TECHNICAL COMMUNICATIONS CORP
Form 10-Q
May 12, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(Mark One)

x **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended March 28, 2015

¨ **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: 001-34816

TECHNICAL COMMUNICATIONS CORPORATION

(Exact name of registrant as specified in its charter)

Massachusetts	**04-2295040**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
100 Domino Drive, Concord, MA	**01742-2892**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (978) 287-5100

N/A

(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 that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x 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 x 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 the 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 x

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock as of the latest practicable date. 1,838,921 shares of Common Stock, $0.10 par value, outstanding as of May 8, 2015.

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TECHNICAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(Unaudited)

	March 28, 2015	September 27, 2014
Assets		
Current Assets:		
Cash and cash equivalents	$ 1,604,033	$ 3,210,237
Marketable securities		
Available for sale	1,022,034	1,416,890
Held to maturity	410,715	310,437
Accounts receivable - trade, less allowance of $25,000 at March 28, 2015 and September 27, 2014	1,860,326	403,139
Inventories, net	2,804,426	2,721,313
Other current assets	190,024	210,379
Total current assets	7,891,558	8,272,395
Marketable securities - held to maturity	881,079	1,105,140
Equipment and leasehold improvements	4,465,096	4,465,096
Less: accumulated depreciation and amortization	(4,135,361)	(4,033,233)
Equipment and leasehold improvements, net	329,735	431,863
Investment in unconsolidated subsidiary	275,000	
Total Assets	$ 9,377,372	$ 9,809,398
Liabilities and Stockholders Equity		
Current Liabilities:		
Accounts payable	$ 297,948	$ 173,553
Accrued liabilities:		
Accrued compensation and related expenses	193,531	163,410
Customer deposits	61,487	169,943
Other current liabilities	121,054	157,784
Income taxes payable	75,877	76,859
Total current liabilities	749,897	741,549
Commitments and contingencies		

Stockholders Equity:				
Common stock, par value $0.10 per share; 7,000,000 shares authorized; 1,838,921 shares issued and outstanding at March 28, 2015 and September 27, 2014		183,892		183,892
Additional paid-in capital		4,061,302		3,986,996
Accumulated other comprehensive loss		(682)		(3,598)
Retained earnings		4,382,963		4,900,559
Total stockholders equity		8,627,475		9,067,849
Total Liabilities and Stockholders Equity	$	9,377,372	$	9,809,398

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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TECHNICAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES

Condensed Consolidated Statements of Operations

(Unaudited)

	Three Months Ended	
	March 28, 2015	**March 29, 2014**
Net sales	$ 2,372,575	$ 1,293,478
Cost of sales	649,334	337,592
Gross profit	1,723,241	955,886
Operating expenses:		
Selling, general and administrative	765,398	841,988
Product development	752,979	765,852
Total operating expenses	1,518,377	1,607,840
Operating income (loss)	204,864	(651,954)
Other income:		
Interest income	5,121	6,491
Income (loss) before provision for income taxes	209,985	(645,463)
Provision for income taxes		821,066
Net income (loss)	$ 209,985	$ (1,466,529)
Net income (loss) per common share:		
Basic	$ 0.11	$ (0.80)
Diluted	$ 0.11	$ (0.80)
Weighted average shares:		
Basic	1,838,921	1,838,907
Diluted	1,846,399	1,838,907

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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TECHNICAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES

Condensed Consolidated Statements of Operations

(Unaudited)

	Six Months Ended	
	March 28, 2015	**March 29, 2014**
Net sales	$ 3,255,721	$ 3,802,198
Cost of sales	920,365	1,126,452
Gross profit	2,335,356	2,675,746
Operating expenses:		
Selling, general and administrative	1,521,424	1,549,106
Product development	1,342,544	1,527,737
Total operating expenses	2,863,968	3,076,843
Operating loss	(528,612)	(401,097)
Other income:		
Interest income	11,016	13,176
Loss before provision for income taxes	(517,596)	(387,921)
Provision for income taxes		894,458
Net loss	$ (517,596)	$ (1,282,379)
Net loss per common share:		
Basic	$ (0.28)	$ (0.70)
Diluted	$ (0.28)	$ (0.70)
Weighted average shares:		
Basic	1,838,921	1,838,812
Diluted	1,838,921	1,838,812

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements

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TECHNICAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES

Condensed Consolidated Statements of Comprehensive Income (Loss)

(Unaudited)

	Three Months Ended	
	March 28, 2015	**March 29, 2014**
Net income (loss)	$ 209,985	$ (1,466,529)
Unrealized gain (loss) on available for sale securities, net of tax	935	(455)
Comprehensive income (loss)	$ 210,920	$ (1,466,984)

	Six Months Ended	
	March 28, 2015	**March 29, 2014**
Net loss	$ (517,596)	$ (1,282,379)
Unrealized gain (loss) on available for sale securities, net of tax	2,916	(4,869)
Comprehensive loss	$ (514,680)	$ (1,287,248)

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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TECHNICAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(Unaudited)

	Six Months Ended	
	March 28, 2015	**March 29, 2014**
Operating Activities:		
Net loss	$ (517,596)	$ (1,282,379)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Depreciation and amortization	102,128	101,897
Stock-based compensation	74,306	138,878
Deferred income taxes		894,459
Amortization of premium on held to maturity securities	24,555	32,924
Changes in certain operating assets and liabilities:		
Accounts receivable	(1,457,187)	1,124,921
Inventories	(83,113)	489,604
Income taxes payable / receivable	(982)	(4,912)
Other current assets	20,355	(9,002)
Customer deposits	(108,456)	97,692
Accounts payable and other accrued liabilities	117,786	(210,666)
Net cash (used in) provided by operating activities	(1,828,204)	1,373,416
Investing Activities:		
Additions to equipment and leasehold improvements		(106,536)
Investment in unconsolidated subsidiary	(275,000)	
Proceeds from maturities of marketable securities	497,000	1,245,000
Purchases of marketable securities		(2,579,000)
Net cash provided by (used in) investing activities	222,000	(1,440,536)
Financing Activities:		
Net cash used in financing activities		
Net decrease in cash and cash equivalents	(1,606,204)	(67,120)
Cash and cash equivalents at beginning of the period	3,210,237	2,810,923
Cash and cash equivalents at end of the period	$ 1,604,033	$ 2,743,803

Supplemental Disclosures:		
Interest paid	$	$
Income taxes paid	982	4,942

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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TECHNICAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Interim Financial Statements

The accompanying unaudited condensed consolidated financial statements of Technical Communications Corporation (the Company or TCC) and its wholly-owned subsidiary include all adjustments which are, in the opinion of management, necessary for a fair presentation of the financial position and results of operations for the periods presented and in order to make the financial statements not misleading. All such adjustments are of a normal recurring nature. Interim results are not necessarily indicative of the results to be expected for the fiscal year ending October 3, 2015.

Certain footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted as allowed by Securities and Exchange Commission (SEC) rules and regulations. The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the Company s consolidated financial statements and the notes thereto in the Company s Annual Report on Form 10-K for the fiscal year ended September 27, 2014 as filed with the SEC.

We follow accounting standards set by the Financial Accounting Standards Board, commonly referred to as the FASB. The FASB sets generally accepted accounting principles (GAAP) that we follow to ensure we consistently report our financial condition, results of operations, and cash flows. References to GAAP issued by the FASB in these footnotes are to the *FASB Accounting Standards Codification* - sometimes referred to as the Codification or ASC.

It is anticipated that cash from operations will fund our near-term research and development and marketing activities through at least March 2016. We also believe that in the long term, based on current billable activities, cash from operations will be sufficient to meet the development goals of the Company, although we can give no assurances. Any increase in development activities - either billable or new product related - will require additional resources, which we may not be able to fund through cash from operations. We plan to continue to closely monitor operating expenses and will reduce them if needed. In circumstances where resources may be insufficient, the Company will look to other sources of financing, including debt and/or equity investments, although we can give no assurances that the Company will be successful in obtaining such financing.

NOTE 1. Summary of Significant Accounting Policies and Significant Judgments and Estimates

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary. All significant intercompany accounts and transactions have been eliminated in consolidation. The Company s investment in an unconsolidated subsidiary is accounted for on a cost basis.

The discussion and analysis of our financial condition and results of operations are based on our unaudited condensed consolidated financial statements, which have been prepared in accordance with GAAP. The preparation of these unaudited condensed consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported revenues and expenses during the reporting periods.

On an ongoing basis, management evaluates its estimates and judgments, including but not limited to those related to revenue recognition, inventory reserves, receivable reserves, marketable securities, impairment of long-lived assets, income taxes, fair value of financial instruments and stock-based compensation. Management bases its estimates on historical experience and on various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. By their nature estimates are subject to an inherent degree of uncertainty. Actual results may differ from these estimates under different assumptions or conditions.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Cont d)

The accounting policies that management believes are most critical to aid in fully understanding and evaluating our reported financial results include the following:

Revenue Recognition

Product revenue is recognized when there is persuasive evidence of an arrangement, the fee is fixed or determinable, delivery of the product and passage of title to the customer has occurred and we have determined that collection of the fee is probable. Title to the product generally passes upon shipment of the product, as the products are shipped FOB shipping point, except for certain foreign shipments for which title passes upon entry of the product into the first port in the buyer s country. If the product requires installation to be performed by TCC or there exists other acceptance criteria, all revenue related to the product is deferred and recognized upon completion of the installation or satisfaction of the customer acceptance criteria. We provide for a warranty reserve at the time the product revenue is recognized.

We perform funded research and development and technology development for commercial companies and government agencies under both cost reimbursement and fixed-price contracts. Cost reimbursement contracts provide for the reimbursement of allowable costs and, in some situations, the payment of a fee. These contracts may contain incentive clauses providing for increases or decreases in the fee depending on how actual costs compare with a budget. Revenue from cost reimbursement contracts is recognized as services are performed. On fixed-price contracts that are expected to exceed one year in duration, revenue is recognized pursuant to the proportional performance method based upon the proportion of actual costs incurred to date to the total estimated costs for the contract. In each type of contract, we receive periodic progress payments or payments upon reaching interim milestones, and we retain the rights to the intellectual property developed in government contracts. All payments to TCC for work performed on contracts with agencies of the U.S. government are subject to audit and adjustment by the Defense Contract Audit Agency. Adjustments are recognized in the period made. There have been no government audits in recent years and the Company believes the result of such audits, should they occur, would not have a material adverse effect on its financial position or results of operations. When current estimates of total contract revenue and contract costs for a product development contract indicate a loss, a provision for the entire amount of the loss on the contract is recorded. Any losses incurred in performing funded research and development projects are recognized as funded research and development expenses.

A portion of the Company s revenues are derived from arrangements that contain multiple deliverables. As a result, the Company separates and assigns value to each element in its multiple element arrangements following ASC 605-25 *Revenue Recognition Multiple Element Arrangements*. This guidance establishes a hierarchy for determining the amount to allocate to each separable deliverable in an arrangement. For those deliverables that qualify as separate units of accounting, the Company must assign value based on each deliverable s vendor-specific objective evidence (VSOE) of value if available, third-party evidence (TPE) of its value if VSOE is not available, or estimated selling price (ESP) if neither VSOE or TPE is available. Arrangement consideration is then allocated to all deliverables using the relative selling price method. Management performs an analysis to determine the relative selling price of each unit of accounting. Management s ESP is used for products. The Company determines ESP for the products using an internal price list matrix, which is used in practice, and recent sales.

Cost of product revenue includes material, labor and overhead. Costs incurred in connection with funded research and development are included in cost of sales. Product development costs are charged to billable engineering services, bid and proposal efforts or business development activities, as appropriate. Product development costs charged to billable projects are recorded as cost of sales; engineering costs charged to bid and proposal efforts are recorded as selling expenses; and product development costs charged to business development activities are recorded as marketing expenses. Product development costs consist primarily of personnel costs, outside contractor and engineering services, supplies and materials.

Cash and Cash Equivalents

Cash and cash equivalents include demand deposits at banks and other investments (including mutual funds) readily convertible into cash. Cash equivalents are stated at cost, which approximates market value. At March 28, 2015, the Company had restrictions on the use of cash used as collateral to secured four outstanding letters of credit totaling $363,414.

Long-lived Assets

The Company s only long-lived assets are equipment and leasehold improvements. Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. These events include a significant decrease in the market price of a long-lived asset, a significant adverse change in the extent or manner in which a long-lived asset is being used or in its physical condition, a significant adverse change in legal factors or in the business climate that could affect the value of a long-lived asset (including an adverse action or assessment by a regulator), an accumulation of costs significantly in excess of the amount originally expected for the acquisition or

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Cont d)

construction of a long-lived asset, a current-period operating or cash flow loss combined with a history of operating or cash flow losses, or a projection or forecast that demonstrates continuing losses associated with the use of a long-lived asset, among other items. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of the asset to the estimated undiscounted future cash flows expected to be generated by such asset. If the carrying amount of the asset exceeds its estimated undiscounted future cash flows, an impairment charge is recognized in the amount by which the carrying amount exceeds the fair value of the asset.

Inventory

We value our inventory at the lower of actual cost (based on first-in, first-out) to purchase and/or manufacture or the current estimated market value (based on the estimated selling prices, less the cost to sell) of the inventory. We periodically review inventory quantities on hand and record a provision for excess and/or obsolete inventory based primarily on our estimated forecast of product demand, as well as historical usage. Due to the custom and specific nature of certain of our products, demand and usage for products and materials can fluctuate significantly. A significant decrease in demand for our products could result in a short-term increase in the cost of inventory purchases and an increase in excess inventory quantities on hand. In addition, our industry is characterized by rapid technological change, frequent new product development and rapid product obsolescence, any of which could result in an increase in the amount of obsolete inventory quantities on hand. Therefore, although we make every effort to ensure the accuracy of our forecasts of future product demand, any significant unanticipated changes in demand or technological developments could have a significant negative impact on the value of our inventory and would reduce our reported operating results.

Accounts Receivable

Accounts receivable are reduced by an allowance for amounts that may become uncollectible in the future. The estimated allowance for uncollectible amounts is based primarily on a specific analysis of accounts in the receivable portfolio and historical write-off experience. While management believes the allowance to be adequate, if the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required and would result in a reduction to our net income. The allowance recorded for accounts receivable at each of March 28, 2015 and September 27, 2014 was $25,000.

Investments

The Company accounts for marketable securities in accordance with FASB ASC 320, *Investments Debt and Equity Securities.* All marketable securities must be classified as one of the following: held to maturity, available for sale, or trading. The Company classifies its marketable securities as either available for sale and or held to maturity. The available for sale investments, comprised of certificates of deposit and money market mutual funds, are valued at fair value, with unrealized holding gains and losses reported in stockholders equity as a separate component of accumulated other comprehensive income (loss). The cost of securities sold is determined based on the specific identification method. Realized gains and losses, and declines in value judged to be other than temporary, are included in investment income. The Company s held to maturity securities, comprised of investments in municipal bonds, are valued at amortized cost. The purchase discount or premium is amortized to income or expense, respectively, over the life of the securities.

Accounting for Income Taxes

The preparation of our unaudited condensed consolidated financial statements requires us to estimate our income taxes in each of the jurisdictions in which we operate, including those outside the United States, which may subject the Company to certain risks that ordinarily would not be expected in the United States. The income tax accounting process involves estimating our actual current exposure together with assessing

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Cont d)

temporary differences resulting from differing treatments of items, such as deferred revenue, reserves on accounts receivable and inventory, as well as depreciation differences for tax and accounting purposes. These differences result in the recognition of deferred tax assets and liabilities. We must then record a valuation allowance to reduce our deferred tax assets to the amount that is more likely than not to be realized.

Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities, and any valuation allowance recorded against deferred tax assets. During the fiscal year ended September 27, 2014, we recorded a full valuation allowance against our net deferred tax assets of approximately $2.4 million due to uncertainties related to our ability to utilize these assets. The valuation allowance is based on our estimates of taxable income by jurisdiction and the period over which our deferred tax assets will be recoverable. In the event that actual results differ from these estimates or we adjust these estimates in future periods, we may need to adjust our valuation allowance, which could materially impact our financial position and results of operation.

We recognize tax liabilities in accordance with FASB ASC 740-10, *Income Taxes* and we adjust such liabilities when our judgment changes as a result of the evaluation of information not previously available. Due to the complexity of some of these uncertainties, the ultimate resolution may result in a payment that is materially different from our current estimate of the tax liabilities. These differences will be reflected as increases or decreases to income tax expense in the period in which they are determined.

The Company also follows FASB ASC 740-10 relative to uncertain tax positions. This standard provides detailed guidance for the financial statement recognition, measurement and disclosure of uncertain tax positions recognized in the financial statements. Uncertain tax positions must meet a recognition threshold of more-likely-than-not in order for those tax positions to be recognized in the financial statements. As of March 28, 2015 and September 27, 2014, the Company had uncertain tax positions of $81,602 and $81,218, respectively. The Company s policy is to reflect the changes in uncertain tax positions in its selling, general and administrative expenses.

Due to the nature of our current operations in foreign countries (selling products into these countries with the assistance of local representatives), the Company has not been subject to any foreign taxes in recent years, and it is not anticipated that we will be subject to foreign taxes in the near future.

Fair Value of Financial Instruments

In determining the fair value of financial instruments, the Company follows the provisions of FASB ASC 820, *Fair Value Measurements and Disclosures*. FASB ASC 820 defines fair value, establishes a framework for measuring fair value under GAAP and enhances disclosures about fair value measurements. The topic provides a consistent definition of fair value which focuses on an exit price, which is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The topic also prioritizes, within the measurement of fair value, the use of market-based information over entity-specific information and establishes a three-level hierarchy for fair value measurements based on the nature of inputs used in the valuation of an asset or liability as of the measurement date. The three-level hierarchy is as follows:

Level 1 -

Pricing inputs are quoted prices available in active markets for identical investments as of the reporting date.

Level 2 - Pricing inputs are quoted prices for similar investments, or inputs that are observable, either directly or indirectly, for substantially the full term through corroboration with observable market data.

Level 3 - Pricing inputs are unobservable for the investment, that is, inputs that reflect the reporting entity s own assumptions about the assumptions market participants would use in pricing the asset or liability.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Cont d)

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, an investment s level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The Company s assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the investment.

The Company s held to maturity securities are comprised of investments in municipal bonds. These securities represent ownership in individual bonds issued by municipalities within the United States. The Company s available for sale securities are comprised of certificates of deposit in U.S. banks and money market funds held in a brokerage account. The fair value of these investments is based on quoted prices from recognized pricing services (e.g. Standard & Poor s, Bloomberg, etc.) or, in the case of mutual funds, at their closing net asset value.

The Company assesses the levels of the investments at each measurement date, and transfers between levels are recognized on the actual date of the event or change in circumstances that caused the transfer in accordance with the Company s accounting policy regarding the recognition of transfers between levels of the fair value hierarchy. During the six month period ended March 28, 2015 and the year ended September 27, 2014, there were no transfers between levels.

The following table sets forth by level, within the fair value hierarchy, the financial instruments carried at fair value as of March 28, 2015 and September 27, 2014, in accordance with the fair value hierarchy as defined above. As of March 28, 2015 and September 27, 2014, the Company did not hold any assets classified as Level 3.

	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
March 28, 2015			
Certificates of deposits:			
Certificates of deposit	$ 1,022,034	$	$ 1,022,034
Total debt instruments	1,022,034		1,022,034
Mutual funds:			
Money market funds	833,619	833,619	
Total mutual funds	833,619	833,619	
Total investments	$ 1,855,653	$ 833,619	$ 1,022,034
September 27, 2014			

Debt and certificates of deposits:			
Certificates of deposit	$ 1,416,890	$	$ 1,416,890
Total debt instruments	1,416,890		1,416,890
Mutual funds:			
Money market funds	1,801,443	1,801,443	
Total mutual funds	1,801,443	1,801,443	
Total investments	$ 3,218,333	$ 1,801,443	$ 1,416,890

There were no assets or liabilities measured on a nonrecurring basis at March 28, 2015 and September 27, 2014.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Cont d)

Stock-Based Compensation

Stock-based compensation cost is measured at the grant date based on the calculated fair value of the award. The expense is recognized over the participant s requisite service period, generally the vesting period of the award. The related excess tax benefit received upon the exercise of stock options, if any, is reflected in the Company s statement of cash flows as a financing activity rather than an operating activity. There were no excess tax benefits recorded during the three and six month periods ended March 28, 2015 and March 29, 2014.

The Company uses the Black-Scholes option pricing model as the method for determining the estimated fair value of its stock awards. The Black-Scholes method of valuation requires several assumptions: (1) the expected term of the stock award, (2) the expected future stock price volatility over the expected term, (3) a risk-free interest rate and (4) the expected dividend rate. The expected term represents the expected period of time the Company believes the options will be outstanding based on historical information. Estimates of expected future stock price volatility are based on the historic volatility of the Company s common stock, and the risk free interest rate is based on the U.S. Treasury Note rate. The Company utilizes a forfeiture rate based on an analysis of its actual experience, which forfeiture rate is not material to the calculation of share-based compensation.

The fair value of options at date of grant was estimated with the following assumptions:

	Three and Six Months Ended	
	March 28, 2015	**March 29, 2014**
Option term		6.5 years
Risk-free interest rate		1.33% to 1.53%
Stock price volatility		60% to 65%
Dividend rate		

There were no options granted during the six months ended March 28, 2015, and 14,200 options granted during the six months ended March 29, 2014. The weighted average grant date fair value for the options granted during the six months ended March 29, 2014 was $4.53.

The following table summarizes stock-based compensation costs included in the Company s condensed consolidated income statements for the three and six month periods ended March 28, 2015 and March 29, 2014:

	March 28, 2015		**March 29, 2014**	
	3 months	**6 months**	**3 months**	**6 months**
Cost of sales	$ 3,801	$ 7,850	$ 4,079	$ 8,158
Selling, general and administrative expenses	11,965	23,942	75,360	87,290
Product development expenses	21,245	42,514	21,165	43,430

Total share-based compensation expense before taxes	$ 37,011	$ 74,306	$ 100,604	$ 138,878

As of March 28, 2015 and September 27, 2014, there was $66,338 and $141,213, respectively, of unrecognized compensation expense related to options outstanding. The unrecognized compensation expense will be recognized over the remaining requisite service period. As of March 28, 2015, the weighted average period over which the compensation expense is expected to be recognized is 1.1 years.

The Company had the following stock option plans outstanding as of March 28, 2015: the 2001 Stock Option Plan, the 2005 Non-Statutory Stock Option Plan and the 2010 Equity Incentive Plan. There were an aggregate 750,000 shares originally authorized for issuance under these plans, of which options to purchase

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Cont d)

268,612 shares were outstanding at March 28, 2015. Vesting periods for options are at the discretion of the Board of Directors and typically range between zero and five years. Options under these plans are granted with an exercise price equal to fair market value at time of grant and have a term of ten years from the date of grant.

As of March 28, 2015, there were no shares available for new option grants under the 2001 Stock Option Plan, there were 19,723 shares available for grant under the 2005 Non-Statutory Stock Option Plan and there were 56,476 shares available for grant under the 2010 Equity Incentive Plan. As of May 5, 2015 the 2005 Non-Statutory Stock Option Plan expired and shares are no longer available for grant.

The following table summarizes stock option activity during the first six months of fiscal 2015:

	Options Outstanding				
	Number of Shares			Weighted Average Exercise Price	Weighted Average Contractual Life
	Unvested	Vested	Total		
Outstanding, September 27, 2014	32,739	236,746	269,485	$ 8.74	5.46 years
Grants					
Vested	(940)	940		10.29	
Cancellations/forfeitures					
Outstanding, December 27, 2014	31,799	237,686	269,485	$ 8.74	5.21 years
Grants					
Vested	(600)	600		7.32	
Cancellations/forfeitures	(175)	(698)	(873)	11.51	
Outstanding, March 28, 2015	31,024	237,588	268,612	$ 8.73	4.96 years

Information related to the stock options vested and expected to vest as of March 28, 2015 is as follows:

Range of Exercise Prices	Number of Shares	Weighted-Average Remaining Contractual Life (years)	Weighted Average Exercise Price	Exercisable Number of Shares	Exercisable Weighted-Average Exercise Price
$ 2.01 - $ 3.00	15,288	0.45	$ 3.00	15,288	$ 3.00
$ 3.01 - $ 4.00	16,600	1.33	$ 3.66	16,600	$ 3.66
$ 4.01 - $ 5.00	28,000	6.06	$ 4.78	27,100	$ 4.78
$ 5.01 - $10.00	69,900	5.29	$ 7.45	66,040	$ 7.46

$10.01 - $15.00	138,824	5.50	$	11.41	112,560	$	11.39
	268,612	4.96	$	8.73	237,588	$	8.46

The aggregate intrinsic value of the Company s in-the-money outstanding and exercisable options as of March 28, 2015 and September 27, 2014 was $24,157 and $29,987, respectively. Nonvested common stock options are subject to the risk of forfeiture until the fulfillment of specified conditions.

NOTE 2. Inventories

Inventories consisted of the following:

	March 28, 2015		September 27, 2014	
Finished goods	$	17,110	$	8,014
Work in process		1,045,894		1,126,365
Raw materials		1,741,422		1,586,934
	$	2,804,426	$	2,721,313

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Cont d)

NOTE 3. Income Taxes

The Company has not recorded an income tax benefit on its net loss for the six months ended March 28, 2015 due to its uncertain realizability. During the second quarter of fiscal 2014, the Company recorded a valuation allowance for the full amount of its net deferred tax assets since it cannot currently predict the realization of these assets.

During the three months ended March 29, 2014, the Company established a valuation allowance against deferred tax assets and as a result recorded an income tax provision for the six month period ended March 29, 2014 of $894,458. The valuation allowance is related to uncertainty with respect to the Company s ability to realize its deferred tax assets. Deferred tax assets consist of net operating loss carryforwards, tax credits, inventory differences and other temporary differences.

The below table details the changes in uncertain tax positions, which if recognized would favorably impact our effective tax rate:

Balance at September 27, 2014	$ 80,829
Addition related to prior year positions	773
Balance at March 28, 2015	$ 81,602

The increase in the Company s total uncertain tax positions relates to additional accrued interest and penalties for the period.

NOTE 4. Earnings (Loss) Per Share

Basic and diluted earnings (loss) per share were calculated as follows:

	March 28, 2015		March 29, 2014	
	3 months	**6 months**	**3 months**	**6 months**
Net income (loss)	$ 209,985	$ (517,596)	$ (1,466,529)	$ (1,282,379)
Weighted average shares outstanding - basic	1,838,921	1,838,921	1,838,907	1,838,812
Dilutive effect of stock options	7,478			
Weighted average shares outstanding - diluted	1,846,399	1,838,921	1,838,907	1,838,812

Basic net income (loss) per share	$	0.11	$	(0.28)	$	(0.80)	$	(0.70)
Diluted net income (loss) per share	$	0.11	$	(0.28)	$	(0.80)	$	(0.70)

Outstanding potentially dilutive stock options, which were not included in the earnings per share calculations because their inclusion would have been anti-dilutive, were 268,612 at March 28, 2015 and 268,185 at March 29, 2014.

NOTE 5. Major Customers and Export Sales

During the three months ended March 28, 2015, the Company had two customers that represented 94% (76% and 18%) of net sales as compared to the three months ended March 29, 2014, during which one customer represented 70% of net sales. During the six months ended March 28, 2015, the Company had three customers that represented 87% (57%, 17% and 13%, respectively) of net sales as compared to the six month period ended March 29, 2014, during which three customers represented 81% (46%, 24% and 11%, respectively) of net sales.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Cont d)

A breakdown of foreign and domestic net sales is as follows:

	March 28, 2015		March 29, 2014	
	3 months	**6 months**	**3 months**	**6 months**
Domestic	$ 515,842	$ 1,280,588	$ 1,262,434	$ 3,525,188
Foreign	1,856,733	1,975,133	31,044	277,010
Total sales	$ 2,372,575	$ 3,255,721	$ 1,293,478	$ 3,802,198

The Company sold products into two countries during the three month period ended March 28, 2015 and one country during the three month period ended March 29, 2014. The Company sold products into five countries during the six month period ended March 28, 2015 and two countries during the six month period ended March 29, 2014. A sale is attributed to a foreign country based on the location of the contracting party. Domestic revenue may include the sale of products shipped through domestic resellers or manufacturers to international destinations. The table below summarizes our foreign revenues by country as a percentage of total foreign revenue.

	March 28, 2015		March 29, 2014	
	3 months	**6 months**	**3 months**	**6 months**
Egypt	97%	93%		
Colombia				89%
Saudi Arabia			100%	11%
Other	3%	7%		

A summary of foreign revenue, as a percentage of total foreign revenue by geographic area, is as follows:

	March 28, 2015		March 29, 2014	
	3 months	**6 months**	**3 months**	**6 months**
North America (excluding the U.S.)				
Central and South America				89%
Europe				
Mid-East and Africa	97%	94%	100%	11%
Far East	3%	6%		

NOTE 6. Cash Equivalents and Marketable Securities

The Company considers all highly liquid instruments with an original maturity of three months or less to be cash equivalents. Substantially all cash equivalents are invested in money market mutual funds. Money market mutual funds held in a brokerage account are considered available for sale. The Company accounts for marketable securities in accordance with FASB ASC 320, *Investments Debt and Equity Securities.* All marketable securities must be classified as one of the following: held to maturity, available for sale, or trading. The Company classifies its marketable securities as either available for sale or held to maturity. Available for sale securities are carried at fair value, with unrealized holding gains and losses reported in stockholders equity as a separate component of accumulated other comprehensive income (loss). Held to maturity securities are carried at amortized cost. The cost of securities sold is determined based on the specific identification method. Realized gains and losses, and declines in value judged to be other than temporary, are included in investment income. During fiscal year 2013, the Company determined it would hold its investment in municipal bonds until maturity and subsequently reclassified these securities from available for sale to held to maturity. These securities are now carried at amortized cost.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Cont d)

As of March 28, 2015, available for sale securities consisted of the following:

	Cost	Accrued Interest	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Money market funds	$ 833,619	$	$	$	$ 833,619
Certificates of deposit	1,021,000	1,716		682	1,022,034
	$ 1,854,619	$ 1,716	$	$ 682	$ 1,855,653

As of March 28, 2015, held to maturity securities consisted of the following:

	Cost	Accrued Interest	Amortization Bond Premium	Amortized Cost	Unrealized Gains	Estimated Fair Value
Municipal bonds	$ 1,392,147	$ 16,886	$ 117,239	$ 1,291,794	$ 10,495	$ 1,302,289

As of September 27, 2014, available for sale securities consisted of the following:

	Cost	Accrued Interest	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Money market funds	$ 1,801,443	$	$	$	$ 1,801,443
Certificates of deposit	1,418,000	2,488		3,598	1,416,890
	$ 3,219,443	$ 2,488	$	$ 3,598	$ 3,218,333

As of September 27, 2014, held to maturity securities consisted of the following:

	Cost	Accrued Interest	Amortization Bond Premium	Amortized Cost	Unrealized Gains	Estimated Fair Value
Municipal bonds	$ 1,506,653	$ 17,963	$ 109,039	$ 1,415,577	$ 15,331	$ 1,430,908

The contractual maturities of available for sale investments as of March 28, 2015 were all due within five months. The contractual maturities of held to maturity investments as of March 28, 2015 were as follows:

	Cost	Amortized Cost

Within 1 year	$	447,162	$	410,700
After 1 year through 5 years		944,985		881,094
	$	1,392,147	$	1,291,794

The Company s available for sale securities were included in the following captions in the consolidated balance sheets:

		March 28, 2015		**September 27, 2014**
Cash and cash equivalents	$	833,619	$	1,801,443
Marketable securities		1,022,034		1,416,890
	$	1,855,653	$	3,218,333

<u>NOTE 7</u> <u>Investment in Unconsolidated Subsidiary</u>

On October 30, 2014 the Company made an investment of $275,000 to purchase 11,000 shares of common stock of PulsedLight, Inc., an early stage start-up company located in Bend, Oregon. Our investment represented an 11% ownership stake in PulsedLight, Inc. at the time of the investment and is accounted for utilizing the cost method of accounting.

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

Certain statements contained herein or as may otherwise be incorporated by reference herein that are not purely historical constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include but are not limited to statements regarding anticipated operating results, future earnings, and the Company s ability to achieve growth and profitability. Such forward-looking statements involve known and unknown risks, uncertainties and other factors, including but not limited to the effect of foreign political unrest; domestic and foreign government policies and economic conditions; future changes in export laws or regulations; changes in technology; the ability to hire, retain and motivate technical, management and sales personnel; the risks associated with the technical feasibility and market acceptance of new products; changes in telecommunications protocols; the effects of changing costs, exchange rates and interest rates; and the Company s ability to secure adequate capital resources. Such risks, uncertainties and other factors could cause the actual results, performance or achievements of the Company, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. For a more detailed discussion of the risks facing the Company, see the Company s filings with the SEC, including its Annual Report on Form 10-K for the fiscal year ended September 27, 2014.

Overview

The Company designs, manufactures, markets and sells communications security equipment that utilizes various methods of encryption to protect the information being transmitted. Encryption is a technique for rendering information unintelligible, which information can then be reconstituted if the recipient possesses the right decryption key . The Company manufactures several standard secure communications products and also provides custom-designed, special-purpose secure communications products for both domestic and international customers. The Company s products consist primarily of voice, data and facsimile encryptors. Revenue is generated principally from the sale of these products, which have traditionally been to foreign governments either through direct sale, pursuant to a U.S. government contract, or made as a sub-contractor to domestic corporations under contract with the U.S. government. We also sell these products to commercial entities and U.S. government agencies. We generate additional revenues from contract engineering services performed for certain government agencies, both domestic and foreign, and commercial entities.

Critical Accounting Policies and Significant Judgments and Estimates

There have been no material changes in the Company s critical accounting policies or critical accounting estimates since September 27, 2014, nor have we adopted any accounting policy that has or will have a material impact on our consolidated financial statements. For further discussion of our accounting policies see Note 1, *Summary of Significant Accounting Policies and Significant Judgments and Estimates* in the Notes to Unaudited Condensed Consolidated Financial Statements in this Quarterly Report on Form 10-Q and the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended September 27, 2014 as filed with the SEC.

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Results of Operations

Three Months ended March 28, 2015 as compared to Three Months ended March 29, 2014

Net Sales

Net sales for the quarter ended March 28, 2015 were $2,373,000, compared to $1,293,000 for the quarter ended March 29, 2014, an increase of 83%. Sales for the second quarter of fiscal 2015 consisted of $516,000, or 22%, from domestic sources and $1,857,000, or 78%, from international customers as compared to the same period in fiscal 2014, during which sales consisted of $1,262,000, or 98%, from domestic sources and $31,000, or 2%, from international customers. The increase in sales reflects receiving an expected major foreign contract in the previous quarter.

Foreign sales consisted of shipments to two countries during the quarter ended March 28, 2015 and one country during the quarter ended March 29, 2014. A sale is attributed to a foreign country based on the location of the contracting party. Domestic revenue may include the sale of products shipped through domestic resellers or manufacturers to international destinations. The table below summarizes our principal foreign sales by country during the second quarters of fiscal 2015 and 2014:

	2015	2014
Egypt	$ 1,808,000	
Saudi Arabia		$ 31,000
Other	49,000	
	$ 1,857,000	$ 31,000

For the three months ended March 28, 2015, product sales revenue was derived primarily from shipments of our DSD 72A-SP military bulk encryption system to a customer in Egypt amounting to $1,808,000. We also sold our link encryptor to a domestic contractor for deployment into the Middle East amounting to $432,000.

For the three months ended March 29, 2014, product sales revenue was derived primarily from shipments of our narrowband radio encryptors to a U.S. radio manufacturer for deployment into Afghanistan amounting to $908,000. The Company also made shipments of our narrowband radio encryptors, and supplied customized cryptographic services and tools and training, for a domestic prime contractor supporting a government customer in North Africa amounting to $144,000 during the quarter. We also had royalty sales to a domestic radio manufacturer of $105,000.

Gross Profit

Gross profit for the second quarter of fiscal 2015 was $1,723,000, compared to gross profit of $956,000 for the same period of fiscal 2014. Gross profit expressed as a percentage of sales was 73% for the second quarter of fiscal 2015 as compared to 74% in fiscal 2014. The 80% dollar value increase in gross profit during the quarter ended March 28, 2015 was the result of higher sales volume during the period.

Operating Costs and Expenses

Selling, General and Administrative Expenses

Selling, general and administrative expenses for the second quarter of fiscal 2015 were $765,000, compared to $842,000 for the same quarter in fiscal 2014. This decrease of $77,000, or 9%, was attributable to decreases in general and administrative expenses of $65,000 and selling and marketing expenses of $12,000 during the three months ended March 28, 2015.

The decrease in general and administrative costs during the second quarter of 2015 was primarily attributable to a decrease in employee stock compensation expense of $63,000 for the period.

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The decrease in selling and marketing expenses for the three months ended March 28, 2015 was primarily attributable to a decrease in engineering support of sales efforts of $25,000, as well as decreases in marketing efforts of $24,000, bid and proposal efforts of $16,000, outside consulting costs of $12,000, travel costs of $5,000 and product demonstration costs of $11,000 during the quarter. These decreases were offset by increases in product evaluation costs of $65,000 and outside sales and marketing agreements of $19,000 during the period.

Product Development Costs

Product development costs for the quarter ended March 28, 2015 were $753,000, compared to $766,000 for the quarter ended March 29, 2014. This decrease of $13,000, or 2%, was attributable to decreases in project material costs of $11,000, personnel-related costs of $6,000 and an increase in engineering support of sales and business development activities, which resulted in decreased product development costs of approximately $45,000. These decreases were partially offset by an increase in outside contractor costs of $51,000 for the quarter.

Product development costs are charged to product development, billable engineering services, bid and proposal efforts or business development activities, as appropriate. Product development costs charged to billable projects are recorded as cost of sales; product development costs charged to bid and proposal efforts are recorded as selling expenses; and product development costs charged to business development activities are recorded as marketing expenses.

The Company actively sells its engineering services in support of funded research and development. The receipt of these orders is sporadic, although such programs can span over several months. In addition to these programs, the Company also invests in research and development to enhance its existing products or to develop new products, as it deems appropriate. There was no billable engineering services revenue generated during the second quarters of fiscal 2015 and fiscal 2014.

Net Income

The Company generated net income of $210,000 for the second quarter of fiscal 2015, compared to a net loss of $1,467,000 for the same period of fiscal 2014. This increase in income is primarily attributable to an 83% increase in sales volume and a 6% decrease in operating expenses during the second quarter of fiscal 2015. During the quarter ended March 28, 2015, the Company did not record a tax provision as the effective tax rate for the Company s 2015 fiscal year is expected to be 0%, the expected losses are not being benefited due to a full valuation allowance. During the three months ended March 29, 2014, the Company established a valuation allowance against deferred tax assets and as a result recorded an income tax provision for the three month period ended March 29, 2014 of $821,000.

Six Months ended March 28, 2015 as compared to Six Months ended March 29, 2014

Net Sales

Net sales for the six months ended March 28, 2015 were $3,256,000, compared to $3,802,000 for the six months ended March 29, 2014, a decrease of 14%. Sales for the first six months of fiscal 2015 consisted of $1,281,000, or 39%, from domestic sources and $1,975,000, or 61%, from international customers as compared to the same period in fiscal 2014, during which sales consisted of $3,525,000, or 93%, from domestic sources and $277,000, or 7%, from international customers.

Foreign sales consisted of shipments to five countries during the six months ended March 28, 2015 and two countries during the six months ended March 29, 2014. A sale is attributed to a foreign country based on

the location of the contracting party. Domestic revenue may include the sale of products shipped through domestic resellers or manufacturers to international destinations. The table below summarizes our principal foreign sales by country during the first six months of fiscal 2015 and 2014:

	2015	2014
Egypt	$ 1,844,000	$
Taiwan	76,000	
Colombia		245,000
Saudi Arabia	2,000	32,000
Other	53,000	
	$ 1,975,000	$ 277,000

For the six months ended March 28, 2015, product sales revenue was derived primarily from shipments of our DSD 72A-SP military bulk encryption system to a customer in Egypt amounting to $1,808,000 and shipments of our narrowband radio encryptors to a domestic customer for deployment into Afghanistan amounting to $546,000. We also sold our link encryptor to a domestic contractor for deployment into the Middle East amounting to $432,000. In addition, the Company made shipments of our narrowband radio encryptors to supply the secure radio and telephone encryption solutions for a domestic prime contractor supporting a government customer in North Africa amounting to $116,000 during the period. We also sold our internet protocol encryptor to a customer in Taiwan amounting to $76,000.

For the six months ended March 29, 2014, product sales revenue was derived from the Company making additional shipments, amounting to $1,764,000, to the U.S. Army Communications and Electronics Command to upgrade the DSD 72A-SP military bulk encryption system currently in use by the Government of Egypt. The Company also made shipments of our narrowband radio encryptors to a U.S. radio manufacturer for deployment into Afghanistan amounting to $908,000, and shipments of our narrowband radio encryptors, while supplying customized cryptographic services and tools and training, for a domestic prime contractor supporting a government customer in North Africa amounting to $408,000, during the period. In addition, we sold our secure telephone, fax, and data encryptors to a foreign customer amounting to $246,000. The Company also made shipments of our narrowband radio encryptors to supply the secure radio and telephone encryption solutions for a domestic customer supporting a government customer in North Africa amounting to $220,000 during the period. We also had royalty sales of $120,000 during the six months ended March 29, 2014 to a domestic radio manufacturer.

Gross Profit

Gross profit for the first six months of fiscal 2015 was $2,335,000, compared to gross profit of $2,676,000 for the same period of fiscal 2014. Gross profit expressed as a percentage of sales was 72% for the first six months of fiscal 2015 as compared to 70% for the first six months of fiscal 2014, due to slightly better margin sales in fiscal 2015. The 13% dollar value decrease in gross profit during the six months ended March 28, 2015 was the result of lower sales volume during the period.

Operating Costs and Expenses

Selling, General and Administrative Expenses

Selling, general and administrative expenses for the first six months of fiscal 2015 were $1,521,000, compared to $1,549,000 for the same period in fiscal 2014. This decrease of $28,000, or 2%, was attributable to decreases in general and administrative expenses of $54,000 offset by an increase in selling and marketing expenses of $26,000 during the six months ended March 28, 2015.

The decrease in general and administrative costs during the first six months of 2015 was primarily attributable to a decrease in employee stock compensation expense of $63,000 and employee bonuses of $10,000 for the period. These decreases were partially offset by an increase in professional and other public company fees of $22,000.

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The increase in selling and marketing expenses for the six months ended March 28, 2015 was primarily attributable to increases in product evaluation costs of $69,000, outside sales and marketing agreements of $38,000, personnel-related costs of $12,000 and outside consulting costs of $11,000 during the period. These increases were partially offset by decreases in bid and proposal efforts of $36,000, third party commissions of $31,000 and marketing efforts of $30,000 during the period.

Product Development Costs

Product development costs for the six months ended March 28, 2015 were $1,343,000, compared to $1,528,000 for the six months ended March 29, 2014. This decrease of $185,000, or 12%, was attributable to decreases in personnel-related costs of $25,000, project material costs of $24,000, and outside contractor costs of $14,000, and an increase in engineering support of sales and business development activities, which resulted in decreased product development costs of approximately $125,000 for the period.

Product development costs are charged to product development, billable engineering services, bid and proposal efforts or business development activities, as appropriate. Product development costs charged to billable projects are recorded as cost of sales; product development costs charged to bid and proposal efforts are recorded as selling expenses; and product development costs charged to business development activities are recorded as marketing expenses.

The Company actively sells its engineering services in support of funded research and development. The receipt of these orders is sporadic, although such programs can span over several months. In addition to these programs, the Company also invests in research and development to enhance its existing products or to develop new products, as it deems appropriate. There was no billable engineering services revenue generated during the first six months of fiscal 2015 and fiscal 2014.

Net Loss

The Company generated a net loss of $518,000 for the first six months of fiscal 2015, compared to a net loss of $1,282,000 for the same period of fiscal 2014. This decrease in net loss is primarily attributable to the tax provision recorded during the first six months of fiscal 2014, which did not occur in fiscal 2015. During the six months ended March 28, 2015, the Company was not required to and did not record a tax provision as the effective tax rate for the 2015 fiscal year is expected to be 0%, because the expected losses are not being benefited due to a full valuation allowance. During the three months ended March 29, 2014, the Company established a valuation allowance against deferred tax assets and as a result recorded an income tax provision for the six month period ended March 29, 2014 of $894,000.

The effects of inflation and changing costs have not had a significant impact on sales or earnings in recent years. As of March 28, 2015, none of the Company s monetary assets or liabilities was subject to foreign exchange risks. The Company usually includes an inflation factor in its pricing when negotiating multi-year contracts with customers.

Liquidity and Capital Resources

We believe that our overall financial condition remains strong. Our cash, cash equivalents and marketable securities at March 28, 2015 totaled $3,918,000 compared with $6,043,000 at September 27, 2014. We continue to have no long-term debt and do not expect to incur any significant indebtedness in the near future. It is anticipated that our cash balances and cash generated from operations will be sufficient to fund our near-term research and development and marketing activities.

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Cash Requirements

We believe that the combination of existing cash, cash equivalents, and highly liquid short-term investments, together with future cash to be generated by operations, will be sufficient to meet our ongoing operating and capital expenditure requirements for the foreseeable future and at least through March 2016. We also believe that, in the long term, an anticipated improvement of business prospects, billable activities and cash from operations will be sufficient to fund the Company s planned investment in product development, although we can give no assurances. Although expected to be lower for fiscal 2015 as compared to prior periods, any increase in development activities - either billable or new product related - will require additional resources, which we may not be able to fund through cash from operations. We plan to continue to closely monitor operating expenses and will reduce them if needed. In circumstances where resources may be insufficient, the Company will look to other sources of financing, including debt and/or equity investments, although we can provide no assurances that we will be successful in securing such additional financing.

Sources and Uses of Cash

The following table presents our abbreviated cash flows for the six month periods ended:

	March 28, 2015 (Unaudited)	**March 29, 2014 (Unaudited)**
Net loss	$ (518,000)	$ (1,282,000)
Changes not affecting cash	201,000	1,168,000
Changes in assets and liabilities	(1,511,000)	1,487,000
Cash (used in) provided by operating activities	(1,828,000)	1,373,000
Cash provided by (used in) investing activities	222,000	(1,440,000)
Cash used in financing activities		
Net change in cash and cash equivalents	(1,606,000)	(67,000)
Cash and cash equivalents - beginning of period	3,210,000	2,811,000
Cash and cash equivalents - end of period	$ 1,604,000	$ 2,744,000

Operating Activities

The Company generated approximately $3,201,000 less cash from operating activities in the first six months of fiscal 2015 compared to the same period in fiscal 2014. This decrease was primarily attributable to the increases in accounts receivable and inventories during the six month period ended March 28, 2015.

Investing Activities

Cash provided by investing activities during the first six months of fiscal 2015 increased by approximately $1,662,000 compared to the same period in fiscal 2014. This change is primarily attributable to fewer purchases of short-term investments in marketable securities, which was partially offset by the cash paid for the Company s investment in an unconsolidated subsidiary during the first six months of 2015.

Financing Activities

There were no financing activities during the first six months of either fiscal 2015 or 2014.

Company Facilities

On April 1, 2014, the Company entered into a new lease for its current facilities. This lease is for 22,800 square feet located at 100 Domino Drive, Concord, MA. The Company has been a tenant in this space since 1983. This is the Company s only facility and houses all manufacturing, research and development, and corporate operations. The initial term of the lease is for five years through March 31, 2019 at an annual rate of $171,000. In addition the lease contains options to extend the lease for two and one half years through September 30, 2021 and another two and one half years through March 31, 2024 at an annual rate of $171,000. Rent expense for each of the six month periods ended March 28, 2015 and March 29, 2014 was $85,000.

Backlog

Backlog at March 28, 2015 and September 27, 2014 amounted to $1,815,000 and $402,000, respectively. The orders in backlog at March 28, 2015 are expected to ship over the next six months depending on customer requirements and product availability.

Performance guaranties

Certain foreign customers require the Company to guarantee bid bonds and performance of products sold. These guaranties typically take the form of standby letters of credit. Guaranties are generally required in amounts of 5% to 10% of the purchase price and last in duration from three months to one year. At March 28, 2015 the Company had four outstanding letters of credit in the amounts of $329,000, $16,000, $14,000 and $4,000, which are secured by collateralized bank accounts totaling $363,000. These collateralized bank accounts represent cash which has restrictions on its use.

Research and development

Research and development efforts are undertaken by the Company primarily on its own initiative. In order to compete successfully, the Company must attract and retain qualified personnel, improve existing products and develop new products. No assurances can be given that the Company will be able to hire and train such technical management and sales personnel or successfully improve and develop its products.

During the six months ended March 28, 2015 and March 29, 2014, the Company spent $1,343,000 and $1,528,000, respectively, on internal product development. During the first six months of 2015, the Company s product development expenses were lower than the same period of fiscal 2014 but in line with the Company s planned commitment to research and development, and reflected the costs of product testing and production readiness efforts.

During the remainder of fiscal 2015, the Company expects to continue to focus on three principal areas: development of solutions that meet the needs of original equipment manufacturers; product enhancements that include expanded features, planned capability and applications growth; and custom solutions that tailor our products and services to meet the unique needs of our customers. Going forward, the Company expects to continue technical efforts in these areas while also increasing our systems design and integration capabilities and services offering portfolio.

It is anticipated that cash from operations will fund our near-term research and development and marketing activities through at least the end of fiscal year 2015. We also believe that, in the long term, based on current billable activities, cash from operations will be sufficient to meet the development goals of the Company, although we can give no assurances. Any increase in development activities - either billable or new product related - will require additional resources, which we may not be able to fund through cash from operations. In circumstances where resources will be insufficient, the Company will look to other sources of financing, including debt and/or equity investments.

Other than those stated above, there are no plans for significant internal product development during the remainder of fiscal 2015 and the Company does not anticipate any significant capital expenditures during the last six months of the year.

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New Accounting Pronouncements

ASU 2013-11, Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists (a consensus of the FASB Emerging Issues Task Force)

In July 2013, the FASB issued guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. This guidance requires an unrecognized tax benefit, or a portion of an unrecognized tax benefit, be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward. If a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date, the unrecognized tax benefit should be presented in the financial statements as a liability and not combined with deferred tax assets. This guidance is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2014, with early adoption permitted. This guidance was adopted by TCC during the six months ended March 28, 2015 and did not have a material impact on the financial results of the Company.

ASU 2014-09, Revenue From Contracts With Customers (Topic 606)

In May 2014, the FASB and the International Accounting Standards Board issued guidance on the principles for recognizing revenue and to develop a common revenue standard for U.S. GAAP and International Financial Reporting Standards that would: (1) remove inconsistencies and weaknesses in revenue requirements, (2) provide a more robust framework for addressing revenue issues, (3) improve comparability of revenue recognition practices across entities, industries, jurisdictions, and capital markets, (4) provide more useful information to users of financial statements through improved disclosure requirements, and (5) simplify the preparation of financial statements by reducing the number of requirements to which an entity must refer. This guidance is effective prospectively for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early adoption is not permitted. The Company is currently evaluating the impact of this guidance and is still considering whether it will have a material effect on the Company s consolidated financial statements. This guidance will become effective for TCC as of the beginning of our 2019 fiscal year.

ASU 2014-15, Presentation of Financial Statements Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity s Ability to Continue as a Going Concern

In August 2014, the FASB updated U.S. GAAP to eliminate a critical gap in existing standards. The new guidance clarifies the disclosures management must make in the organization s financial statement footnotes when management has substantial doubt about its ability to continue as a going concern. The Company is currently evaluating the impact of this guidance but does not expect its adoption will have a material effect on the Company s consolidated financial statements. The guidance applies to all companies and is effective for the annual reporting periods ending after December 15, 2016, including interim periods within that reporting period.

ASU 2015-01, Income Statement Extraordinary And Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation By Eliminating The Concept Of Extraordinary Items

In connection with the FASB s efforts to simplify accounting standards, the FASB determined that eliminating the concept of extraordinary items from GAAP would reduce the cost and complexity of applying U.S. GAAP, while maintaining or improving the usefulness of information included in financial statements. The changes in ASU 2015-01 are effective for fiscal years beginning after December 15, 2015 and interim periods within those fiscal years. Early adoption is permitted provided that the guidance is applied from the beginning of the fiscal year of adoption.

The Company is currently evaluating the impact of this guidance but does not expect its adoption will have any effect on the Company s consolidated financial statements. This guidance will become effective for TCC as of the beginning of our 2017 fiscal year.

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Management does not believe that any other recently issued, but not yet effective, accounting standards if currently adopted would have a material impact on the accompanying financial statements.

Off-Balance Sheet Arrangements

The Company does not have any off-balance sheet arrangements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Not applicable.

Item 4. Controls and Procedures

Evaluation of disclosure controls and procedures. The Company s chief executive officer and chief financial officer have reviewed and evaluated the effectiveness of the Company s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of the end of the period covered by this quarterly report. Based on that review and evaluation, the chief executive officer and chief financial officer have concluded that the Company s current disclosure controls and procedures, as designed and implemented, are effective to ensure that such officers are provided with information relating to the Company required to be disclosed in the reports the Company files or submits under the Exchange Act and that such information is recorded, processed, summarized and reported within the specified time periods.

Changes in internal control over financial reporting. There were no changes in the Company s internal control over financial reporting that occurred during the quarter ended March 28, 2015 that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

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PART II. Other Information

Item 1. Legal Proceedings

There were no legal proceedings pending against or involving the Company or its subsidiary during the period covered by this quarterly report.

Item 1A. Risk Factors

Not applicable.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not applicable.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

Not applicable.

Item 6. Exhibits

31.1	Certification of principal executive officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of principal financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certifications of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Report Instance Document

101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Calculation Linkbase Document
101.LAB	XBRL Taxonomy Label Linkbase Document
101.PRE	XBRL Presentation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

	TECHNICAL COMMUNICATIONS CORPORATION (Registrant)
May 12, 2015 Date	By: /s/ Carl H. Guild, Jr. Carl H. Guild, Jr., President and Chief Executive Officer
May 12, 2015 Date	By: /s/ Michael P. Malone Michael P. Malone, Chief Financial Officer