued under Equity Compensation Plan

None

Item 6. Selected Financial Data

Not applicable.

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

Twelve Months Ended	
11/30/15	11/30/14