

Universal Power Group, Inc.

Auditor's Report and Consolidated Financial Statements

December 31, 2015 and 2014



Universal Power Group, Inc.
December 31, 2015 and 2014

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Independent Auditor's Report

Board of Directors
Universal Power Group, Inc.
Coppell, Texas

We have audited the accompanying consolidated financial statements of Universal Power Group, Inc. and its subsidiaries, which comprise the consolidated balance sheets as of December 31, 2015 and 2014, and the related consolidated statements of income, changes in shareholders' equity and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Board of Directors
Universal Power Group, Inc.
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Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Universal Power Group, Inc. and its subsidiaries as of December 31, 2015 and 2014, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

BKD, LLP

Dallas, Texas
August 5, 2016

Universal Power Group, Inc.

Consolidated Balance Sheets

December 31, 2015 and 2014

(in thousands, except share information)

Assets

	2015	2014
Current Assets		
Cash and cash equivalents	\$ 205	\$ 399
Accounts receivable		
Trade, net of allowances of \$145 and \$156, respectively	16,092	12,063
Other	142	282
Inventories – finished goods, net of allowances for obsolescence of \$687 and \$583, respectively	24,235	24,178
Current deferred tax assets	706	655
Prepaid expenses and other current assets	1,387	748
Total current assets	42,767	38,325
Property and Equipment, at Cost		
Logistics and distribution systems	1,932	1,932
Machinery and equipment	1,216	490
Furniture and fixtures	905	881
Leasehold improvements	1,121	968
Vehicles	24	24
	5,198	4,295
Less accumulated depreciation and amortization	(3,292)	(2,913)
	1,906	1,382
Other Assets		
Goodwill	9,440	1,387
Intangible assets, net	551	311
Other	160	160
Noncurrent deferred tax assets	241	244
	10,392	2,102
Total assets	\$ 55,065	\$ 41,809

Universal Power Group, Inc.
Consolidated Balance Sheets (Continued)
December 31, 2015 and 2014
(in thousands, except share information)

Liabilities and Shareholders' Equity

	<u>2015</u>	<u>2014</u>
Current Liabilities		
Line of credit	\$ 15,000	\$ 4,568
Accounts payable	10,385	8,455
Accrued liabilities	884	515
Income tax payable	-	259
Current portion of capital lease and note obligations	571	571
Current portion of deferred rent	19	92
	<u>26,859</u>	<u>14,460</u>
Total current liabilities	26,859	14,460
Long-term Liabilities		
Deferred rent, less current portion	1,123	1,131
Capital leases and note obligations, less current portion	3,143	2,333
	<u>31,125</u>	<u>17,924</u>
Total liabilities	31,125	17,924
Shareholders' Equity		
Common stock – \$0.01 par value, 50,000,000 shares authorized, 5,020,000 shares issued and outstanding	50	50
Additional paid-in capital	16,468	16,468
Retained earnings	7,422	7,367
	<u>23,940</u>	<u>23,885</u>
Total shareholders' equity	23,940	23,885
Total liabilities and shareholders' equity	<u>\$ 55,065</u>	<u>\$ 41,809</u>

Universal Power Group, Inc.
Consolidated Statements of Income
Years Ended December 31, 2015 and 2014
(in thousands)

	<u>2015</u>	<u>2014</u>
Net Sales	\$ 90,947	\$ 88,613
Cost of Sales	<u>73,961</u>	<u>72,729</u>
Gross Profit	16,986	15,884
Operating Expenses	<u>15,621</u>	<u>14,126</u>
Operating Income	1,365	1,758
Other Income (Expense)		
Interest expense	(413)	(238)
Other, net	<u>13</u>	<u>15</u>
Total other expense, net	<u>(400)</u>	<u>(223)</u>
Income Before Provision for Income Taxes	965	1,535
Provision for Income Taxes	<u>(410)</u>	<u>(691)</u>
Net Income	<u><u>\$ 555</u></u>	<u><u>\$ 844</u></u>
Net Income Per Share		
Basic	\$ 0.11	\$ 0.17
Diluted	\$ 0.11	\$ 0.17
Weighted Average Shares Outstanding		
Basic	5,020	5,020
Diluted	5,111	5,098

Universal Power Group, Inc.
Consolidated Statements of Changes in Shareholders' Equity
Years Ended December 31, 2015 and 2014
(in thousands)

	Common Stock		Additional Paid-in Capital	Retained Earnings	Total
	Shares	Amount			
Balance, January 1, 2014	5,020	\$ 50	\$ 16,434	\$ 6,523	\$ 23,007
Stock-based compensation expense	-	-	34	-	34
Net income	-	-	-	844	844
	5,020	50	16,468	7,367	23,885
Balance, December 31, 2014	5,020	50	16,468	7,367	23,885
Dividends paid	-	-	-	(500)	(500)
Net income	-	-	-	555	555
	5,020	50	16,468	7,422	23,940
Balance, December 31, 2015	5,020	\$ 50	\$ 16,468	\$ 7,422	\$ 23,940

Universal Power Group, Inc.
Consolidated Statements of Cash Flows
Years Ended December 31, 2015 and 2014
(in thousands)

	<u>2015</u>	<u>2014</u>
Operating Activities		
Net income	\$ 555	\$ 844
Items not requiring (providing) cash		
Depreciation and amortization	499	361
Provision for doubtful accounts	128	59
Provision for obsolete inventory	203	681
Deferred income taxes	(48)	329
Stock-based compensation	-	34
Changes in operating assets and liabilities, net of acquisition		
Accounts receivable – trade	(1,911)	(110)
Accounts receivable – other	140	(184)
Inventories	2,567	108
Income taxes receivable/payable	-	702
Prepaid expenses and other assets	(333)	320
Accounts payable	241	738
Accrued liabilities	(253)	(539)
Deposits	(259)	-
Deferred rent	(81)	(66)
	<u>1,448</u>	<u>3,277</u>
Net cash provided by operating activities		
Investing Activities		
Purchase of property and equipment	(292)	(4)
Payment for iTech acquisition, net of cash acquired	(12,092)	-
	<u>(12,384)</u>	<u>(4)</u>
Net cash used in investing activities		
Financing Activities		
Net activity on line of credit	10,432	(3,075)
Dividends paid	(500)	-
Proceeds from note obligations	4,000	-
Payments on capital lease and note obligations	(3,190)	(979)
	<u>10,742</u>	<u>(4,054)</u>
Net cash provided by (used in) financing activities		
Net Decrease in Cash and Cash Equivalents	(194)	(781)
Cash and Cash Equivalents, Beginning of Year	<u>399</u>	<u>1,180</u>
Cash and Cash Equivalents, End of Year	<u>\$ 205</u>	<u>\$ 399</u>
Supplemental Disclosures		
Income taxes paid (received)	\$ 714	\$ (322)
Interest paid	\$ 379	\$ 241

The Company purchased all of the membership interests of iTech for \$12,128. In conjunction with the acquisition, liabilities were assumed as follows:

Fair value of assets acquired	\$ 14,438
Cash paid for the membership interests	<u>(12,128)</u>
Liability assumed	<u>\$ 2,310</u>

Universal Power Group, Inc.
Notes to Consolidated Financial Statements
December 31, 2015 and 2014

Note 1: Organization

Universal Power Group, Inc. (UPG or the Company), a Texas corporation, is a distributor and supplier of batteries and related power accessories to a diverse range of industries, a provider of third-party fulfillment and logistics services, and value-added solutions. The Company's primary logistics center is located in Coppell, Texas, and regional logistic centers are located in Las Vegas, Nevada and Atlanta, Georgia. The Company's customers are primarily located in the United States. A small portion of the Company's sales is to customers located in the United Kingdom, Australia, Ireland, Japan, China, Canada and Latin America.

Until December 20, 2006, the Company was a wholly owned consolidated subsidiary of Zunicom, Inc. (Zunicom), a Texas corporation, whose stock is quoted on the OTC Bulletin Board under the symbol ZNCM.OB. On December 20, 2006, the U.S. Securities and Exchange Commission (SEC) declared effective a registration statement filed by the Company registering the sale of 3,000,000 shares of its common stock, including 1,000,000 shares owned by Zunicom (IPO). As a result of the IPO, Zunicom's interest in the Company was reduced to 40%. Zunicom no longer owns a controlling interest in UPG; however, as the largest shareholder, Zunicom does have significant influence over UPG.

On April 20, 2011, the Company completed an acquisition of substantially all of the business assets of Progressive Technologies, Inc. ("PTI"), a North Carolina company established in 1985 that designs and builds custom battery packs. PTI is a manufacturer of lithium-ion battery packs, among other chemistries, expanding the Company's position in power solutions for the future in medical and other market segments. PTI is ISO 9001:2008 certified. On September 1, 2011, Progressive Technologies, Inc. changed its legal name to ProTechnologies, Inc.

On January 9, 2013, the Company became the sole member of a newly formed entity, SAM Security, LLC (SAM). SAM provided a do-it-yourself (DIY) home security system to a large retailer.

On October 31, 2013, the Company decided to voluntarily withdraw its common stock from trading on the NYSE MKT exchange and completed this de-listing with the filing of Form 25. In addition, on November 12, 2013, the Company completed the certification and notice of termination of registration and suspension of duty to file reports with the SEC with the filing of Form 15. At that time, the Company ceased filing periodic reports pursuant to the *Securities Exchange Act of 1934, as amended* (the Exchange Act). The Company's common stock is currently quoted on the over-the-counter market under the symbol UPGI.

On April 30, 2015, the Company completed an acquisition of all the membership interests of Intelligent Technologies, LLC (iTech), a California company and a manufacturer of market-leading portable power solutions to performance-critical industries and Fortune 500 companies. iTech provides innovative design and manufacture of smart lithium-ion batteries, chargers, docking stations and power sub-systems for performance critical applications in the handheld electronics, medical, intrinsic safety, industrial and communications markets. iTech is ISO 9001:2008 certified, ISO 13845 certified, and FDA registered.

Universal Power Group, Inc.
Notes to Consolidated Financial Statements
December 31, 2015 and 2014

Note 2: Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries PTI, iTech, and SAM Security, LLC. All significant intercompany accounts and transactions have been eliminated in consolidation.

Cash and Cash Equivalents

The Company considers all liquid investments with original maturities of three months or less to be cash and cash equivalents.

Accounts Receivable

Trade accounts receivable are stated at the amount the Company expects to collect. The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. Management considers the following factors when determining the collectibility of specific customer accounts: customer credit-worthiness, past transaction history with the customer, current economic industry trends and changes in customer payment terms and financial condition. If the financial condition of the Company's customers were to deteriorate, adversely affecting their ability to make payments, additional allowances would be required. Based on management's assessment, the Company provides for estimated uncollectible amounts through a charge to earnings and a credit to a valuation allowance. Balances that remain outstanding after the Company has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable.

Inventories

Inventories consist of finished goods, primarily of batteries and security products related to the Company's third-party fulfillment services and materials used in the assembly of batteries into "packs" and "charging stations." All items are stated at the lower of cost, determined using the average cost or standard cost methods by specific item or market. The Company performs periodic evaluations based upon business trends and expected future demands, to specifically identify obsolete, slow-moving and non-salable inventory.

Property and Equipment

Property and equipment are carried at cost less applicable depreciation and amortization. Depreciation and amortization of property and equipment is provided for using the straight-line method over the estimated useful lives of the assets ranging from 3 – 10 years. Leasehold improvements are amortized on a straight-line basis over the shorter of the remaining lease term or the estimated useful life of the related asset. Equipment leased under capital leases is amortized over the service life of the related asset or term of the lease, whichever is shorter. Depreciation expense for the years ended December 31, 2015 and 2014, totaled approximately \$381,000 and \$256,000, respectively.

Universal Power Group, Inc.
Notes to Consolidated Financial Statements
December 31, 2015 and 2014

Goodwill

Goodwill is evaluated annually for impairment or more frequently if impairment indicators are present. A qualitative assessment is performed to determine whether the existence of events or circumstances leads to a determination that it is more-likely-than-not the fair value is less than the carrying amount, including goodwill. If, based on the evaluation, it is determined to be more-likely-than-not that the fair value is less than the carrying value, then goodwill is tested further for impairment. If the implied fair value of goodwill is lower than its carrying amount, a goodwill impairment is indicated and goodwill is written down to its implied fair value.

Intangible Assets

Intangible assets consist primarily of intellectual property, non-competes, tradename and customer lists. These assets are carried at historical cost and are amortized over the estimated useful lives of the assets, which range from 1 – 20 years. Such assets are periodically evaluated as to the recoverability of their carrying values.

Income Taxes

The Company accounts for income taxes in accordance with income tax accounting guidance Accounting Standards Code (ASC) 740, *Income Taxes*. The income tax accounting guidance results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. The Company determines deferred income taxes using the liability method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax bases of assets and liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur. Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. Deferred tax assets are reduced by a valuation allowance if, based on the weight of evidence available, it is more-likely-than-not that some portion or all of a deferred tax asset will not be realized. The Company files consolidated income tax returns with its subsidiaries.

Impairment of Long-lived Assets

The Company evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimated future cash flows expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value. No asset impairment was recognized during the years ended December 31, 2015 and 2014.

Universal Power Group, Inc.
Notes to Consolidated Financial Statements
December 31, 2015 and 2014

Deferred Rent

The Company's operating leases for its primary office and various warehouse spaces contains free rent periods and contains predetermined fixed increases of the minimum rental rate during the initial lease term. For these leases, the Company recognizes rental expense on a straight-line basis over the minimum lease term and records the difference between the amounts charged to expense and the rent paid as deferred rent. In addition, one of the landlords provided certain allowances for leasehold improvements on some of the facilities which has been recorded as deferred rent and property and equipment. Deferred rent is amortized as an offset to rent expense over the term of the related lease.

Revenue Recognition

The Company recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed and determinable and collectability is reasonably assured.

The Company is a distributor and purchases both finished goods and components from domestic and international suppliers. The Company adds value to products and components by packaging them in customer specified "kits" or tailor made units that are convenient for the customer to order and ship. Additionally, the Company designs and assembles battery packs for custom applications by obtaining batteries and components and reconfiguring finished goods based upon customer specifications. The Company recognizes sales of finished goods at the time the customer takes title to the product.

The Company also offers "drop shipments" to customers whereby orders are taken for bulk quantities and the Company arranges for the delivery of the product directly from the vendor to the customer, reducing freight costs and wear and tear on the product from excessive handling. Revenues from drop shipment transactions are recognized on a gross basis at the time the customer takes title to the product, based on an analysis of the criteria defined for gross revenue reporting. Specifically, (i) the Company is the primary obligor; (ii) the Company has general and physical loss inventory risk; (iii) the Company has credit risk; (iv) in most cases, the Company has discretion in supplier selection and product specifications; and (v) the Company has reasonable latitude within economic constraints to negotiate prices and terms with its customers.

Post-shipment Obligations

The Company offers its customers a limited warranty for replacement of finished goods that have manufacturer's defect. Generally, the limited warranty period ranges from 90 days to three years. The most common types of warranty claims are for manufacturer's defect. The Company's written warranty is limited to the replacement value of the product purchased and does not cover the product the battery is intended to power. The Company's replacement rate is insignificant, and is therefore recorded when the warranty expense is incurred. If the Company determines that a shipment of product had a manufacturing defect, the Company has recourse with the manufacturer to recover the replacement costs incurred. The costs of isolated or individual instances of defects are borne by the Company. At December 31, 2015 and 2014, the Company has a warranty reserve of approximately \$10,000.

Universal Power Group, Inc.
Notes to Consolidated Financial Statements
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Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and 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. Actual results could differ from those estimates.

Advertising Costs

Advertising costs are charged to operations when incurred. Advertising expense totaled approximately \$345,000 and \$667,000 for the years ended December 31, 2015 and 2014, respectively.

Shipping and Handling Costs

Shipping and handling costs are charged to cost of sales in the accompanying consolidated statements of income.

Earnings Per Share

Basic earning per common share is computed by dividing net income applicable to common shareholders by the weighted average number of common shares outstanding during each year.

Diluted earnings per common share are computed by dividing net income by the weighted average number of common shares and common stock equivalents outstanding for the year. The Company's common stock equivalents include all dilutive common stock issuable upon exercise of outstanding stock options and warrants.

For the years ended December 31, 2015 and 2014, 661,250 stock options are excluded from the calculation of diluted earnings per share because they are anti-dilutive.

Stock Option Plan

At December 31, 2015 and 2014, the Company has a stock-based compensation plan, which is described more fully in *Note 6*.

Taxes Collected from Customers and Remitted to Governmental Authorities

Taxes collected from customers and remitted to governmental authorities are presented in the accompanying consolidated statements of income on a net basis.

Universal Power Group, Inc.
Notes to Consolidated Financial Statements
December 31, 2015 and 2014

Note 3: Line of Credit

The Company has a credit agreement with Comerica Bank (Comerica) under which it may borrow up to \$34,000,000, including a \$30,000,000 revolving line of credit (Credit Line) and \$4,000,000 term loan (Term Loan). All borrowings are secured by a first lien on all assets of the Company. In addition, the Company may request an increase in the maximum Credit Line to \$40,000,000. The borrowing availability is dependent upon the Company's level of accounts receivable and inventory. With respect to the interest rate for each borrowing, the Company has the option to choose a LIBOR-base rate or daily adjusted LIBOR-based rate plus an applicable LIBOR margin. Under the Credit Line, interest is payable monthly and the outstanding principal was originally due on December 20, 2016 (Maturity Date). The credit agreement was amended to extend the maturity date to December 2020. See *Note 12*. At December 31, 2015 and 2014, approximately \$15,000,000 and \$4,600,000, respectively, was outstanding under the Credit Line. The Credit Line was accruing interest at the rate of 2.49% and 2.04% per annum at December 31, 2015 and 2014, respectively.

The credit agreement contains customary negative covenants restricting the Company's ability to take certain actions without Comerica's consent, including incurring additional indebtedness, transferring or encumbering assets, and acquiring other businesses. If there is an "event of default," including failure to pay, bankruptcy, breach of covenants and breach of representations and warranties, all amounts outstanding under the credit agreement will become immediately due and payable. In addition, the Company must maintain certain financial covenants, measured on a quarterly basis. During the year ended December 31, 2015, the Company did not meet certain covenants and Comerica has formally waived the noncompliance of these covenants through June 2016.

Note 4: Note Obligation

Note obligation consist of the following at December 31, 2015 and 2014 (in thousands):

	<u>2015</u>	<u>2014</u>
Term loan with Comerica	\$ 3,714	\$ 2,904
Less current portion	<u>(571)</u>	<u>(571)</u>
Long-term portion of capital lease and note obligations	<u>\$ 3,143</u>	<u>\$ 2,333</u>

All borrowings under the credit agreement are secured by a first lien on all of the Company's assets. The note bears interest at the same rate as the Credit Line and is paid quarterly along with the quarterly principal payment of \$143,000, which is based on a seven year amortization period. The remaining loan balance is due in a balloon payment on the loan maturity date. At December 31, 2015 and 2014, the term loan was accruing interest at the rate of 2.49% and 2.04% per annum, respectively. The Term Loan originally matured on December 20, 2016. The credit agreement was amended to extend the maturity date to December 2020. See *Note 12*.

Universal Power Group, Inc.
Notes to Consolidated Financial Statements
December 31, 2015 and 2014

Aggregate annual maturities of the note obligation at December 31, 2015, are:

2016	\$	571
2017		571
2018		571
2019		571
2020		859
		<u>859</u>
	\$	<u>3,143</u>

Note 5: Income Taxes

The Company files income tax returns in the U.S. federal jurisdiction and various states.

Deferred tax assets and liabilities consist of the following at December 31, 2015 and 2014 (in thousands):

	<u>2015</u>	<u>2014</u>
Deferred tax assets, current		
Inventory obsolescence	\$ 234	\$ 198
Inventory capitalization	346	344
Allowance for doubtful accounts	4	-
Other	31	92
Accrued liabilities	<u>91</u>	<u>21</u>
Total deferred tax assets, current	<u>706</u>	<u>655</u>
Deferred tax assets(liabilities), noncurrent		
Intangible assets	(14)	84
Deferred rent	415	55
Stock-based compensation	1,005	1,005
Property and equipment	(397)	(132)
Valuation allowance	<u>(768)</u>	<u>(768)</u>
Total deferred tax assets, noncurrent	<u>241</u>	<u>244</u>
Net deferred tax assets	<u>\$ 947</u>	<u>\$ 899</u>

Universal Power Group, Inc.
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December 31, 2015 and 2014

The Company's provision for income taxes is comprised as follows for the years ended December 31, 2015 and 2014 (in thousands):

	2015	2014
Current federal income tax expense	\$ 380	\$ 249
Current state income tax expense	78	113
Deferred income tax expense (benefit)	<u>(48)</u>	<u>329</u>
Provision for income taxes	<u>\$ 410</u>	<u>\$ 691</u>

The Company's income tax expense from continuing operations for the years ended December 31, 2015 and 2014, differed from the statutory federal rate of 34% as follows (in thousands):

	2015	2014
Tax at statutory rate	\$ 328	\$ 522
Amounts not deductible for income tax purposes	60	50
State income taxes, net of federal income tax effect	52	74
Other	<u>(30)</u>	<u>45</u>
Income tax expense	<u>\$ 410</u>	<u>\$ 691</u>

In assessing the reliability of deferred tax assets, management considers whether it is more-likely-than-not that, some portion of the deferred tax asset will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible.

As of December 31, 2015, management could not determine based on weighing of objective evidence that it is more-likely-than-not, that all of the deferred tax assets will be realized. As a result, as of December 31, 2015, a valuation allowance of \$768,000 was recorded to reduce the deferred tax assets to the amount that is more-likely-than-not to be realized.

Note 6: Stock-based Compensation

Stock Options

In December 2006, the Company adopted, and its shareholders approved and ratified, the 2006 Stock Option Plan (Plan), the purpose of which is to attract and retain the personnel necessary for the Company's success. The Plan gives the Board of Directors (Board) the ability to provide incentives through grants of stock options, restricted stock awards and other types of equity-based incentive compensation awards to the Company's key employees, consultants and directors (other than directors that are not compensated for their time by the Company or receive only a director's fee). The Compensation Committee administers the Plan. Except as may otherwise be provided in the Plan, the Compensation Committee has complete authority and discretion to determine the terms of awards.

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The Plan authorizes the granting of options, including options that satisfy the requirements of Section 422 of the Internal Revenue Code (IRC) of 1986, as amended. The Compensation Committee will determine the period of time during which a stock option may be exercised, as well as any vesting schedule, except that no stock option may be exercised more than 10 years after its date of grant. The exercise price for shares of the Company's common stock covered by an incentive stock option cannot be less than the fair market value of the Company's common stock on the date of grant; provided that, that exercise of an incentive stock option granted to an eligible employee that owns more than 10% of the voting power of all classes of the Company's capital stock must be at least 110% of the fair market value of the Company's common stock on the date of grant.

The Plan also authorizes the grant of restricted stock awards on terms and conditions established by the Compensation Committee. The terms and conditions will include the designation of a restriction period during which the shares are not transferable and are subject to forfeiture.

The Board may terminate the Plan without shareholder approval or ratification at any time. Unless sooner terminated, the Plan will terminate in December 2016. The Board may also amend the Plan, provided that no amendment will be effective without approval of the Company's shareholders if shareholder approval is required to satisfy any applicable statutory or regulatory requirements.

If an award expires or terminates unexercised or is forfeited to the Company, or shares covered by an award are used to fully or partially pay the exercise price of an option granted under the Plan or shares are retained by the Company to satisfy tax withholding obligations in connection with an option exercise or the vesting of another award, those shares will become available for further awards under the Plan.

At December 31, 2015, common shares reserved for future issuance include 1,980,000 shares issuable under the Plan, as well as 20,000 shares issuable outside the Plan. At December 31, 2015, there are 1,488,933 options outstanding under the Plan and 491,067 options are available for future grants.

Valuation Assumptions

There were no options granted in 2015. The fair values of new option awards granted under the Plan were estimated at the grant date or modification date using a Black-Scholes option pricing model with the following assumptions for the fiscal year ended December 31, 2014:

Weighted-average assumptions used	
Expected dividend yield	0.00%
Risk-free interest rate	1.64%
Expected volatility	54%
Expected life (in years)	5
Weighted-average grant date fair value	\$ 0.94

Universal Power Group, Inc.
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Volatility for the year ended December 31, 2014, is computed using the volatility of the Company's common stock. The risk-free interest rate is based on the rates in effect on the grant date for U.S. Treasury instruments with maturities matching the relevant expected term of the award. Due to the limited trading of its equity shares and the lack of sufficient historical exercise data to provide a reasonable basis upon which to estimate expected term, the expected term is calculated using the simplified method for all options granted on each grant date.

Stock Incentive Plan Summary

Stock option activity under the Plan for the years ended December 31, 2015 and 2014, was as follows:

	Number of Shares	Weighted- Average Exercise Price
Options outstanding at January 1, 2014	1,462,569	\$ 3.44
Granted	30,000	1.96
Expired	<u>(3,000)</u>	1.54
Options outstanding at December 31, 2014	1,489,569	3.41
Granted	-	-
Expired	<u>(636)</u>	1.54
Options outstanding and exercisable at December 31, 2015	<u>1,488,933</u>	\$ 3.41

At December 31, 2015, all outstanding options under the Plan were fully vested and exercisable with no remaining unrecognized compensation expense. At December 31, 2015, the weighted-average remaining contractual term for all outstanding options is 2.66 years.

Non-employee Stock Options

On March 21, 2007, the Company issued stock options to non-employees to purchase 20,000 shares of the Company's common stock at an exercise price of \$7.00 per share vesting over the next three years and expiring December 19, 2016. These stock options remain outstanding as of December 31, 2015.

Restricted Stock

On June 24, 2011, Zunicom issued an additional 99,538 restricted shares of its common stock to Company employees who were still employed by the Company. As a condition to this grant, the grantees agreed to extend the restricted period on the shares (398,145) issued in June 2007, for an additional three years. As a result, all 497,683 shares vested on June 24, 2014. The fair value of the shares issued on June 24, 2011, at the issue date was approximately \$34,000. The Company amortized the fair value as compensation expense over the 36-month vesting period in accordance with ASC Topic 718, *Compensation – Stock Compensation*. Approximately \$6,600 of compensation expense related to these shares was recorded during 2014. All shares were fully vested during the year ended December 31, 2014.

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Note 7: Credit Concentrations and Significant Customers

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents and accounts receivable.

In the normal course of business, the Company extends unsecured credit to virtually all of its customers. Because of the credit risk involved, management has provided an allowance for doubtful accounts that reflects its estimate of amounts, which may become uncollectible. In the event of complete nonperformance by the Company's customers, the maximum exposure to the Company is the outstanding accounts receivable balance at the date of nonperformance.

At December 31, 2015 and 2014, the Company had one customer that comprised approximately 19% and 18% of total trade receivables, respectively. During the year ended December 31, 2014, one customer accounted for 12% of net sales.

A significant portion of the Company's inventory purchases are from three suppliers. These suppliers accounted for 61% and 70% of the Company's inventory purchases in 2015 and 2014, respectively. The Company purchased approximately 19% and 12% of its inventory for the years ended December 31, 2015 and 2014, respectively, from domestic sources with the remainder purchased from international sources, predominantly China. The Company has since expanded its supplier relationships throughout the Pacific Rim including Taiwan and Vietnam, in an effort to reduce supplier concentration and better improve the Company's supply base.

Note 8: Business Acquisition

On April 30, 2015, the Company completed an acquisition of all the membership interests of Intelligent Technologies, LLC (iTech), a California company and a manufacturer of market-leading portable power solutions to performance-critical industries and Fortune 500 companies. iTech provides innovative design and manufacture of smart lithium-ion batteries, chargers, docking stations and power sub-systems for performance critical applications in the handheld electronics, medical, intrinsic safety, industrial and communications markets. iTech is ISO 9001:2008 certified, ISO 13845 certified, and FDA licensed.

As a result of the acquisition, the Company will have an opportunity to increase its manufacturing capacity, customer base and market reach. The Company also expects to reduce costs through economies of scale.

During 2015, the Company incurred approximately \$108,000 of third-party acquisition-related costs. The expenses are included in operating expenses in the Company's consolidated statement of income for the year ended December 31, 2015.

Goodwill of \$8,053,379 arising from the acquisition consists largely of the synergies and economies of scale expected from combining the operations of the Company and iTech. All of the goodwill was assigned to the iTech segment of the business. All of this amount is expected to be deductible for tax purposes.

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The following table summarizes the consideration paid for iTech and the amounts of the assets acquired and liabilities assumed recognized at the acquisition date (in thousands).

Fair Value of Consideration Transferred

Cash	\$	12,128
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Recognized amounts of identifiable assets acquired and liabilities assumed

Cash	\$	36
Prepays		306
Receivables		2,246
Inventories		2,827
Property, plant and equipment		612
Non-compete agreements (3 year life)		15
Tradename (20 year life)		25
Customer list (6 year life)		318
Accounts payable		1,688
Current liabilities		<u>622</u>
Total identifiable net assets		<u>4,075</u>
Goodwill	\$	<u>8,053</u>

The fair value of the assets acquired includes receivables with a fair value of approximately \$2,246,000, all of which is expected to be collectible.

Note 9: Commitments and Contingencies

Litigation

The Company is subject to legal proceedings and claims that arise in the ordinary course of business. Management does not believe that the outcome of these matters will have a material adverse effect on the Company's financial position, operating results or cash flows. However, there can be no assurance that such legal proceedings will not have a material impact.

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Operating Leases Including Related Party Leases

The Company leases certain office and warehouse facilities and various vehicles and equipment under noncancelable operating leases, some with escalating payment and free rent clauses with various maturity dates through 2023. The leases require the Company to pay executory costs (property taxes, maintenance and insurance). Minimum future payments on these leases as of December 31, 2015, are as follows:

Years Ending December 31,	
<i>(in thousands)</i>	
2016	\$ 1,406
2017	1,367
2018	1,282
2019	1,245
2020	875
Thereafter	<u>1,921</u>
	<u><u>\$ 8,096</u></u>

Rent expense for the years ended December 31, 2015 and 2014, totaled approximately \$1,469,000 and \$1,390,000, respectively.

In connection with the business acquisition (*Note 8*), the Company assumed leases for two of its branch locations under operating leases with an officer and director of the Company. The leases expire in April 2020. Total lease payments for fiscal year 2015 were approximately \$160,000. Total lease obligations remaining at December 31, 2015, under these related party leases included in the table above total \$2,341,000.

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Note 10: Intangible Assets

The carrying basis and accumulated amortization of recognized intangible assets at December 31, 2015 and 2014, were:

	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
December 31, 2015	<i>(in thousands)</i>		
Definite-lived assets			
Customer list	\$ 627	\$ 288	\$ 339
Trademarks and intellectual property	<u>280</u>	<u>68</u>	<u>212</u>
Total gross carrying amount	<u>\$ 907</u>	<u>\$ 356</u>	<u>\$ 551</u>
December 31, 2014	<i>(in thousands)</i>		
Definite-lived assets			
Customer list	\$ 309	\$ 189	\$ 120
Trademarks and intellectual property	<u>240</u>	<u>49</u>	<u>191</u>
Total gross carrying amount	<u>\$ 549</u>	<u>\$ 238</u>	<u>\$ 311</u>

The changes in the carrying amount of goodwill for the year ended December 31, 2015 (in thousands):

Balance as of January 1	\$ 1,387
Goodwill acquired during the year	<u>8,053</u>
Balance as of December 31	<u>\$ 9,440</u>

On December 19, 2012, UPG acquired the Kinetik® brand, trademarks and intellectual property. The Company recorded \$240,000 for the acquired assets. The agreement contains a contingent consideration that has benchmarks for each year starting in 2013 for the next seven years. The contingent consideration is earned based upon achieving both the annual revenue and annual net profit thresholds for each year. Additional amounts will be recorded as a part of the amortized cost when the contingency is resolved and the consideration is paid or becomes payable. During the years ended December 31, 2015 and 2014, there was no additional amount added to the recorded amount of this asset.

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Amortization expense for the years ended December 31, 2015 and 2014, was \$118,000 and \$105,000, respectively. The weighted-average remaining useful life of the intangibles at December 31, 2015 is 5.90 years. Estimated amortization at December 31, 2015, for each of the following five years is (in thousands):

2016	\$	135
2017		99
2018		90
2019		78
2020		78
		<hr/>
	\$	480
		<hr/> <hr/>

Note 11: Employee Benefit Plan

UPG established and continues to maintain a 401(k) plan intended to qualify under sections 401(a) and 401(k) of the IRC of 1986, as amended. All employees of the Company who are at least 18 years of age are eligible to participate in the plan. There is no minimum service requirement to participate in the plan. Under the plan, an eligible employee can elect to defer from 1% to 85% of their salary subject to IRC limitations. The Company may, at its sole discretion, contribute and allocate to plan participant's account a percentage of the plan participant's contribution. During 2015 and 2014, there were no contributions made to the plan.

iTech has a 401(K) plan which the employer contributes 50% of the eligible employee's contribution up to a maximum of 2%. An employee is vested in the company contribution at 20% per year and is 100% vested after six (6) years of service. Employees must be 21 or older and have completed three months service or 1,000 hours of service in a given plan year. Total Company contribution to the 401(k) plans were \$36,000 and \$0 for the years ended December 31, 2015 and 2014, respectively.

Note 12: Subsequent Events

In June 2016, the Company entered into an amended and restated credit agreement with Comerica to include a \$30,000,000 credit line and a \$3,428,571 term loan. In addition, the amended credit agreement extended the maturity date of the credit line and term loan to December 2020.

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On April 16, 2015, the Compensation Committee of the Board of Directors approved the grant of 500,000 restricted shares of common stock to our Chief Executive Officer. On September 23, 2015, the Board of Directors approved the grant of an aggregate of 500,000 restricted shares of common stock to two other senior executive officers. The shares were issued on May 4, 2016, in consideration of past and future services, have full dividend and voting rights, but remain subject to full forfeiture for 10 years from the anniversary date. The shares granted includes restrictions on which they cannot be sold, transferred or pledged as well as being tied to their employment with the Company. The Company is amortizing the fair value as compensation expense over the 10-year vesting period. Fair value of \$1.3 million was calculated based on the share price of \$1.30 on the date of grant.

Subsequent events have been evaluated through August 5, 2016, which is the date the financial statements were available to be issued.