SL INDUSTRIES INC
Form 10-Q
November 03, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 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 September 30, 2015

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE**

SECURITIES EXCHANGE ACT OF 1934

Commission file number 1-4987

SL INDUSTRIES, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**21-0682685**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

520 Fellowship Road, Suite A114, Mt. Laurel, NJ	**08054**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: 856-727-1500

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes 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

The number of shares of common stock outstanding as of October 23, 2015 was 3,961,000.

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Item 1. Financial Statements

SL INDUSTRIES, INC.

CONSOLIDATED BALANCE SHEETS

	September 30, 2015 (Unaudited)	December 31, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	$ 5,659,000	$ 31,950,000
Receivables, net	34,581,000	33,966,000
Inventories, net	24,701,000	23,597,000
Other current assets	6,056,000	4,751,000
Deferred income taxes, net	4,493,000	6,105,000
Total current assets	75,490,000	100,369,000
Property, plant and equipment, net	17,463,000	8,070,000
Deferred income taxes, net	5,830,000	5,496,000
Goodwill	17,209,000	13,072,000
Other intangible assets, net	17,664,000	3,788,000
Other assets and deferred charges, net	1,018,000	981,000
Total assets	$ 134,674,000	$ 131,776,000
LIABILITIES		
Current liabilities:		
Short-term borrowings and current portion of long-term debt	$ 13,500,000	$
Accounts payable	17,950,000	19,285,000
Accrued income taxes	153,000	3,618,000
Accrued liabilities:		
Payroll and related costs	5,395,000	4,880,000
Other	16,503,000	16,466,000
Total current liabilities	53,501,000	44,249,000
Deferred compensation and supplemental retirement benefits	1,137,000	1,427,000
Other long-term liabilities	5,134,000	8,779,000
Total liabilities	59,772,000	54,455,000
Commitments and contingencies		

SHAREHOLDERS EQUITY		
Preferred stock, no par value; authorized, 6,000,000 shares; none issued		
Common stock, $.20 par value; authorized, 25,000,000 shares; issued, 6,496,000 and 6,656,000 shares, respectively	1,299,000	1,331,000
Capital in excess of par value	17,078,000	22,747,000
Retained earnings	86,665,000	79,415,000
Accumulated other comprehensive (loss), net of tax	(1,422,000)	(638,000)
Treasury stock at cost, 2,535,000 and 2,512,000 shares, respectively	(28,718,000)	(25,534,000)
Total shareholders equity	74,902,000	77,321,000
Total liabilities and shareholders equity	$ 134,674,000	$ 131,776,000

See accompanying notes to consolidated financial statements.

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SL INDUSTRIES, INC.

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Net sales	$ 49,675,000	$ 50,725,000	$ 147,078,000	$ 151,140,000
Cost and expenses:				
Cost of products sold	33,340,000	34,326,000	98,526,000	101,696,000
Engineering and product development	2,339,000	2,908,000	7,509,000	8,442,000
Selling, general and administrative	9,244,000	8,730,000	25,897,000	24,005,000
Depreciation and amortization	847,000	579,000	2,065,000	1,608,000
Restructuring charges	223,000		223,000	463,000
Total cost and expenses	45,993,000	46,543,000	134,220,000	136,214,000
Income from operations	3,682,000	4,182,000	12,858,000	14,926,000
Other income (expense):				
Amortization of deferred financing costs	(59,000)	(22,000)	(119,000)	(65,000)
Interest income	2,000	2,000	23,000	5,000
Interest expense	(52,000)	(7,000)	(63,000)	(21,000)
Other gain (loss), net	(669,000)	56,000	(23,000)	1,535,000
Income from continuing operations before income taxes	2,904,000	4,211,000	12,676,000	16,380,000
Income tax provision	1,067,000	1,716,000	4,421,000	5,832,000
Income from continuing operations	1,837,000	2,495,000	8,255,000	10,548,000
(Loss) income from discontinued operations, net of tax	(700,000)	400,000	(1,005,000)	402,000
Net income	$ 1,137,000	$ 2,895,000	$ 7,250,000	$ 10,950,000
Basic net income (loss) per common share				
Income from continuing operations	$ 0.46	$ 0.60	$ 2.06	$ 2.55
(Loss) income from discontinued operations, net of tax	(0.17)	0.10	(0.25)	0.10
Net income	$ 0.29	$ 0.70	$ 1.81	$ 2.65
Diluted net income (loss) per common share				
Income from continuing operations	$ 0.46	$ 0.59	$ 2.03	$ 2.52
(Loss) income from discontinued operations, net of tax	(0.17)	0.10	(0.24)	0.10

Net income	$ 0.29	$ 0.69	$ 1.79	$ 2.62
Shares used in computing basic net income (loss) per common share	3,960,000	4,145,000	4,015,000	4,137,000
Shares used in computing diluted net income (loss) per common share	3,989,000	4,204,000	4,059,000	4,178,000

SL INDUSTRIES, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Net income	$ 1,137,000	$ 2,895,000	$ 7,250,000	$ 10,950,000
Other comprehensive income, net of tax:				
Foreign currency translation	(427,000)	(314,000)	(784,000)	(196,000)
Net unrealized gain reclassified into income on sale of available-for-sale securities				(1,094,000)
Comprehensive income	$ 710,000	$ 2,581,000	$ 6,466,000	$ 9,660,000

See accompanying notes to consolidated financial statements.

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SL INDUSTRIES, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE NINE MONTHS ENDED SEPTEMBER 30,

(Unaudited)

	2015	2014
OPERATING ACTIVITIES:		
Net income	$ 7,250,000	$ 10,950,000
Adjustment for loss (income) from discontinued operations	1,005,000	(402,000)
Income from continuing operations	8,255,000	10,548,000
Adjustments to reconcile income from continuing operations to net cash provided by (used in) operating activities:		
Depreciation	1,500,000	1,138,000
Amortization	565,000	470,000
Amortization of deferred financing costs	119,000	65,000
Stock-based compensation	741,000	525,000
Excess tax benefit on stock compensation	(574,000)	
Loss on foreign exchange contracts	88,000	167,000
Losses on (recoveries of) accounts receivable	77,000	(71,000)
Deferred compensation and supplemental retirement benefits	18,000	239,000
Deferred compensation and supplemental retirement benefit payments	(308,000)	(335,000)
Deferred income taxes	1,176,000	577,000
(Gain) on sale of available-for-sale securities		(1,691,000)
Loss on sale of equipment		79,000
Changes in operating assets and liabilities, excluding the effect of business combinations and dispositions:		
Accounts receivable	3,018,000	(4,194,000)
Inventories	1,140,000	(1,442,000)
Other assets	(1,445,000)	1,245,000
Accounts payable	(2,464,000)	1,308,000
Other accrued liabilities	(139,000)	2,000
Accrued income taxes	(2,317,000)	2,888,000
Net cash provided by operating activities from continuing operations	9,450,000	11,518,000
Net cash (used in) operating activities from discontinued operations	(7,619,000)	(3,862,000)
NET CASH PROVIDED BY OPERATING ACTIVITIES	1,831,000	7,656,000
INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	(2,243,000)	(1,647,000)
Proceeds from sale of available-for-sale securities		4,054,000

Acquisition of businesses	(29,207,000)	(3,973,000)
Purchases of other assets	(240,000)	(294,000)
Net cash (used in) investing activities from continuing operations	(31,690,000)	(1,860,000)
Net cash (used in) investing activities from discontinued operations		(182,000)
NET CASH (USED IN) INVESTING ACTIVITIES	(31,690,000)	(2,042,000)
FINANCING ACTIVITIES:		
Proceeds from Senior Revolving Credit Facility	21,900,000	
Payments of Senior Revolving Credit Facility	(8,400,000)	(1,000,000)
Payments of deferred financing costs	(182,000)	(45,000)
Repurchase and retirement of common stock	(6,796,000)	
Treasury stock purchases	(3,511,000)	(106,000)
Proceeds from stock options exercised	140,000	
Excess tax benefit on stock compensation	574,000	
Net cash provided by (used in) financing activities from continuing operations	3,725,000	(1,151,000)
Net cash (used in) financing activities from discontinued operations		(36,000)
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	3,725,000	(1,187,000)
Effect of exchange rate changes on cash	(157,000)	(17,000)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(26,291,000)	4,410,000
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	31,950,000	7,163,000
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 5,659,000	$ 11,573,000
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid during the period for:		
Interest	$ 62,000	$ 54,000
Income taxes	$ 5,431,000	$ 3,418,000

See accompanying notes to consolidated financial statements.

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SL INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Unaudited)

1. Basis Of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions for Form 10-Q and Article 10 of Regulation S-X promulgated under the Securities Exchange Act of 1934, as amended. Accordingly, they do not include all the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, the accompanying financial statements contain all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation. Operating results for interim periods are not necessarily indicative of the results that may be expected for the year ending December 31, 2015. These financial statements should be read in conjunction with the Company s audited financial statements and notes thereon included in the Company s Annual Report on Form 10-K for the year ended December 31, 2014. Unless the context requires otherwise, the terms the Company, SL Industries, we, us and our mean SL Industries, Inc., a Delaware Corporat and its consolidated subsidiaries.

On November 17, 2014, SL Delaware Holdings, Inc. (SL Delaware Holdings), a wholly-owned subsidiary of the Company, entered into a definitive Stock Purchase Agreement (the Purchase Agreement) with Hubbell Power Systems, Inc. (Hubbell), a subsidiary of Hubbell Incorporated, pursuant to which SL Delaware Holdings sold all of the issued and outstanding capital stock of RFL Electronics Inc. (RFL). The Company concluded that the accounting requirements for reporting the results of operations and cash flows of the divested business as discontinued operations were met at November 17, 2014. As a result, the accompanying consolidated statements of income for 2014, the consolidated statements of cash flows for 2014, and certain amounts in these notes to the consolidated financial statements related to 2014 have been recast to reflect the presentation of the results of operations and cash flows of the formerly owned RFL businesses as discontinued operations. Refer to Note 18, Discontinued Operations , for additional information regarding this transaction.

2. Receivables

Receivables consist of the following:

	September 30, 2015	December 31, 2014
	(in thousands)	
Trade receivables	$ 34,547	$ 34,025
Less: allowance for doubtful accounts	(348)	(281)
Trade receivables, net	34,199	33,744
Recoverable income taxes	21	81
Other	361	141
Receivables, net	$ 34,581	$ 33,966

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3. Inventories

Inventories consist of the following:

	September 30, 2015	December 31, 2014
	(in thousands)	
Raw materials	$ 18,972	$ 16,865
Work in process	4,781	4,584
Finished goods	3,320	4,232
Gross inventory	27,073	25,681
Less: allowances	(2,372)	(2,084)
Inventories, net	$ 24,701	$ 23,597

During the third quarter of 2015, the Company elected to change its method of valuing inventory held at two of its manufacturing facility s reporting within our SL Montevideo Technology, Inc. (SL-MTI) subsidiary from the last-in, first-out (LIFO) method to the first-in, first-out (FIFO) method. The Company believes that the FIFO method is preferable as it better reflects the current value of inventory reported in the Company s consolidated balance sheet, provides a better matching of cost of goods sold with revenue, provides consistency across all of our operations, and FIFO is the method used by the Company s management to monitor the financial results of SL-MTI. The cumulative effect of the change was a $160,000 increase to gross margin and a $107,000 increase to net income from continuing operations, which was recorded in the third quarter of 2015. The change was not applied retrospectively to prior periods, as the effect of the change was immaterial to the consolidated financial statements of all prior periods, including interim periods.

4. Other Current Assets

Other current assets consist of the following:

	September 30, 2015	December 31, 2014
	(in thousands)	
Prepaid insurance	$ 969	$ 228
Taxes receivable [1]	2,281	299
RFL escrow [2]	1,000	2,000
Other	1,806	2,224
Other current assets	$ 6,056	$ 4,751

(1)

The increase in taxes receivable in 2015 was primarily due to an increase in TEAL Electronics Corp. s (TEAL) value-added tax receivable related to activities in Mexico.

(2) See Note 18 Discontinued Operations for further information concerning the RFL escrow.

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5. Income Per Share

The Company has presented net income (loss) per common share pursuant to Accounting Standards Codification (ASC) 260 Earnings Per Share. Basic net income per common share is computed by dividing reported net income available to common shareholders by the weighted-average number of shares outstanding for the period.

Diluted net income per common share is computed by dividing reported net income available to common shareholders by the weighted-average shares outstanding for the period, adjusted for the dilutive effect of common stock equivalents, which consist of stock options, using the treasury stock method.

There were no anti-dilutive options for the three and nine months ended September 30, 2015. There were no anti-dilutive options for the three months ended September 30, 2014. For the nine months ended September 30, 2014, 3,000 stock options were excluded from the dilutive computation as the assumed shares repurchased under the treasury method would have been anti-dilutive.

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The table below sets forth the computation of basic and diluted net income per share:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
	(in thousands, except per share amounts)			
Net income (loss) available to common shareholders:				
Basic net income available to common shareholders from continuing operations	$ 1,837	$ 2,495	$ 8,255	$ 10,548
Basic net (loss) income available to common shareholders from discontinued operations	$ (700)	$ 400	$ (1,005)	$ 402
Diluted net income available to common shareholders from continuing operations	$ 1,837	$ 2,495	$ 8,255	$ 10,548
Diluted net (loss) income available to common shareholders from discontinued operations	$ (700)	$ 400	$ (1,005)	$ 402
Shares:				
Basic weighted average number of common shares outstanding	3,960	4,145	4,015	4,137
Common shares assumed upon exercise of stock options	29	59	44	41
Diluted weighted average number of common shares outstanding	3,989	4,204	4,059	4,178
Basic net income (loss) per common share:				
Income from continuing operations	$ 0.46	$ 0.60	$ 2.06	$ 2.55
(Loss) income from discontinued operations, net of tax	(0.17)	0.10	(0.25)	0.10
Net income	$ 0.29	$ 0.70	$ 1.81	$ 2.65
Diluted net income (loss) per common share:				
Income from continuing operations	$ 0.46	$ 0.59	$ 2.03	$ 2.52
(Loss) income from discontinued operations, net of tax	(0.17)	0.10	(0.24)	0.10
Net income	$ 0.29	$ 0.69	$ 1.79	$ 2.62

6. Stock-Based Compensation

At September 30, 2015, the Company had stock-based employee compensation plans as described below. For the three and nine months ended September 30, 2015, the total compensation expense (included in selling, general and

administrative expense) related to these plans was $251,000 and $741,000 ($160,000 and $482,000 net of tax), respectively. For the three and nine months ended September 30, 2014, the total compensation expense was $191,000 and $525,000 ($116,000 and $337,000, net of tax), respectively.

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During the first quarter of 2015, the Company implemented a Long-Term Incentive Plan (the 2015 LTIP) pursuant to the 2008 Incentive Stock Plan (the 2008 Plan) which awarded restricted stock units (RSUs) to eligible executives. Under the terms of the 2015 LTIP, the number of RSUs that may vest, if any, will be based on, among other things, the Company achieving certain sales and return on invested capital (ROIC), as defined, targets during the January 2015 to December 2017 performance period. Earned RSUs, if any, cliff vest at the end of fiscal 2017 (100% of earned RSUs vest at December 31, 2017). The final value of these RSUs will be determined by the number of shares earned. The value of these RSUs is charged to compensation expense on a straight-line basis over the three year vesting period with periodic adjustments to account for changes in anticipated award amounts. The weighted-average price for these RSUs was $39.17 per share based on the grant date of February 13, 2015. During the three and nine months ended September 30, 2015, $20,000 and $54,000 was charged to compensation expense. As of September 30, 2015, total unamortized compensation expense for this grant was $198,000. As of September 30, 2015, the maximum number of achievable RSUs under the 2015 LTIP was 11,000 RSUs.

During the first quarter of 2012, the Company implemented a Long-Term Incentive Plan (the 2012 LTIP) pursuant to the 2008 Plan which awarded RSUs to eligible executives. The weighted-average price for these RSUs was $18.00 per share based on the grant date of February 17, 2012. Under the terms of the 2012 LTIP, 6,000 RSUs were earned and issued on February 27, 2015.

On May 12, 2014, the Company granted each Director 3,000 restricted shares pursuant to the 2008 Plan. The shares vest upon the first anniversary of the grant date. All shares vested and were granted under this award on May 12, 2015.

On May 28, 2015, the Company granted each Director 3,000 restricted shares pursuant to the 2008 Plan. The shares vest upon the first anniversary of the grant date. Based on the terms of the awards the value of these restricted shares is charged to compensation expense on a straight-line basis over the one year vesting period. As a result, the Company recognized $141,000 and $191,000 of stock compensation expense during the three and nine months ended September 30, 2015. As of September 30, 2015, total unamortized compensation expense for this grant was $379,000. The weighted-average price of these restricted stock grants was $38.00 per share based on the grant date of May 28, 2015. As of September 30, 2015, no shares were granted under this award.

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Stock Options

Option activity under the principal option plans as of September 30, 2015 and changes during the nine months ended September 30, 2015 were as follows:

	Outstanding Options (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Life (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding as of December 31, 2014	184	$ 19.71	3.59	$ 3,540
Granted				
Exercised	(58)	12.02		
Forfeited				
Expired				
Outstanding as of September 30, 2015	126	$ 23.23	3.50	$ 1,388
Exercisable as of September 30, 2015	28	$ 13.36	2.57	$ 590

The aggregate intrinsic value in the table above represents the total pretax intrinsic value (the difference between the Company s closing stock price on the last trading day of the third quarter of fiscal 2015 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had all option holders exercised their options on September 30, 2015. This amount changes based on the fair market value of the Company s stock. The total intrinsic value of options exercised for the nine months ended September 30, 2015 was $1,731,000. No options were exercised during the nine months ended September 30, 2014.

As of September 30, 2015, $432,000 of total unrecognized compensation cost related to stock options is expected to be recognized over a weighted-average period of 1.4 years.

During 2015, 58,000 stock options were exercised at a gross exercise value of $692,000, of which 13,000 shares of common stock were delivered by the option holders as payment for the exercise price of stock options exercised. As a result, net cash received from option exercises for the nine months ended September 30, 2015 was $140,000. No options were exercised during the nine months ended September 30, 2014. Tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options are classified as financing cash flows. The actual tax benefit realized for the tax deduction from option exercises of share-based payment arrangements totaled $616,000 for the nine months ended September 30, 2015. The Company has applied the Short-cut method in calculating the historical windfall tax benefits. All tax shortfalls will be applied against this windfall before being charged to earnings.

7. Income Tax

The Company calculates its interim tax provision in accordance with the provisions of ASC 740-270 Income Taxes Interim Reporting. For each interim period the Company estimates its annual effective income tax rate and applies the estimated rate to its year-to-date income or loss before income taxes. The Company also computes the tax provision or benefit related to items separately reported, such as discontinued operations, and recognizes the items net of their

related tax effect in the interim periods in which they occur. The Company also recognizes the effect of changes in enacted tax laws or rates in the interim periods in which the changes occur.

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For the nine months ended September 30, 2015 and September 30, 2014, the estimated income tax rate from continuing operations was 35% and 36%, respectively.

During the three and nine months ended September 30, 2015, the Company recorded additional benefits from state research and development tax credits of $47,000 and $141,000, respectively. In addition, a $69,000 benefit was recognized during the third quarter of 2015 due to a change in estimate of the 2014 federal tax credits. During the three and nine months ended September 30, 2014, the Company recorded additional benefits from state research and development tax credits of $61,000 and $183,000, respectively.

As of September 30, 2015, the Company s gross research and development tax credit carryforwards totaled approximately $1,822,000. Of these credits, approximately $743,000 can be carried forward for 15 years and will expire between 2015 and 2030, and approximately $1,079,000 of state credits can be carried forward indefinitely.

The Company has recorded gross unrecognized tax benefits, excluding interest and penalties, as of September 30, 2015 and December 31, 2014 of $915,000 and $865,000, respectively. Tax benefits are recorded pursuant to the provisions of ASC 740 Income Taxes. If such unrecognized tax benefits are ultimately recorded in any period, the Company s effective tax rate would be reduced accordingly for such period.

The Company adopted FASB Accounting Standard 2013-11 during the first quarter of 2014. The pronouncement requires the Company to offset its uncertain tax positions against certain deferred tax assets in the same jurisdiction. As of September 30, 2015, the Company reclassified $430,000 of its uncertain tax positions against its related deferred tax assets.

The Company has been examined by the Internal Revenue Service (the IRS) through the calendar year 2010. The federal and state income tax statutes are generally open for periods back to and including the calendar years 2011 and 2010, respectively. During the first quarter of 2015 the Company was contacted by the IRS to examine the calendar year 2013. The examination began in May 2015 and is expected to conclude during the second half of 2016. In addition, the Company reached a settlement with the IRS regarding the Company s transfer pricing policies. As a result of the settlement, the Company is expected to receive a refund of $394,000, excluding interest. The financial statement impact was recorded in a prior year.

It is reasonably possible that the Company s gross unrecognized tax benefits, including interest, may change within the next twelve months due to the expiration of the statutes of limitation of the federal government and various state governments by a range of zero to $348,000. The Company records such unrecognized tax benefits upon the expiration of the applicable statute of limitations or the settlement with tax authorities. As of September 30, 2015, the Company has a liability for unrecognized benefits of $281,000, $203,000, and $431,000 for federal, international, and state taxes, respectively. Such benefits relate primarily to expenses incurred in those jurisdictions.

The Company classifies interest and penalties related to unrecognized tax benefits as income tax expense. At September 30, 2015, and December 31, 2014, the Company has accrued approximately $113,000 and $81,000 for the payment of interest and penalties, respectively.

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8. Recently Adopted and Issued Accounting Pronouncements

In April 2014, the FASB issued ASU No. 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of an Entity, which amends the guidance for reporting discontinued operations and disposals of components of an entity. The amended guidance requires that a disposal representing a strategic shift that has (or will have) a major effect on an entity s financial results or a business activity classified as sale should be reported as discontinued operations. The amendments also expand the disclosure requirements for discontinued operations and add new disclosures for individually significant dispositions that do not qualify as discontinued operations. ASU 2014-08 is effective prospectively for fiscal periods beginning after December 15, 2014 (early adoption is permitted only for disposals that have not been previously reported). The implementation of this guidance did not have a material impact on the Company s consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), which provides guidance that revenue should be recognized to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 is effective for fiscal periods beginning after December 15, 2017 and may be applied either (i) retrospectively to each prior reporting period presented with an election for certain specified practical expedients, or (ii) retrospectively with the cumulative effect of initially applying the ASU recognized at the date of initial application, with additional disclosure requirements. Early application is not permitted. The Company is currently evaluating the impact of the implementation of this guidance on the Company s consolidated financial statements. The Company s management has not yet determined the method by which it will adopt the standard in 2018.

In January 2015, the FASB issued ASU No. 2015-01, Income Statement Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items, which removes the concept of extraordinary items from U.S. GAAP. Companies are no longer required to assess whether an event or transaction is both unusual in nature and infrequent in occurrence and to separately present any such items on the statement of operations after income from continuing operations. Such items will either be presented as a separate component of income from continuing operations or disclosed in the notes to the financial statements. ASU 2015-01 is effective for fiscal periods beginning after December 15, 2015. The implementation of this guidance is not expected to have a material impact on the Company s consolidated financial statements.

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In April 2015, the FASB issued ASU No. 2015-03, Interest Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs, which requires debt issuance costs related to a recognized debt liability to be presented in the balance sheet as a direct deduction from the debt liability rather than as an asset. ASU 2014-15 is effective on for fiscal years beginning after December 15, 2015. Early adoption is permitted. Upon adoption, an entity must apply the new guidance retrospectively to all prior periods presented in the financial statements, and must provide certain disclosures about the change in accounting principle, including the nature of and reason for the change, the transition method, a description of the prior-period information that has been retrospectively adjusted and the effect of the change on the financial statement line items (that is, debt issuance cost asset and the debt liability). The implementation of this guidance is not expected to have a material impact on the Company s consolidated financial statements.

In April 2015, the FASB issued ASU No. 2015-05, Intangibles Goodwill and Other Internal-Use Software (Subtopic 350-40): Customer s Accounting for Fees Paid in a Cloud Computing Arrangement, which clarifies that if a cloud computing arrangement includes a software license, the customer should account for the license in a manner consistent with its accounting for other software licenses. If the arrangement does not include a software license, the customer should account for the arrangement as a service contract. ASU 2015-05 is effective for fiscal years beginning after December 15, 2015. The implementation of this guidance is not expected to have a material impact on the Company s consolidated financial statements.

In June 2015, the FASB issued ASU No. 2015-10, Technical Corrections and Improvements, which amends a number of Topics in the FASB Accounting Standards Codification, which updates the Codification for non-substantive technical corrections, clarifications, and improvements that are not expected to have a significant effect on accounting practice or create a significant administrative cost to most entities. The amendments that require transition guidance are effective for all entities for fiscal years, and interim periods within those years, beginning after December 15, 2015. All other amendments were effective immediately. The implementation of this guidance is not expected to have a material impact on the Company s consolidated financial statements.

In July 2015, the FASB issued ASU No. 2015-11, Inventory (Topic 330): Simplifying the Measurement of Inventory, which requires entities to measure inventory, excluding inventory measured using last-in, first out or the retail inventory method, at the lower of cost and net realizable value. ASU 2015-11 is effective for fiscal years beginning after December 15, 2016 with early adoption permitted. The Company is currently evaluating the impact of the implementation of this guidance on the Company s consolidated financial statements.

In September 2015, the FASB issued ASU No. 2015-16, Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments, which eliminates the requirement for an acquirer in a business combination to account for measurement-period adjustments retrospectively. Acquirers must now recognize measurement-period adjustments during the period in which they determine the amount of the adjustment. ASU 2015-16 is effective for fiscal years beginning after December 15, 2015 and should be applied prospectively to adjustments for provisional amounts that occur after the effective date. Early adoption is permitted for financial statements that have not been issued. The implementation of this guidance is not expected to have a material impact on the Company s consolidated financial statements.

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9. Acquisitions

Acquisitions in Fiscal 2015

On May 22, 2015, the Company acquired certain assets and assumed certain liabilities of ITT Torque Systems, Inc. (Torque Systems), pursuant to an Asset Purchase Agreement for an initial purchase price of $9,000,000, plus a working capital adjustment of $169,000 (the Torque Systems Acquisition). The transaction was paid in cash on May 22, 2015 while the working capital adjustment was paid during the fourth quarter of 2015. Torque Systems designs and manufactures engineered motion control products, including brush servo motors, brushless servo motors, incremental encoders, and linear actuators. In connection with the Torque Systems Acquisition, SL-MTI recorded direct acquisition costs of approximately $186,000 during the first nine months of 2015, which are recorded within selling, general and administrative expenses in the Consolidated Statements of Income. SLMTI DS LLC (SLMTI DS), a subsidiary of SL-MTI, holds the assets acquired in the Torque Systems Acquisition.

At September 30, 2015, the financial statements reflect the preliminary purchase price allocation based on estimated fair values at the date of acquisition. The acquisition resulted in intangible assets of $3,343,000 and goodwill of $1,176,000, which is deductible for tax purposes (see Note 10 for additional information).

The Company continues to evaluate certain assets and liabilities related to the Torque Systems Acquisition. Additional information, which existed as of the acquisition date but was at that time unknown to the Company, may become known during the remainder of the measurement period. Changes to amounts recorded as assets or liabilities may result in a corresponding adjustment to goodwill. The determination of the estimated fair values of all assets and liabilities acquired is expected to be completed during the fourth quarter of 2015.

For the three and nine months ended September 30, 2015, $2,102,000 and $2,783,000 of net revenue was included in the Company s consolidated statement of income due to Torque Systems. For the three and nine months ended September 30, 2015, $249,000 and $153,000 of income from operations was included in the Company s consolidated statement of income due to Torque Systems. Income from operations for the nine months ended September 30, 2015 was negatively impacted by direct acquisition costs previously mentioned. The results from the acquisition date through September 30, 2015 are included in the SL-MTI segment.

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On July 27, 2015, the Company acquired all of the issued and outstanding stock of Davall Gears, LTD. (Davall) pursuant to a Share Purchase Agreement (SPA) for a purchase price of £13,035,000, which was approximately $20,207,000 at the exchange rates then in effect, subject to certain adjustments, principally the Completion Statement adjustment, as defined in the SPA (the Davall Acquisition). The transaction was paid for primarily from borrowings under the Company s 2012 Credit Facility with the remainder in cash. Davall, headquartered in Welham Green, Hatfield, Hertfordshire, United Kingdom, is a manufacturer of custom gears, gearboxes, and assemblies primarily for the military and aerospace markets. Davall specializes in the design and manufacture of high precision, special form geometry gearing, and Spiradrive gear systems. In connection with the Davall Acquisition, SL-MTI recorded $1,028,000 of direct acquisition costs, of which $913,000 is recorded within selling, general and administrative expenses and $115,000 is recorded in other gain (loss), net in the Consolidated Statements of Income, and a $325,000 non-cash inventory purchase accounting adjustment, which is recorded within costs of products sold in the Consolidated Statements of Income. SL-MTI holds the assets acquired and liabilities assumed in the Davall Acquisition.

At September 30, 2015, the financial statements reflect the preliminary purchase price allocation based on estimated fair values at the date of acquisition. As of the acquisition date, the acquisition resulted in intangible assets of $11,044,000 and goodwill of $2,982,000, which consists largely of new product offerings and new sales channels expected from combining the operations of SL-MTI and Davall. None of the goodwill recognized is expected to be deductible for income tax purposes (see Note 10 for additional information).

The following table summarizes the amounts of the assets acquired and liabilities assumed as of the acquisition date:

	July 27, 2015
Receivables	$ 2,726,000
Inventories	1,354,000
Other assets	267,000
Property, plant and equipment	5,796,000
Identifiable intangible assets	11,044,000
Accounts payable	(834,000)
Warranty	(165,000)
Accrued liabilities	(2,963,000)
Goodwill	2,982,000
Total consideration transferred	$ 20,207,000

The Company continues to evaluate certain assets and liabilities related to the Davall Acquisition. Additional information, which existed as of the acquisition date but was at that time unknown to the Company, may become known during the remainder of the measurement period. Changes to amounts recorded as assets or liabilities may result in a corresponding adjustment to goodwill. The determination of the estimated fair values of all assets and liabilities acquired is expected to be completed during fiscal year 2015.

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For the three and nine months ended September 30, 2015, $2,416,000 of net revenue was included in the Company s consolidated statement of income due to Davall. For the three and nine months ended September 30, 2015, a $676,000 loss from operations was included in the Company s consolidated statement of income due to Davall. The loss from operations was primarily due to the direct acquisition costs previously mentioned. The results from the acquisition date through September 30, 2015 are included in the SL-MTI segment.

Acquisition in Fiscal 2014

On July 25, 2014, the Company acquired certain assets and assumed certain liabilities of Dynetic Systems, Inc. (Dynetic), pursuant to an Asset Purchase Agreement for an initial purchase price of $4,000,000 less a working capital adjustment of $27,000 (the Dynetic Acquisition). The transaction was paid in cash. The Asset Purchase Agreement also includes a possible earn-out, initially estimated at $310,000, which is comprised of annual payments based on sales of Dynetic products and sales to Dynetic customers over the period immediately following the date of the Dynetic Acquisition through December 31, 2017. Dynetic designed, developed and manufactured precision quality, instrument grade motion control products, and provided custom motor and motion control solutions to the aerospace, defense, medical, commercial and industrial markets. SLMTI DS holds the assets acquired in the Dynetic Acquisition.

As of September 30, 2015, the total liability for the estimated earn-out was $216,000. During the first nine months of 2015, the Company reversed $72,000 of previously recorded expense associated with the fiscal 2015 earn-out provision since it was deemed that the annual target would not be achieved. The Company has an accrual established for the annual 2016 and 2017 earn-out targets. The Dynetic results from the date of acquisition through September 30, 2015 are included in the SL-MTI segment.

Unaudited proforma financial information has not been presented for any of these acquisitions since the effects of the acquisitions were not material individually or in the aggregate in 2015 and 2014.

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10. Goodwill And Intangible Assets

Intangible assets consist of the following:

	Amortizable Life (years)	September 30, 2015 Gross Value	Accumulated Amortization	Net Value	December 31, 2014 Gross Value	Accumulated Amortization	Net Value
				(in thousands)			
Finite-lived intangible assets:							
Customer relationships [1] [2]	5 to 10	$ 11,817	$ 4,100	$ 7,717	$ 5,378	$ 3,858	$ 1,520
Patents [3]	5 to 20	1,523	1,236	287	1,501	1,223	278
Developed technology [1] [2]	5 to 10	6,630	1,801	4,829	1,980	1,719	261
License [2]	10	421		421			
Trademarks	2	60	35	25	60	13	47
Backlog [1] [2]	1 to 2	530	35	495			
Non-compete agreements	5	11	3	8	11	1	10
Total amortized finite-lived intangible assets		20,992	7,210	13,782	8,930	6,814	2,116
Indefinite-lived intangible assets:							
Trademarks [1] [2]		3,882		3,882	1,672		1,672
Other intangible assets, net		$ 24,874	$ 7,210	$ 17,664	$ 10,602	$ 6,814	$ 3,788

[1] On May 22, 2015, the Company acquired certain assets and assumed certain liabilities of Torque Systems. Included in the purchase price allocation are customer relationships valued at $1,535,000 with an estimated useful life of 5 years, developed technology valued at $1,124,000 with an estimated useful of 8 years, backlog valued at $211,000 with an estimated life of 2 years, and an indefinite-lived trademark valued at $473,000. The total weighted-average amortization period of the Torque Systems intangible assets, excluding the indefinite-lived trademark, is approximately 6 years.

[2] On July 27, 2015, the Company acquired all of the issued and outstanding stock of Davall. As of the acquisition date, included in the purchase price allocation are customer relationships valued at $4,966,000 with an estimated useful life of 10 years, developed technology valued at $3,570,000 with an estimated useful of 10 years, a royalty-free, perpetual license valued at $426,000 with an estimated useful life of 10 years, backlog valued at $323,000 with an estimated life of 1 year, and an indefinite-lived trademark valued at $1,759,000. The total weighted-average amortization period of the Davall intangible assets, excluding the indefinite-lived trademark, is approximately 10 years.

[3] During 2015, MTE Corporation (MTE) capitalized $22,000 of legal fees related to a new patent application. The estimated useful life of the asset is 20 years.

In accordance with ASC 350 Intangibles Goodwill and Other, goodwill and other indefinite-lived intangible assets are not amortized, but are tested for impairment. Such impairment testing is undertaken annually, or more frequently upon the occurrence of some indication that an impairment has taken place. The Company conducted an annual impairment

test as of December 31, 2014.

A two-step process is utilized to determine if goodwill has been impaired. In the first step, the fair value of each reporting unit is compared to the net asset value recorded for such unit. If the fair value exceeds the net asset value, the goodwill of the reporting unit is not adjusted. However, if the recorded net asset value exceeds the fair value, the Company performs a second step to measure the amount of impairment loss, if any. In the second step, the implied fair value of the reporting unit s goodwill is compared with the goodwill recorded for such unit. If the recorded amount of goodwill exceeds the implied fair value, an impairment loss is recognized in the amount of the excess.

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Going forward there can be no assurance that economic conditions or other events may not have a negative material impact on the long-term business prospects of any of the Company s reporting units. In such case, the Company may need to record an impairment loss, as stated above. The next annual impairment test will be conducted as of December 31, 2015, unless management identifies a triggering event in the interim.

Management has not identified any triggering events, as defined by ASC 350, during the nine months ended September 30, 2015. Accordingly, no interim impairment test has been performed.

Estimated future amortization expense for intangible assets subject to amortization in each of the next five fiscal years is as follows:

	Amortization Expense (in thousands)
2015	$ 1,112
2016	$ 1,954
2017	$ 1,611
2018	$ 1,561
2019	$ 1,560

Total amortization expense, excluding the amortization of deferred financing costs, consists of amortization expense related to intangible assets and software. Amortization expense related to intangible assets for the three months ended September 30, 2015 and September 30, 2014 was $291,000 and $136,000 respectively. Amortization expense related to intangible assets for the nine months ended September 30, 2015 and September 30, 2014 was $396,000 and $319,000, respectively. Amortization expense related to software for the three months ended September 30, 2015 and September 30, 2014 was $51,000. Amortization expense related to software for the nine months ended September 30, 2015 and September 30, 2014 was $169,000 and $151,000, respectively.

Changes in goodwill balances by segment (which are defined below) are as follows:

	Balance December 31, 2014	Acquisitions	Foreign Exchange	Balance September 30, 2015
		(in thousands)		
SL Power Electronics Corp.	$ 4,230	$	$ 17	$ 4,247
High Power Group:				
MTE Corporation	8,189			8,189
SL-MTI	653	4,158	(38)	4,773
Goodwill	$ 13,072	$ 4,158	$ (21)	$ 17,209

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The following table reflects the components of goodwill as of September 30, 2015, and December 31, 2014:

	September 30, 2015			December 31, 2014		
	Gross Amount	Accumulated Impairment Losses	Goodwill, Net	Gross Amount	Accumulated Impairment Losses	Goodwill, Net
	(in thousands)					
SL Power Electronics Corp.	$ 4,247	$	$ 4,247	$ 4,230	$	$ 4,230
High Power Group:						
MTE Corporation	8,189		8,189	8,189		8,189
TEAL Electronics Corp.	5,055	5,055		5,055	5,055	
SL-MTI	4,773		4,773	653		653
Goodwill	$ 22,264	$ 5,055	$ 17,209	$ 18,127	$ 5,055	$ 13,072

11. Investments

Investments in publicly traded equity securities (which include equity interests of less than 20%) are classified as available-for-sale securities. These investments are carried at fair value using quoted market prices and are included in other current assets in the Company s Consolidated Balance Sheets. Unrealized gains and losses, net of tax, are included in the determination of comprehensive income and reported in shareholders equity.

During the six months ended June 30, 2014, the Company sold all of its available-for-sale securities for total proceeds of $4,054,000. The gross realized gains on these sales totaled $1,691,000 ($1,063,000 net of tax) for the nine months ended September 30, 2014. For the purpose of determining gross realized gains, the cost of securities sold was based on the first in, first out (FIFO) method. The Company had no available-for-sale securities as of September 30, 2015 and December 31, 2014.

12. Debt

Debt as of September 30, 2015 consisted of the following:

	September 30, 2015 (in thousands)
2012 Credit Facility:	
$40 million variable interest rate senior revolving credit facility maturing in 2016	$ 13,500
Total debt	13,500
Less current portion	(13,500)
Total long-term portion	$

The Company had no debt as of December 31, 2014.

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On August 9, 2012, the Company entered into a Credit Agreement with PNC Bank, National Association, as administrative agent and lender (PNC Bank), and the lenders from time to time party thereto, as amended (the 2012 Credit Facility). The 2012 Credit Facility provides for borrowings up to $40,000,000 and under certain conditions maximum borrowings up to $70,000,000. The 2012 Credit Facility includes a sublimit for letters of credit and provides for a separate $10,700,000 letter of credit which expires one year from the date of closing, with annual extensions. The sublimit for letters of credit equals the lesser of (i) an amount equal to $5,000,000 plus the aggregate amount of Designated Usage LC issued and outstanding under the Designated Usage LC sublimit or (ii) $25,000,000. The 2012 Credit Facility expires on August 9, 2016.

Borrowings under the 2012 Credit Facility bear interest, at the Company s option, at the London interbank offering rate (LIBOR) plus a margin rate ranging from 1.25% to 2.0%, or the higher of a Base Rate plus a margin rate ranging from 0.25% to 1.0%. The Base Rate is equal to the highest of (i) the Federal Funds Open Rate plus 0.5% and (ii) the Prime Rate and (iii) the Daily Libor Rate plus 1%. The margin rates are based on certain leverage ratios, as defined. As of September 30, 2015, the interest rate under the 2012 Credit Facility equaled 1.47%. The Company is subject to compliance with certain financial covenants set forth in the 2012 Credit Facility, including, but not limited to, indebtedness to EBITDA, as defined, minimum levels of fixed charges and limitations on capital expenditures, as defined. Availability under the 2012 Credit Facility is based upon the Company s trailing twelve month EBITDA, as defined.

The Company s obligations under the 2012 Credit Facility are secured by the grant of security interests in substantially all of its assets.

On May 28, 2013 a letter of credit in the amount of $8,564,000 was issued in favor of the Environmental Protection Agency (EPA) to provide financial assurance related to the Company s annual environmental payments in accordance with the terms of the Consent Decree reached with the United States Department of Justice (DOJ) and EPA related to its liability for both the first operable unit (OU-1) and the second operable unit (OU-2) (see Note 15 for additional information). The letter of credit requires an annual commitment fee of 0.125% and standby commission of 1%, and does not reduce amounts available under the 2012 Credit Facility. On June 1, 2015, the Company made the third payment related to its obligation under the Consent Decree in the amount of $2,141,000, excluding interest. As of September 30, 2015, the total liability under the letter of credit equaled $4,282,000. The letter of credit expires on June 10, 2016, and is renewed annually.

On March 25, 2015, the Company entered into a Fourth Amendment (the Fourth Amendment) to the 2012 Credit Facility. The Fourth Amendment amends the Credit Agreement in order to, among other things: (a) allow for permitted recapitalization distributions, and (b) provide greater flexibility with certain bank covenants, including with regard to EBITDA (as defined) and fixed charges.

On May 5, 2015, the Company entered into a Fifth Amendment (the Fifth Amendment) to the 2012 Credit Facility. The Fifth Amendment amends the Credit Agreement in order to, among other things: (a) provide greater flexibility for acquisitions outside of the U.S., and (b) permit one of the Company s subsidiaries to participate in a quick pay discount program with a major customer.

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In connection with the Davall Acquisition, on July 24, 2015, the Company entered into a Sixth Amendment (the Sixth Amendment) to the 2012 Credit Facility. The Sixth Amendment amends the Credit Agreement in order to, among other things: (a) join Davall as a borrower under the 2012 Credit Facility, and (b) establish a $4,000,000 subline for loans funded in USD to be made available to Davall (see Note 9 for additional information).

The Company had an outstanding balance of $13,500,000 under the 2012 Credit Facility as of September 30, 2015. The Company had no outstanding balance under the 2012 Credit Facility as of December 31, 2014. At September 30, 2015, and December 31, 2014, the Company had total availability under the 2012 Credit Facility of $26,044,000 and $39,527,000, respectively.

13. Accrued Liabilities Other

Accrued liabilities other consist of the following:

	September 30, 2015	December 31, 2014
	(in thousands)	
Environmental	$ 7,074	$ 9,475
Warranty	1,076	1,176
Taxes (other than income) and insurance	927	879
Commissions	482	551
Foreign currency forward contracts	761	673
Other professional fees	754	496
Accrued customer incentive plans	402	414
Deferred compensation current	265	265
Litigation and legal fees	135	91
Acquisition earn-out, current		32
Deferred revenue	38	44
Other	4,589	2,370
Accrued liabilities other	$ 16,503	$ 16,466

Included in the environmental accrual are estimates for all known costs believed to be probable and reasonably estimable for sites that the Company currently operates or operated at one time (see Note 15 for additional information).

A liability is established for estimated future warranty and service claims that relate to current and prior period sales. The Company estimates warranty costs based on historical claim experience and other factors including evaluating specific product warranty issues.

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The following is a summary of activity in accrued warranty and service liabilities:

	September 30, 2015 (in thousands)
Liability, beginning of year	$ 1,176
Expense for new warranties issued	226
Accruals assumed in acquisition [1]	165
Accruals related to preexisting warranties [2]	(216)
Warranty claims paid	(275)
Liability, end of period	$ 1,076

[1] On July 27, 2015, the Company acquired all of the issued and outstanding stock of Davall. As of the acquisition date, included in the purchase price allocation is a warranty reserve valued at $165,000.

[2] During 2015, the Company reversed $216,000 of specific warranty reserves which were recognized in previous years. The specific warranty reserves were reversed primarily due to lower than anticipated customer warranty claims or due to the expiration of warranty periods.

14. Other Long-Term Liabilities

Other long-term liabilities consist of the following:

	September 30, 2015	December 31, 2014
	(in thousands)	
Environmental	$ 3,724	$ 7,384
Unrecognized tax benefits, interest and penalties	598	549
Long-term incentive plan	596	558
Acquisition earn-out, long-term	216	288
Other long-term liabilities	$ 5,134	$ 8,779

15. Commitments and Contingencies

The Company is involved in certain legal and regulatory actions. Management believes that the ultimate resolution of such matters is unlikely to have a material adverse effect on the Company s financial condition or results of operations, except as described below.

Letters Of Credit: As of September 30, 2015 and December 31, 2014, the Company was contingently liable for $456,000 and $473,000, respectively, under an outstanding letter of credit issued for casualty insurance requirements.

As of September 30, 2015 and December 31, 2014, the Company was contingently liable for $4,282,000 and $6,423,000, respectively, under an outstanding letter of credit issued to provide financial assurance related to the Company s environmental payments in accordance with the terms of the Consent Decree reached with the DOJ and EPA related to its liability for both OU-1 and OU-2.

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Litigation: The Company has been and is the subject of administrative actions that arise from its ownership of SL Surface Technologies, Inc. (SurfTech), a wholly-owned subsidiary, the assets of which were sold in November 2003. SurfTech formerly operated chrome-plating facilities in Pennsauken Township, New Jersey (the Pennsauken Site) and Camden, New Jersey (the Camden Site).

In 2006 the EPA named the Company as a potential responsible party (a PRP) in connection with the remediation of the Puchack Well Field, which has been designated as a Superfund Site. The EPA is remediating the Puchack Well Field Superfund Site in two separate operable units. The first operable unit (OU-1) consists of an area of chromium groundwater contamination in three aquifers that exceeds the selected cleanup standard. The second operable unit (OU-2) pertains to sites that are allegedly the sources of contamination for the first operable unit.

The Company has reached an agreement with both the DOJ and EPA effective April 30, 2013 related to its liability for both OU-1 and OU-2 pursuant to the terms of a Consent Decree which governs the agreement. Specifically, the Company has agreed to perform the remediation for OU-2 and pay a fixed sum for the EPA s past cost for OU-2 and a portion of the EPA s past cost for OU-1. The payments are to be made in five equal payments of $2,141,000, for a total $10,705,000, plus interest. The Company has also agreed to pay the EPA s costs for oversight of the OU-2 remediation. The United States District Court judge signed the Consent Decree effective April 30, 2013, thereby triggering the Company s obligation under the Consent Decree. The Company has made three payments totaling $6,569,000 which includes interest, related to its obligation under the Consent Decree with the most recent payment being made on June 1, 2015. The fourth and fifth payments will be made on the anniversary of the prior year s payment plus ten days in the amount of $2,141,000, plus interest. In 2013, the Company had obtained financial assurances for the OU-2 remediation and the fixed payments as required by the terms of the Consent Decree. The financial assurance is reduced annually as the fixed payments are made. Also, the financial instruments did not affect the Company s availability under its Credit facility (see Note 12 Debt).

The Company s consultants performed a significant amount of work at the Pennsauken Site during 2015, which included demolition of the Company s former facility and a building on an adjacent property, shoring, equipment mobilization and have been excavating and treating the impacted soils as required. Treatment of impacted soils at the site is approximately 70% complete. The Company s consultants are also conducting remediation on an adjacent site. The location of the chromium impacted soils and geology has required additional characterization to complete the off-site remediation. After additional testing, remedial options will be presented to the EPA. An additional accrual was recorded during the quarter to provide a reserve for the cost arising from the work beyond the scope of the original project design. The Company s consultants have been providing the EPA with progress reports on a monthly basis. The Company expects to incur significant remediation costs in the fourth quarter of 2015, which have been accrued.

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During the third quarter of 2012, the Company s legal counsel was notified by the Assistant Attorney General of the State of New Jersey that they may file a claim for certain costs. On December 3, 2012, the Company received a demand letter from the State of New Jersey. The demand was for $1,300,000 for past and future cleanup costs and $500,000 for natural resource damages (NRD) for a total of $1,800,000. Although the Company and its counsel believe that it has meritorious defenses to any claim for reimbursement of past cost and NRD damages, the Company has offered to pay $250,000, which has been accrued, to fully resolve the claim presented by the State of New Jersey for past costs, future costs and NRD at the Puchack Well Field Superfund site. On June 29, 2015 the Company s legal counsel received a letter from New Jersey s Deputy Attorney General rejecting the Company s counter offer, but stated that the matter was open for further negotiations. The Company is standing by its original defenses and has opened a dialogue with the New Jersey Deputy Attorney General. No further communication has been received from the New Jersey Deputy Attorney General regarding this matter.

Other

On March 10, 2015, Compass Directional Guidance, Inc. (Compass) filed a complaint (the Complaint) against SL-MTI in the District Court in Harris County, Texas. The Complaint seeks damages in excess of $18 million arising from the SL-MTI s sale of certain brushless motors to Compass. Compass asserts that SL-MTI breached express and implied warranties, violated the Texas Deceptive Trade Practices Act, and negligently misrepresented the quality, specification and uses of its motors to Compass. SL-MTI intends to vigorously defend the claims asserted in the Complaint which it believes are limited by the contractual terms between the parties as well as the applicable statute of limitations, and are substantially without merit. The complaint is currently in the discovery phase. A trial date is currently set for April 2016.

In the ordinary course of its business the Company is and may be subject to other loss contingencies pursuant to foreign and domestic federal, state and local governmental laws and regulations and may be party to certain legal actions, frequently involving complaints by terminated employees and disputes with customers, suppliers and others. In the opinion of management, any such other loss contingencies are not expected to have a material adverse effect on the financial condition or results of operations of the Company.

Environmental Matters: Loss contingencies include potential obligations to investigate and eliminate or mitigate the effects on the environment of the disposal or release of certain chemical substances at various sites, such as Superfund sites and other facilities, whether or not they are currently in operation. The Company is currently participating in environmental assessments and cleanups at a number of sites and in the future may be involved in additional environmental assessments and cleanups. Based upon investigations completed to date by the Company and its independent engineering-consulting firms, management has provided an estimated accrual for all known costs believed to be probable and costs that can be reasonably estimated in the amount of $10,798,000, of which $3,724,000 is included as other long-term liabilities, with the remainder recorded as other short-term accrued liabilities, as of September 30, 2015. However, it is the nature of environmental contingencies that other circumstances might arise, the costs of which are indeterminable at this time due to such factors as changing government regulations and stricter standards, the unknown magnitude of cleanup costs, and the unknown timing and extent of the remedial actions that may be required. These other circumstances could result in additional expenses or judgments, or offsets thereto. The adverse resolution of any one or more of these other circumstances could have a material adverse effect on the business, operating results, financial condition or cash flows of the Company.

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The Company s environmental costs primarily relate to discontinued operations and such costs have been recorded in discontinued operations, net of tax.

There are three sites on which the Company may incur material environmental costs in the future as a result of past activities of its former subsidiary, SurfTech. There are two Company owned sites related to its former subsidiary, SurfTech. These sites are located in Pennsauken, New Jersey (the Pennsauken Site) and in Camden, New Jersey (the Camden Site). There is also a third site, which is not owned by the Company, referred to as the Puchack Well Field Site. The Puchack Well Field Site and the Pennsauken Site are part of the Puchack Well Field Superfund Site.

With respect to the Camden Site, the Company has reported soil contamination and a groundwater contamination plume emanating from the site. The New Jersey Department of Environmental Protection (NJDEP) approved, and the Company implemented in 2010, an interim remedial action pilot study to inject neutralizing chemicals into the unsaturated soil. Based on an assessment of post-injection data, our consultants believe the pilot study can be implemented as a full scale soil remedy to treat unsaturated contaminated soil. A Remedial Action Workplan (RAWP) for soils is being developed. The RAWP will select the injection remedy as the site wide remedy for unsaturated soils, along with demolition and proper disposal of the former concrete building slab and targeted excavation and disposal of impacted soil immediately underlying the slab. Additionally, the RAWP will address a small area of impacted soil off the property. The RAWP for soils is expected to be submitted to the NJDEP in the fourth quarter of 2015, by the Licensed Site Remediation Professional (LSRP) for the site. The RAWP for treatment of unsaturated soils is scheduled to be implemented in the fourth quarter of 2015. The Company s environmental consultants also implemented an interim remedial action pilot study to treat on-site contaminated groundwater, which consisted of injecting food-grade product, into the groundwater at the down gradient property boundary, to create a bio-barrier. Post-injection groundwater monitoring to assess the bio-barrier s effectiveness was completed. Consistent decreases in target contaminants concentrations in groundwater were observed. In December 2014, a report was submitted to the NJDEP stating sufficient information was obtained from the pilot study to complete the full scale groundwater remedy design. A full scale groundwater bioremediation will be implemented in 2016 following the soil remediation mentioned above.

As previously reported, the Company is currently participating in environmental assessments and cleanups at a number of sites. One of these sites is a commercial facility, located in Wayne, New Jersey. Contaminated soil and groundwater has undergone remediation with NJDEP and LSRP oversight, but contaminants of concern (COCs) in groundwater and surface water, which extend off-site, still remain above applicable NJDEP remediation standards. A soil remedial action plan has been developed to remove the new soil source contamination that continues to impact groundwater. Our LSRP completed a supplemental groundwater remedial action, pursuant to a RAWP filed with, and permit approved by, the NJDEP. The remedial action consisted of additional in-situ injections of food grade product into on-site groundwater and post-performance groundwater monitoring. The in-situ injections are completed, and remedial action performance monitoring for groundwater is scheduled to occur through 2015. Enhancements to the existing vapor intrusion system were completed in the fourth quarter 2014. No site constituents of concern were detected at concentrations exceeding applicable NJDEP indoor air screening levels. A report was filed with the NJDEP on March 23, 2015. The Company s

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consultants have developed cost estimates for supplemental remedial injections, soil excavation and additional tests and remedial activities. Costs related to this site are recorded as part of discontinued operations, net of tax. The Remedial Investigation deadline for this site has been extended to May 7, 2016.

The Company s sale of RFL triggered certain requirements of the Industrial Site Recovery Act (ISRA), which applies to New Jersey statutorily, defined transactions involving industrial establishments. Under the stock purchase agreement pursuant to which RFL was sold (the RFL-SPA), the Company agreed to undertake, or cause to undertake, all actions necessary to comply with ISRA arising from the RFL-SPA. The Company hired an LSRP to complete a Preliminary Assessment. Based on the Preliminary Assessment, the LSRP recommended the completion of a site investigation (the Site Investigation) for certain areas of concern, including the sampling of on-site soils and installation and sampling of temporary groundwater wells, which will continue through the first quarter of 2016. Also, the Company s LSRP anticipates that an ecological evaluation of the pond and installation of permanent groundwater monitoring wells will be conducted by the end of second quarter 2016. A Preliminary Assessment Report and Site Investigation Report are scheduled to be filed with the NJDEP by November 17, 2016 under a one-year filing extension with the NJDEP. Based on the outcome of the Preliminary assessment and Site Investigation, the Company may be obligated to perform additional investigation or remediation.

The Company has reported soil and groundwater contamination at the facility of SL-MTI located on its property in Montevideo, Minnesota. An analysis of the contamination has been completed and a remediation plan has been implemented at the site pursuant to the remedial action plan approved by the Minnesota Pollution Control Agency (MPCA). A soil vapor extraction system has been operating at the site since October 2008. In 2013 the regulatory and screening levels for soil vapor and groundwater were lowered for some of the contaminants at the site. In response to this regulatory change, SL-MTI s consultants are conducting additional testing to delineate site impacts and update the site conceptual model. A work plan was submitted to MPCA and approved on September 22, 2014. An Investigation Report and Monitoring Well Work Plan (WP) was submitted to the MPCA during the third quarter of 2015. No site work has been completed to date in 2015 as the MPCA has yet to respond the WP. Pending the approval of the WP, additional investigations, monitoring wells or remedial actions may be required in the future. Costs related to this site are recorded as a component of continuing operations.

As of September 30, 2015 and December 31, 2014, environmental accruals of $10,798,000 and $16,859,000, respectively, have been recorded by the Company in accrued liabilities other and in other long-term liabilities, as appropriate (see Notes 13 and 14 for additional information).

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16. Segment Information

The Company has historically operated under four business segments: SL Power Electronics Corp. (SLPE), the High Power Group, SL-MTI and RFL. On November 17, 2014, the Company completed the sale of all the issued and outstanding capital stock of RFL and classified the results of operations of its RFL segment as discontinued operations. As a result, the Company currently operates under three business segments from continuing operations: SLPE, the High Power Group, and SL-MTI. TEAL Electronics Corp. (TEAL) and MTE Corporation (MTE) are combined into one business segment, which is reported as the High Power Group. The Company aggregates operating business subsidiaries into a single segment for financial reporting purposes if aggregation is consistent with the objectives of ASC 280 Segment Reporting. Business units are also combined if they have similar characteristics in each of the following areas:

nature of products and services

nature of production process

type or class of customer

methods of distribution

SLPE designs, manufactures and markets high-reliability power conversion products in internal and external footprints. The Company s power supplies provide a reliable and safe power source for the customer s specific equipment needs. SLPE, which sells products under three brand names (SL Power Electronics, Condor and Ault), is a major supplier to the original equipment manufacturers (OEMs) of medical, industrial/instrumentation, military, information technology equipment, and LED lighting and audio visual systems. The High Power Group sells products under two brand names (TEAL and MTE). TEAL designs and manufactures custom power conditioning and distribution units for OEMs of medical imaging, medical treatment, military aerospace, semiconductor, solar and advanced simulation systems. MTE designs and manufactures power quality products used to protect equipment from power surges, bring harmonics into compliance and improve the efficiency of variable speed motor drive systems. SL-MTI designs and manufactures high power density precision motors that are used in numerous applications, including military and commercial aerospace, oil and gas, and medical and industrial products. With the acquisition of Torque Systems, SL-MTI s product portfolio has expanded to include engineered motion control products, including brush servo motors, brushless servo motors, incremental encoders, and linear actuators. SL-MTI s product portfolio was further expanded by the Davall acquisition, which includes custom gears, gearboxes, and assemblies primarily for the military and aerospace markets. The Unallocated Corporate Expenses segment includes corporate related items, financing activities and other costs not allocated to reportable segments, which includes but is not limited to certain treasury, risk management, legal, litigation and public reporting charges and certain legacy costs. The accounting policies for the business units are the same as those described in the summary of significant accounting policies. For additional information, see Note 1 of the Notes to the Consolidated Financial Statements included in Part IV of the Company s Annual Report on Form 10-K for the year ended December 31, 2014.

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Business segment operations are conducted through domestic subsidiaries. For all periods presented, sales between business segments were not material. Each of the segments has certain major customers, the loss of any of which would have a material adverse effect on such segment.

The unaudited comparative results for the three and nine month periods ended September 30, 2015 and September 30, 2014 are as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
	(in thousands)		(in thousands)	
Net sales				
SLPE	$ 17,243	$ 17,821	$ 51,687	$ 54,504
High Power Group	15,224	21,699	53,366	64,461
SL-MTI	17,208	11,205	42,025	32,175
Net sales	$ 49,675	$ 50,725	$ 147,078	$ 151,140

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
	(in thousands)		(in thousands)	
Income from operations				
SLPE	$ 2,416	$ 1,971	$ 6,140	$ 5,203
High Power Group	1,028	2,838	5,914	9,676
SL-MTI	1,791	1,243	6,200	5,146
Unallocated Corporate Expenses [1]	(1,553)	(1,870)	(5,396)	(5,099)
Income from operations	$ 3,682	$ 4,182	$ 12,858	$ 14,926

(1) Unallocated Corporate Expenses includes corporate related items, financing activities and other costs not allocated to reportable segments, which includes but is not limited to certain legal, litigation and public reporting charges and certain legacy costs.

Total assets as of September 30, 2015 and December 31, 2014 are as follows:

	September 30, 2015	December 31, 2014
	(in thousands)	
Total assets		
SLPE	$ 33,128	$ 34,989

High Power Group	33,267	33,306
SL-MTI	58,236	22,752
Unallocated Corporate Assets	10,043	40,729
Total assets	$ 134,674	$ 131,776

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Goodwill and other intangible assets, net, as of September 30, 2015 and December 31, 2014 are as follows:

	September 30, 2015	December 31, 2014
	(in thousands)	
Goodwill and other intangible assets, net		
SLPE	$ 4,547	$ 4,530
High Power Group	9,848	9,839
SL-MTI	20,478	2,491
Goodwill and other intangible assets, net	$ 34,873	$ 16,860

17. Retirement Plans and Deferred Compensation

During the nine months ended September 30, 2015 and September 30, 2014, the Company maintained a defined contribution pension plan covering all full-time, U.S. employees of SLPE, the High Power Group, including TEAL and MTE, SL-MTI, and the corporate office. The Company s contributions to this plan are based on a percentage of employee contributions and/or plan year gross wages, as defined. Costs incurred under these plans amounted to $126,000 and $397,000 during the three and nine months ended September 30, 2015 compared to $114,000 and $430,000 during the three and nine months ended September 30, 2014. The decrease in 2015 was primarily due to the utilization of forfeitures within the plan to offset the Company s cost.

The Company has agreements with certain retired directors, officers and key employees providing for supplemental retirement benefits. The liability for supplemental retirement benefits is based on the most recent mortality tables available and discount rates ranging from 8% to 12%. The amount charged to expense in connection with these agreements amounted to $102,000 and $18,000 for the three month and nine month periods ended September 30, 2015. During the first nine months of 2015, the Company reversed a deferred compensation accrual due to the death of a pensioner. The amount charged to expense in connection with these agreements amounted to $88,000 and $239,000 for the three month and nine month periods ended September 30, 2014.

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18. Discontinued Operations

The results of total income from discontinued operations for the three and nine months ended September 30, 2015 and September 30, 2014 were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
	(in thousands)		(in thousands)	
(Loss) income from discontinued operations before income taxes:				
Divested operations RFL	$	$ 808	$	$ 1,219
Environmental costs	(1,150)	(205)	(1,652)	(641)
Total (loss) income from discontinued operations before income taxes	$ (1,150)	$ 603	$ (1,652)	$ 578
(Loss) income from discontinued operations, net of tax:				
Divested operations RFL	$	$ 525	$	$ 792
Environmental costs	(700)	(125)	(1,005)	(390)
Total (loss) income from discontinued operations, net of tax	$ (700)	$ 400	$ (1,005)	$ 402

The loss from discontinued operations due to environmental costs in 2015 and 2014 is related to remediation costs, consulting fees, and legal expenses associated with the past operations of the Company s five environmental sites (See Note 15 Commitments and Contingencies for further information concerning the environmental sites).

On November 17, 2014, SL Delaware Holdings, a wholly-owned subsidiary of the Company, entered into the Purchase Agreement with Hubbell pursuant to which SL Delaware Holdings sold all of the issued and outstanding capital stock of RFL to Hubbell for aggregate cash consideration of $20,000,000, subject to a post-closing working capital adjustment which amounted to $299,000 and was received in February 2015. As a result, the Company recognized a pre-tax gain of $6,650,000 ($4,322,000 net of tax) as of December 31, 2014.

A portion of the cash consideration was held in escrow to secure the indemnification obligations of SL Delaware Holdings. The Company was eligible to receive 50% of the total $2,000,000 escrow, or $1,000,000, subject to certain adjustments, after the first nine months from the date of sale, and the remainder after eighteen months from the date of sale. During the third quarter of 2015, the Company collected $835,000 of the escrow, which was net of a $165,000 payment related to a service agreement for a former executive. This amount had been accrued in 2014.

The Company concluded that the accounting requirements for reporting the results of operations and cash flows of the divested business as discontinued operations were met at November 17, 2014. As a result, the consolidated statements of income for 2014 and the consolidated statements of cash flows for 2014 have been recast to reflect the formerly owned RFL businesses as discontinued operations.

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The results of the discontinued operations for RFL for the three and nine months ended September 30, 2014 were as follows:

	Three Months Ended September 30, 2014	Nine Months Ended September 30, 2014
Net sales	$ 5,449	$ 14,368
Costs and expenses:		
Cost of products sold	2,624	7,117
Engineering and product development	502	1,363
Selling, general and administrative	1,415	4,319
Depreciation and amortization	98	319
Total cost and expenses	4,639	13,118
Income from operations	810	1,250
Other income (expense):		
Interest expense	(2)	(31)
Income from discontinued operations before income taxes	808	1,219
Income tax provision	283	427
Income from discontinued operations, net of tax	$ 525	$ 792

In the Consolidated Statements of Cash Flows for the nine months ended September 30, 2014, environmental costs and the financial results of the RFL segment were included in net cash (used in) operating activities from discontinued operations. The financial results of the RFL segment were included in net cash (used in) investing activities from discontinued operations and net cash (used in) financing activities from discontinued operations.

19. Fair Value Measurement and Financial Instruments

ASC 820 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. ASC 820 applies to reported balances that are required or permitted to be measured at fair value under existing accounting pronouncements; accordingly, the standard does not require any new fair value measurements of reported balances.

ASC 820 emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, ASC 820 establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity s own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

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Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access. Level 2 inputs are inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs may include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the asset or liability (other than quoted prices), such as interest rates, foreign exchange rates, and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability, which is typically based on an entity s own assumptions, as there is little, if any, related market activity. In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. 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 asset or liability.

Currently, the Company uses foreign currency forward contracts to hedge its foreign currency risk. The valuation of these instruments is determined using widely accepted valuation techniques including discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, including spot rates and market forward points. The fair value of the foreign currency forward contracts is based on interest differentials between the currencies being traded, spot rates and market forward points.

To comply with the provisions of ASC 820, the Company incorporates credit valuation adjustments to appropriately reflect both its own nonperformance risk and the respective counterparty s nonperformance risk in the fair value measurements. In adjusting the fair value of its derivative contracts for the effect of nonperformance risk, the Company has considered the impact of netting and any applicable credit enhancements, such as collateral postings, thresholds, mutual puts, and guarantees, where applicable.

Although the Company has determined that the majority of the inputs used to value its derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with its derivatives utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by itself and its counterparties. However, as of September 30, 2015, the Company has assessed the significance of the impact of the credit valuation adjustments on the overall valuation of its derivative positions and has determined that the credit valuation adjustments are not significant to the overall valuation of its derivatives. As a result, the Company has determined that its derivative valuations in their entirety are classified in Level 2 of the fair value hierarchy.

In conjunction with its implementation of updates to the fair value measurements guidance, the Company made an accounting policy election to measure derivative financial instruments subject to master netting agreements on a net basis.

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The following table presents the Company s assets and liabilities measured at fair value on a recurring basis as of September 30, 2015 and December 31, 2014, aggregated by the level in the fair value hierarchy within which those measurements fall:

	Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at September 30, 2015
		(in thousands)		
Liabilities				
Derivative financial instruments	$	$ 761	$	$ 761

	Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2014
		(in thousands)		
Liabilities				
Derivative financial instruments	$	$ 673	$	$ 673

The Company believes that the fair values of its current assets and current liabilities (cash and cash equivalents, receivables, net, short-term borrowings and current portion of long-term debt, accounts payable, and accrued liabilities) approximate their reported carrying amounts.

The Company does not have any fair value measurements using significant unobservable inputs (Level 3) as of September 30, 2015 and December 31, 2014.

Credit Risk Contingent Features

The Company has agreements with its derivative counterparties that contain a provision where if the Company defaults or is capable of being declared in default on any of its indebtedness, then the Company could also be declared in default on its derivative obligations.

20. Derivative Instruments and Hedging Activities

ASC Topic 815, as amended and interpreted, establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. As required by ASC Topic 815, the Company records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative and the resulting designation. Derivatives used to hedge the exposure to variability in expected future cash flows related to forecasted foreign exchange-based risk are considered economic hedges of the Company s forecasted cash flows.

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Risk Management Objective of Using Derivatives

The Company is a U.S. dollars (USD) functional currency entity that manufactures products in the USA, Mexico and China. The Company s sales are priced in USD and its costs and expenses are priced in USD, Mexican pesos (MXN) and Chinese Yuan (CNH). As a result, the Company has exposure to changes in exchange rates between the time when expenses in the non-functional currencies are initially incurred and the time when the expenses are ultimately paid. The Company s objective in using derivatives is to add stability and to manage its exposure to foreign exchange risks. To accomplish this objective, the Company uses foreign currency forward contracts to manage its exposure to fluctuations in the exchange rates. Foreign currency forward contracts involve fixing the USD-MXN and USD-CNH exchange rates for delivery of a specified amount of foreign currency on a specified date.

During 2014 and 2015, the Company entered into a series of foreign currency forward contracts to hedge its exposure to foreign exchange rate movements in its forecasted expenses in China and Mexico. The foreign currency forwards are not speculative and are being used to manage the Company s exposure to foreign exchange rate movements. Foreign currency forward contracts involve fixing the USD-MXN and USD-CNH exchange rates for delivery of a specified amount of foreign currency on a specified date. The Company has elected not to apply hedge accounting to these derivatives and they are marked to market through earnings. Therefore, gains and losses resulting from changes in the fair value of these contracts are recognized at the end of each reporting period directly in earnings. The gains and losses associated with the foreign currency forward contracts are included in other gain (loss), net on the Consolidated Statements of Income. As of September 30, 2015, the fair value of the foreign currency forward contracts was recorded as a $761,000 liability in other current liabilities on the Consolidated Balance Sheets. As of December 31, 2014, the fair value of the foreign currency forward contracts was recorded as a $673,000 liability in other current liabilities on the Consolidated Balance Sheets.

Non-designated Hedges of Foreign Exchange Risk

The notional amounts are used to measure the volume of foreign currency forward contracts and do not represent exposure to foreign currency losses. The following table summarizes the notional values of the Company s derivative financial instruments as of September 30, 2015.

Product	Number of Instruments	Notional (in thousands)
Mexican Peso (MXN) Forward Contracts	16	MXN 95,741
Chinese Yuan (CNH) Forward Contracts	14	CNH 59,176

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The following table details the location in the financial statements of the gain or loss recognized on foreign currency forward contracts that are marked to market for the three and nine months ended September 30, 2015 and September 30, 2014:

Derivatives Not Designated as Hedging Instruments	Location of Income (Loss) Recognized in Income on Derivative	Amount of Gain (Loss) Recognized in Income on Derivative Three Months Ended September 30, 2015 (in thousands)	Three Months Ended September 30, 2014 (in thousands)
Foreign Exchange Contracts	Other gain (loss), net	$ (564)	$ 54

Derivatives Not Designated as Hedging Instruments	Location of Income (Loss) Recognized in Income on Derivative	Amount of Gain (Loss) Recognized in Income on Derivative Nine Months Ended September 30, 2015 (in thousands)	Nine Months Ended September 30, 2014 (in thousands)
Foreign Exchange Contracts	Other gain (loss), net	$ (88)	$ (167)

21. Other Gain (Loss), net

Other gain (loss), net for the nine months ended September 30, 2015 includes a $88,000 unrealized loss on foreign currency forward contracts (see Note 20 Derivative Instruments and Hedging Activities for further information) and $65,000 of net foreign currency transaction gains. The primary driver of the net foreign currency transaction gains were the fluctuations in the value of the USD to CNH and fluctuations in the value of the USD to British Pound (GBP). Other gain (loss), net for the nine months ended September 30, 2014 includes a $1,691,000 gain recognized from the sale of available-for-sale securities (see Note 11 Investments for further information) and $11,000 of dividend income received from investments in available-for-sale securities, which were partially offset by a $167,000 unrealized loss on foreign currency forward contracts.

22. Supplemental Cash Flow Information

For the nine months ended September 30, 2015 and September 30, 2014, net cash used in operating activities from discontinued operations was $7,619,000 and $3,862,000, respectively. In 2015, net cash used in operating activities from discontinued operations was primarily related to environmental payments. In 2014, net cash used in operating activities from discontinued operations was primarily related to environmental payments previously mentioned, which was partially offset by an add back of depreciation and amortization expense associated with the formerly owned RFL segment (see Note 18 for additional information).

For the nine months ended September 30, 2014, net cash used in investing activities from discontinued operations was $182,000. In 2014, net cash used in investing activities from discontinued operations was related to purchases of property, plant and equipment by the Company s formerly owned RFL segment. Net cash used in investing activities from discontinued operations was zero in 2015.

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23. Shareholders Equity

On March 27, 2015, the Company announced a modified Dutch Auction Tender Offer to purchase up to $20 million of its common shares (the Tender Offer). The Tender Offer expired at the end of the day on April 23, 2015. Under the terms of the Tender Offer, the Company s shareholders had the option of tendering all or a portion of the Company s common stock that they owned (1) at a price of not less than $39.00 and not greater than $42.00, in increments of $0.25 per share, or (2) without specifying a purchase price, in which case the common stock that they owned would have been purchased at the purchase price determined in accordance with the Tender Offer. All common stock purchased by the Company in the Tender Offer were purchased at the same price.

The Company accepted for purchase approximately 160,000 shares of its common stock at a purchase price of $42.00 per share. These shares represented approximately 3.9% of the total common stock outstanding as of April 24, 2015 prior to the purchase of shares pursuant to the Tender Offer. Upon completion of the Tender Offer, the Company had approximately 3,934,000 shares of common stock outstanding at that time. The aggregate purchase price paid by the Company in connection with the Tender Offer was $6,734,000 excluding transaction costs. On April 27, 2015, the Company paid for the Tender Offer with available cash on hand.

On December 24, 2014, the Board of Directors authorized a plan that allows for the repurchase up to an aggregate of 420,000 shares of the Company s outstanding common stock (the 2014 Repurchase Plan). Any repurchases pursuant to the 2014 Repurchase Plan would be made in the open market or in negotiated transactions. During the first nine months of 2015, the Company purchased approximately 89,000 shares of Company stock at an average price of $39.37 a share. As a result, as of September 30, 2015, approximately 331,000 shares remained available for purchase under the 2014 Repurchase Plan. Currently, the 2014 Repurchase Plan has no expiration date.

24. Related Party Transactions

On May 1, 2014, the Company renewed the Management Services Agreement (Management Services Agreement) with SP Corporate Services LLC (SP Corporate). SP Corporate is an affiliate of SPH Group Holdings LLC (SPHG). A member of the Company s Board of Directors, Warren G. Lichtenstein, is affiliated with SPHG. Also, the Company s Chairman of the Board of Directors, Glen M. Kassan is affiliated with SPHG. Pursuant to the Management Services Agreement, SP Corporate agreed to provide, at the direction of the Company s Chief Executive Officer (CEO), non-exclusive services to support the Company s growth strategy, business development, planning, execution assistance and related support services. The monthly fee for these services is $10,400 paid in advance. The Management Services Agreement has a term of one year and has been approved by the Audit Committee of the Board of Directors and a majority of the disinterested directors of the Company.

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On March 25, 2015, the Company and SP Corporate entered into an amendment to the Management Services Agreement (the Amendment) in order to, among other things, extend the term of the Management Services Agreement until May 1, 2016, and to provide, at the direction of the Company s CEO, non-exclusive services to support the Company s talent and organizational development, including transformative change management, talent recruitment, talent development (both domestic and international), organizational review services, and other related support services (the Talent Services). The services provided under the Amendment are in addition to the services provided under the Management Services Agreement prior to such amendment. The Amendment is effective May 1, 2015. Upon effectiveness of the Amendment, the monthly fee for services under the Management Services Agreement was set at $27,400 paid in advance. During the third quarter of 2015 it was determined that the Talent Services portion of the Amendment will not be utilized. Accordingly, the Amendment will be modified to exclude the Talent Services component of the Amendment and related service fee. The monthly service fee will revert back to the original amount of $10,400 to be paid in advance.

25. Restructuring Costs

Restructuring activity for the period ended September 30, 2015 was as follows:

	Accrual at Beginning of the Year	Charged to Earnings	Cash Payments	Accrual at September 30, 2015
			(in thousands)	
2015 Plan				
Severance and other employee-related charges	$	$ 223	$ 186	$ 37

2015 Restructuring Plan

During the third quarter of 2015, the Company announced to its employees a restructuring plan (2015 Restructuring Plan) to align its costs with current and projected sales activity. The costs reductions were primarily production, engineering, selling and administration employees at MTE and TEAL, which comprise the High Power Group. As of September 30, 2015, there was a consolidated charge to earnings of $223,000, which was composed of severance and other employee related charges. The total number of employees affected by the restructuring plan was 28, of which 26 had been terminated during the third quarter of 2015.

2014 Restructuring Plan

During the first quarter of 2014, the Company announced to its employees a restructuring plan (2014 Restructuring Plan) to align its costs with current and projected sales activity. The costs reductions were primarily production, engineering, selling and administration employees at TEAL, which is part of the High Power Group. As of September 30, 2014, there was a consolidated charge to earnings of $463,000, which was composed of severance and other employee related charges. The total number of employees affected by the restructuring plan was 11, all of which had been terminated during the first quarter of 2014.

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26. Non-Binding Proposal to Acquire SL Industries

On June 18, 2015, the independent members of the Company s Board of Directors received a non-binding proposal from Handy & Harman Ltd. (H&H), a publicly-traded NASDAQ company and an affiliate of Steel Partners Holdings L.P. (Steel), to acquire all the outstanding shares of common stock of the Company, through an appropriate acquisition entity, for a price of $43.00 to $45.00 per share (subject to limited confirmatory due diligence). The proposal contemplates that the Company s stockholders other than Steel would be able to elect to receive cash or stock of H&H (with Steel electing to receive all stock), subject to proration so that the aggregate consideration consists of 55% cash and 45% H&H stock.

The Company s Board of Directors has established a Special Committee of the Board (the Special Committee) comprising independent directors, which has been authorized, among other things, to evaluate the proposal. The Special Committee is reviewing and considering the proposal carefully in due course, as well as other proposals from unaffiliated third parties that have been or may be received, consistent with its fiduciary duties to act in the best interest of stockholders. There is no assurance that the Special Committee will recommend any transaction, or that any such transaction will be consummated. The Company undertakes no obligation to update this disclosure.

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ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following section highlights significant factors impacting the consolidated operations and financial condition of the Company and its subsidiaries. The following discussion should be read in conjunction with the Consolidated Financial Statements included in Part I of this Quarterly Report on Form 10-Q.

Forward-Looking Statements

In addition to other information in this Quarterly Report on Form 10-Q, this Management s Discussion and Analysis of Financial Condition and Results of Operations contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are based on current expectations and the current economic environment. These statements are not guarantees of future performance. They involve a number of risks and uncertainties that are difficult to predict, including, but not limited to, the Company s ability to implement its business plan, retain key management, anticipate industry and competitive conditions, realize operating efficiencies, secure necessary capital facilities and obtain favorable determinations in various legal and regulatory matters. Actual results could differ materially from those expressed or implied in the forward-looking statements. Some important assumptions and other critical factors that could cause actual results to differ materially from those in the forward-looking statements are specified in the Company s filings with the Securities and Exchange Commission (the SEC), including the Company s Annual Report on Form 10-K for the year ended December 31, 2014, and Current Reports on Form 8-K.

Overview

SL Industries, Inc., through its subsidiaries, designs, manufactures and markets power electronics, motion control, power protection, and power quality electromagnetic equipment that are used in a variety of medical, commercial and military aerospace, computer, datacom, industrial, LED lighting and audio visual systems, and telecom applications. Its products are generally incorporated into larger systems to improve operating performance, safety, reliability and efficiency. The Company s products are largely sold to OEMs, and, to a lesser extent, to commercial distributors. The Company is comprised of three domestic business segments, all of which have significant manufacturing operations in Mexico. SLPE has manufacturing, engineering and sales capability in China. Most of the Company s sales are made to customers who are based in the United States. The Company places an emphasis on highly engineered, well-built, high quality, dependable products and is dedicated to continued product enhancement and innovation.

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The Company s business strategy has been to enhance the growth and profitability of each of its businesses through the penetration of attractive new market niches, further improvement of operations through the implementation of lean manufacturing principles, expansion of lean principles into the transactional side of the business, and expansion of global capabilities. The Company intends to focus on improving efficiencies that better leverage the Company s resources. Lean initiatives, both on the factory floor and throughout the organization, are ongoing. The Company expects to pursue its goals during the next twelve months principally through organic growth. The Company also continues to pursue strategic alternatives to maximize shareholder value. Some of these alternatives have included, and could continue to include, selective acquisitions, divestitures and the sale of certain assets. The Company has provided, and may from time to time in the future provide, information to interested parties.

In the sections that follow, statements with respect to the quarter ended 2015 or nine months ended 2015 refer to the three month and nine month periods ended September 30, 2015. Statements with respect to the quarter ended 2014 or nine months ended 2014 refer to the three month and nine month periods ended September 30, 2014. Also, statements with respect to operating costs refer to engineering and product development costs, selling, general and administrative costs, depreciation and amortization, and restructuring costs (operating costs).

Non-Binding Proposal to Acquire SL Industries

On June 18, 2015, the independent members of the Company s Board of Directors received a non-binding proposal from Handy & Harman Ltd. (H&H), a publicly-traded NASDAQ company and an affiliate of Steel Partners Holdings L.P. (Steel), to acquire all the outstanding shares of common stock of the Company, through an appropriate acquisition entity, for a price of $43.00 to $45.00 per share (subject to limited confirmatory due diligence). The proposal contemplates that the Company s stockholders other than Steel would be able to elect to receive cash or stock of H&H (with Steel electing to receive all stock), subject to proration so that the aggregate consideration consists of 55% cash and 45% H&H stock.

The Company s Board of Directors has established a Special Committee of the Board (the Special Committee) comprising independent directors, which has been authorized, among other things, to evaluate the proposal. The Special Committee is reviewing and considering the proposal carefully in due course, as well as other proposals from unaffiliated third parties that have been or may be received, consistent with its fiduciary duties to act in the best interest of stockholders. There is no assurance that the Special Committee will recommend any transaction, or that any such transaction will be consummated. The Company undertakes no obligation to update this disclosure.

Significant Transactions and Financial Trends

On March 27, 2015, the Company announced the modified Dutch Auction Tender Offer to purchase up to $20 million of its common shares. The Company accepted for purchase approximately 160,000 shares of its common stock at a purchase price of $42.00 per share. These shares represented approximately 3.9% of the total common stock outstanding as of April 24, 2015, prior to the purchase of shares pursuant to the Tender Offer. Upon completion of the Tender Offer, the Company had approximately 3,934,000 shares of common stock outstanding at that time. The aggregate purchase price paid by the Company in connection with the Tender Offer was $6,734,000 excluding transaction costs. On April 27, 2015, the Company paid for the Tender Offer with available cash on hand.

On May 22, 2015, the Company acquired certain assets and assumed certain liabilities of Torque Systems, Inc., pursuant to an Asset Purchase Agreement for an initial purchase price of $9,000,000, plus a working capital adjustment of $169,000. The transaction was paid in cash on May 22, 2015 while the working capital adjustment was paid during the fourth quarter of 2015. Torque Systems designs and manufactures engineered motion control products, including brush servo motors, brushless servo motors, incremental encoders, and linear actuators. In connection with

the Torque Systems Acquisition, SL-MTI recorded direct acquisition costs of approximately $186,000 during the first nine months of 2015, which are recorded within selling, general and administrative expenses in the Consolidated Statements of Income. SLMTI DS, a subsidiary of SL-MTI, holds the assets acquired in the Torque Systems Acquisition. The results from the acquisition date through September 30, 2015 are included in the SL-MTI segment.

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On July 27, 2015, the Company acquired all of the issued and outstanding stock of Davall pursuant to a SPA for a purchase price of £13,035,000, which was approximately $20,207,000 at the exchange rates then in effect, subject to certain adjustments, principally the Completion Statement adjustment, as defined in the SPA. The transaction was paid for primarily from borrowings under the Company s 2012 Credit Facility with the remainder in cash. Davall, headquartered in Welham Green, Hatfield, Hertfordshire, United Kingdom, is a manufacturer of custom gears, gearboxes, and assemblies primarily for the military and aerospace markets. Davall specializes in the design and manufacture of high precision, special form geometry gearing, and Spiradrive gear systems. In connection with the Davall Acquisition, SL-MTI recorded $1,028,000 of direct acquisition costs, of which $913,000 is recorded within selling, general and administrative expenses and $115,000 is recorded in other gain (loss), net in the Consolidated Statements of Income, and a $325,000 non-cash inventory purchase accounting adjustment, which is recorded within costs of products sold in the Consolidated Statements of Income. SL-MTI holds the assets acquired and liabilities assumed in the Davall Acquisition. The results from the acquisition date through September 30, 2015 are included in the SL-MTI segment.

During the second quarter of 2013, the Company reached an agreement with both the United States DOJ and EPA related to its liability for both OU-1 and OU-2 pursuant to the terms of a Consent Decree which governs the agreement. On June 1, 2015, the Company made the third payment related to its obligation under the Consent Decree in the amount of $2,173,000, which included interest. The remaining two payments will be made on the anniversary of the prior year s payment plus ten days in the same amount of $2,141,000, plus interest.

On December 24, 2014, the Board of Directors authorized a plan that allows for the repurchase up to an aggregate of 420,000 shares of the Company s outstanding common stock (the 2014 Repurchase Plan). Any repurchases pursuant to the 2014 Repurchase Plan would be made in the open market or in negotiated transactions. During the first nine months of 2015, the Company purchased approximately 89,000 shares of Company stock at an average price of $39.37 a share. As a result, as of September 30, 2015, approximately 331,000 shares remained available for purchase under the 2014 Repurchase Plan. Currently, the 2014 Repurchase Plan has no expiration date.

Business Trends

Demand for the Company s products and services decreased during 2015 compared to 2014. Sales for the nine months ended September 30, 2015, decreased by $4,062,000 or 3%, and income from operations decreased by $2,068,000, or 14%.

Sales decreased during the nine months ended September 30, 2015 due to decreases at the High Power Group and SLPE, which were partially offset by an increase at SL-MTI. The sales decrease at the High Power Group was primarily due to a large project-based domestic order in 2014 for harmonic filters from a customer in the electronic equipment industry without a comparable large order in 2015. The sales decrease at SLPE was primarily attributable to SLPE s current strategy to exit certain low margin business while developing new products at higher margins. The increase at SL-MTI included non-comparable sales of $2,783,000 from the Torque Systems Acquisition and $2,416,000 related to the Davall Acquisition, which were previously mentioned. SL-MTI also benefited from non-comparable sales of $2,743,000 from the Dynetics Acquisition, which was completed on July 25, 2014.

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Income from operations decreased during the nine months ended September 30, 2015 due to a decrease at the High Power Group, which was partially offset by increases at SL-MTI and SLPE. In addition, Unallocated Corporate Expenses increased in 2015 compared to 2014.

During the nine months ended September 30, 2015, the Company s backlog increased to $80,946,000 from $76,448,000 for the same period in the prior year, for a change of 6% on a comparative basis. The increase in backlog in 2015 was attributable to SL-MTI, who recorded a 17% increase, which was primarily due to the Davall Acquisition. The increase in backlog was partially offset by decreases at SLPE and the High Power Group of 7% and 4%, respectively. The Company s net new orders for the nine months ended September 30, 2015 decreased by 4%, compared to the nine months ended September 30, 2014.

The Company s management is taking numerous actions to improve sales through the deployment of growth tools aimed at identifying attractive market segments and penetrating those markets through aggressive new product introduction. The Company is also identifying and penetrating selected geographic opportunities and continues to pursue strategic alternatives, including selective acquisitions. The Company emphasizes lean initiatives at all of its facilities in manufacturing as well as in finance and administration.

While these items are important in understanding and evaluating financial results and trends, other transactions or events, which are disclosed in this Management s Discussion and Analysis, may have a material impact on continuing operations. A complete understanding of these transactions is necessary in order to estimate the likelihood that these trends will continue.

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Critical Accounting Policies

The Company s consolidated financial statements have been prepared in accordance with Generally Accepted Accounting Principles in the United States (GAAP). GAAP requires management to make estimates and assumptions that affect the amounts of reported and contingent assets and liabilities at the date of the consolidated financial statements and the amounts of reported net sales and expenses during the reporting period.

The SEC has issued disclosure guidance for critical accounting policies. The SEC defines critical accounting policies as those that are most important to the portrayal of the Company s financial condition and results, and that require application of management s most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods.

The Company s significant accounting policies are described in Note 1 in the Notes to Consolidated Financial Statements included in Part IV of the Company s Annual Report on Form 10-K for the year ended December 31, 2014. Not all of these significant accounting policies require management to make difficult, subjective or complex judgments or estimates. However, the following policies are deemed to be critical within the SEC definition. The Company s senior management has reviewed these critical accounting policies and estimates and the related Management s Discussion and Analysis of Financial Condition and Results of Operations with the Audit Committee of the Board of Directors.

Revenue Recognition

Revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the purchase price is fixed or determinable and collectability is reasonably assured. Revenue is recorded in accordance with Staff Accounting Bulletin (SAB) No. 104. The major portion of the Company s revenue is derived from equipment sales. The Company recognizes equipment revenue upon shipment or delivery, depending upon the terms of the order, and transfer of title. Generally, the revenue recognition criteria are met at the time the product is shipped. The Company does not currently have any multiple-element arrangements.

Provisions are established for product warranties, principally based on historical experience. At times the Company establishes reserves for specific warranty issues known by management. Customer service and installation revenue is recognized when completed.

SLPE has two sales programs with distributors, pursuant to which credits are issued to distributors: (1) a re-stocking program and (2) a competitive discount program. The distributor re-stocking program allows distributors to rotate up to a pre-determined percentage of their purchases over the previous six month period. SLPE provides for this allowance as a decrease to revenue based upon the amount of sales to each distributor and other historical factors. The competitive discount program allows a distributor to sell a product out of its inventory at a negotiated price in order to meet certain competitive situations. SLPE records this discount as a reduction to revenue based on the distributor s eligible inventory. The eligible distributor inventory is reviewed at least quarterly. No cash is paid under either distributor program. These programs affected consolidated gross revenue for each of the nine month periods ended 2015 and 2014 by approximately 0.5% and 0.3%, respectively.

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Certain judgments affect the application of the Company s revenue policy, as mentioned above. Revenue recognition is significant because net revenue is a key component of results of operations. In addition, revenue recognition determines the timing of certain expenses, such as commissions, royalties and certain incentive programs. Revenue results are difficult to predict. Any shortfall in revenue or delay in recognizing revenue could cause operating results to vary significantly from year to year and quarter to quarter.

Allowance For Doubtful Accounts

The Company s estimate for the allowance for doubtful accounts related to trade receivables is based on two methods. The amounts calculated from each of these methods are combined to determine the total amount reserved. First, the Company evaluates specific accounts where it has information that the customer may have an inability to meet its financial obligations (e.g., bankruptcy or insolvency). In these cases, the Company uses its judgment, based on the best available facts and circumstances, and records a specific reserve for that customer against amounts due to reduce the receivable to the amount that is expected to be collected. These specific reserves are reevaluated and adjusted as additional information is received that impacts the amount reserved. Second, a general reserve is established for all customers based on several factors, including historical write-offs as a percentage of sales. If circumstances change (e.g., higher than expected defaults or an unexpected material adverse change in a major customer s ability to meet its financial obligation), the Company s estimates of the recoverability of amounts due could be reduced by a material amount. Receivables are charged off against the reserve when they are deemed uncollectible. The Company s allowance for doubtful accounts equaled 1.0% and 0.8% of gross trade receivables as of September 30, 2015 and December 31, 2014.

Inventories

The Company values inventory at the lower of cost or market, and continually reviews the book value of discontinued product lines to determine if these items are properly valued. The Company identifies these items and assesses the ability to dispose of them at a price greater than cost. If it is determined that cost is less than market value, then cost is used for inventory valuation. If market value is less than cost, then related inventory is adjusted to market value.

If a write down to the current market value is necessary, the market value cannot be greater than the net realizable value, which is defined as selling price less costs to complete and dispose, and cannot be lower than the net realizable value less a normal profit margin. The Company also continually evaluates the composition of its inventory and identifies obsolete, slow-moving and excess inventories. Inventory items identified as obsolete, slow-moving or excess are evaluated to determine if reserves are required. If the Company were not able to achieve its expectations of the net realizable value of the inventory at current market value, it would have to adjust its reserves accordingly. The Company attempts to accurately estimate future product demand to properly adjust inventory levels. However, significant unanticipated changes in demand could have a significant impact on the value of inventory and of operating results.

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During the third quarter of 2015, the Company elected to change its method of valuing inventory held at two of its manufacturing facility s reporting within our SL-MTI subsidiary from the LIFO method to the FIFO. The Company believes that the FIFO method is preferable as it better reflects the current value of inventory reported in the Company s consolidated balance sheet, provides a better matching of cost of goods sold with revenue, provides consistency across all of our operations, and FIFO is the method used by the Company s management to monitor the financial results of SL-MTI. The cumulative effect of the change was a $160,000 increase to gross margin and a $107,000 increase to net income from continuing operations, which was recorded in the third quarter of 2015. The change was not applied retrospectively to prior periods, as the effect of the change was immaterial to the consolidated financial statements of all prior periods, including interim periods.

Investments

The Company determines the appropriate classification of its investments in equity securities at the time of purchase and reevaluates such determinations at each balance sheet date. Marketable securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and are reported at fair value, with unrealized gains and losses recognized in earnings. Marketable equity securities not classified as trading are classified as available for sale, and are carried at fair market value, with the unrealized gains and losses, net of tax, included in the determination of comprehensive income and reported in shareholders equity. The fair value of all securities held by the Company is determined by quoted market prices.

Derivative Instruments and Hedging Activities

FASB ASC 815, Derivatives and Hedging (ASC 815), provides the disclosure requirements for derivatives and hedging activities with the intent to provide users of financial statements with an enhanced understanding of: (a) how and why an entity uses derivative instruments, (b) how the entity accounts for derivative instruments and related hedged items, and (c) how derivative instruments and related hedged items affect an entity s financial position, financial performance, and cash flows. Further, qualitative disclosures are required that explain the Company s objectives and strategies for using derivatives, as well as quantitative disclosures about the fair value of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative instruments.

The Company is exposed to certain risks arising from both its business operations and economic conditions. The Company principally manages its exposures to a wide variety of business and operational risks through management of its core business activities. Certain of the Company s foreign operations expose the Company to fluctuations of foreign interest rates and exchange rates. These fluctuations may impact the value of the Company s revenues, expenses, cash receipts and payments in terms of the Company s functional currency. The Company enters into derivative financial instruments to protect the value or fix the amount of certain cash flows in terms of the functional currency of the business unit with that exposure.

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As required by ASC 815, the Company records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative, whether the Company has elected to designate a derivative in a hedging relationship and apply hedge accounting and whether the hedging relationship has satisfied the criteria necessary to apply hedge accounting. The Company enters into derivative contracts that are intended to economically hedge certain of its risk, even though hedge accounting does not apply or the Company elects not to apply hedge accounting. Currently, the Company does not apply hedge accounting to any of its foreign currency derivatives.

Accounting For Income Taxes

Significant management judgment is required in determining the provision for income taxes, deferred tax assets and liabilities and any valuation allowance recorded against deferred tax assets. Net deferred tax assets as of September 30, 2015 and December 31, 2014 were $10,323,000 and $11,601,000, respectively, net of valuation allowances of $2,784,000 and $1,720,000 as of September 30, 2015 and December 31, 2014, respectively. The 2015 and 2014 valuation allowances were primarily related to discontinued operations. The carrying value of the Company s net deferred tax assets assumes that the Company will be able to generate sufficient future taxable income in certain tax jurisdictions. Valuation allowances are attributable to uncertainties related to the Company s ability to utilize certain deferred tax assets prior to expiration. These deferred tax assets primarily consist of the state tax expense on certain expenses and loss carryforwards. The valuation allowance is based on estimates of taxable income, expenses and credits by the jurisdictions in which the Company operates and the period over which deferred tax assets will be recoverable. In the event that actual results differ from these estimates or these estimates are adjusted in future periods, the Company may need to establish an additional valuation allowance that could materially impact its consolidated financial position and results of operations. Each quarter, management evaluates the ability to realize the deferred tax assets and assesses the need for additional valuation allowances.

The Company applies the provisions of ASC 740-10-55 to all tax positions for which the statute of limitations remain open. The amount of unrecognized tax benefits, excluding interest and penalties, as of September 30, 2015 and December 31, 2014 was $915,000 and $865,000, respectively. This amount represents unrecognized tax benefits, which, if ultimately recognized, will reduce the Company s effective tax rate. As of September 30, 2015 and December 31, 2014, the Company reported accrued interest and penalties related to unrecognized tax benefits of $113,000 and $81,000, respectively. For additional disclosures related to accounting for income taxes, see Note 11 in the Notes to the Consolidated Financial Statements included in Part IV of the Company s Annual Report on Form 10-K for the year ended December 31, 2014.

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Legal Contingencies

The Company is currently involved in certain legal proceedings. As discussed in Note 15 of the Notes to the Consolidated Financial Statements included in Part I of this Quarterly Report on Form 10-Q, the Company has accrued an estimate of the probable costs for the resolution of these claims. This estimate has been developed based on the current stage of negotiations and data from the Company s environmental engineering consultants and legal counsel. Management does not believe these proceedings will have a further material adverse effect on the Company s consolidated financial position, except as discussed in Note 15. As with litigation, generally the outcome is inherently uncertain. It is possible, however, that future results of operations for any particular quarterly or annual period could be materially affected by changes in these assumptions, or the effectiveness of these strategies, related to these proceedings.

Goodwill

The Company has allocated its adjusted goodwill balance to its reporting units. The Company tests goodwill for impairment annually at fiscal year-end and in interim periods if certain events occur indicating that the carrying value of goodwill may be impaired, such as a significant adverse change in business climate, an adverse action or assessment by a regulator or the decision to sell a business, that would make it more likely than not that an impairment may have occurred. The goodwill impairment test is a two-step process. The first step of the impairment analysis compares the fair value to the net book value. In determining fair value, the accounting guidance allows for the use of several valuation methodologies, although it indicates that quoted market prices are the best evidence of fair value. The Company uses a combination of expected present values of future cash flows and comparative market multiples. It has also performed a review of market capitalization with estimated control premiums at December 31, 2014. If the fair value of a reporting unit is less than its net book value, the Company would perform a second step in its analysis, which compares the implied fair value of goodwill to its carrying amount. If the carrying amount of goodwill exceeds its implied fair value, the Company recognizes an impairment loss equal to that excess amount. Application of the goodwill impairment test requires judgment, including the identification of reporting units, assigning assets and liabilities to reporting units, assigning goodwill to reporting units and determining the fair value of each reporting unit. Significant judgments required to estimate the fair value of reporting units include estimating future cash flows, determining appropriate discount and growth rates, operating margins and working capital requirements, selecting comparable companies within each reporting unit and market and determining control premiums. Changes in these estimates and assumptions could materially affect the determination of fair value for each reporting unit.

The assumptions about future cash flows and growth rates are based on the budget and long-term business plans of each reporting unit. Such assumptions take into account numerous factors including but not limited to historical experience, anticipated economic conditions, new product introductions, product cost and cost structure of each reporting unit. The growth rates assumptions were generally consistent with those utilized in prior year forecasted periods, except in certain circumstances where operational strategies support otherwise.

There were no impairment charges for the nine months ended 2015 and 2014. As of September 30, 2015 and December 31, 2014, goodwill totaled $17,209,000 and $13,072,000, representing 13% and 10% of total assets, respectively.

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There can be no assurance that the economic conditions currently affecting the world economy or other events may not have a negative material impact on the long-term business prospects of any of the Company s reporting units. In such case, the Company may need to record an impairment loss, as stated above. The next annual impairment test will be conducted as of December 31, 2015, unless management identifies a triggering event in the interim.

Management has not identified any triggering events, as defined by ASC 350 Intangibles Goodwill and Other, during 2015. Accordingly, no interim impairment test has been performed.

Impairment Of Long-Lived And Intangible Assets

The Company s long-lived and intangible assets primarily consist of fixed assets, goodwill and other intangible assets. The Company periodically reviews the carrying value of its long-lived assets held and used, other than goodwill and intangible assets with indefinite lives, and assets to be disposed of whenever events or circumstances indicate that the carrying amount of an asset may not be recoverable. The Company assesses the recoverability of the asset by estimated cash flows and at times by independent appraisals. It compares estimated cash flows expected to be generated from the related assets, or the appraised value of the asset, to the carrying amounts to determine whether impairment has occurred. If the estimate of cash flows expected to be generated changes in the future, the Company may be required to record impairment charges that were not previously recorded for these assets. If the carrying value of a long-lived asset is considered impaired, an impairment charge is recorded for the amount by which the carrying value of the long-lived asset exceeds its fair value. Asset impairment evaluations are by nature highly subjective.

Environmental Expenditures

Expenditures that relate to current operations are charged to expense or capitalized, as appropriate. Expenditures that relate to an existing condition caused by formerly owned operations are expensed and recorded as part of discontinued operations, net of tax. Expenditures include costs of remediation, consulting, legal fees to defend against claims for environmental liability and certain costs to assist the Company with compliance matters and administrative tasks. Liabilities are recorded when remedial efforts are probable and the costs can be reasonably estimated. The liability for remediation expenditures includes, as appropriate, elements of costs such as site investigations, consultants fees, feasibility studies, outside contractor expenses and monitoring expenses. Estimates are not discounted and they are not reduced by potential claims for recovery from insurance carriers. The Company does not currently have any outstanding claims against insurance carriers related to remediation expenditures. The liability is periodically reviewed and adjusted to reflect current remediation progress, prospective estimates of required activity and other relevant factors, including changes in technology or regulations. For additional information related to environmental matters, see Note 15 of the Notes to the Consolidated Financial Statements.

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The above listing is not intended to be a comprehensive list of all of the Company s accounting policies. In many cases, the accounting treatment of a particular transaction is specifically dictated by GAAP with no need for management s judgment in its application. There are also areas in which management s judgment in selecting any available alternatives would not produce a materially different result. For a discussion of accounting policies and other disclosures required by GAAP, see the Company s audited Consolidated Financial Statements and Notes thereto included in Part IV of the Company s Annual Report on Form 10-K for the year ended December 31, 2014 and Part 1 to this Quarterly Report.

Liquidity And Capital Resources

	September 30, 2015	December 31, 2014	$ Variance	% Variance
		(in thousands)		
Cash and cash equivalents	$ 5,659	$ 31,950	$ (26,291)	(82%)
Bank debt	$ 13,500		$ 13,500	100%
Working capital	$ 21,989	$ 56,120	$ (34,131)	(61%)
Shareholders equity	$ 74,902	$ 77,321	$ (2,419)	(3%)

The Company s liquidity needs have related to, and are expected to continue to relate to, capital investments, product development costs, acquisitions, working capital requirements, and certain environmental and legal remediation costs. The Company has met its liquidity needs primarily through cash generated from operations and through bank borrowings. The Company believes that cash provided by operating activities from continuing operations and funding available under a credit facility will be adequate to service debt and meet working capital needs, capital investment, and product development requirements for the next twelve months. The Company expects to negotiate a new long-term debt agreement before the expiration of the 2012 Credit Facility on August 9, 2016.

At September 30, 2015, the Company reported $5,659,000 of cash, compared to $31,950,000 of cash and cash equivalents as of December 31, 2014. Cash and cash equivalents decreased in 2015 primarily due to $31,690,000 of cash used in investing activities and $7,619,000 of cash used in operating activities from discontinued operations, which were partially offset by $9,450,000 of cash provided by operating activities from continuing operations and $3,725,000 of cash provided by financing activities.

Net cash provided by operating activities from continuing operations during the nine month period ended September 30, 2015 was $9,450,000 as compared to net cash provided by operating activities from continuing operations of $11,518,000 during the nine month period ended September 30, 2014. The primary source of cash from operating activities from continuing operations for the nine month period ended September 30, 2015 was income from continuing operations of $8,255,000, a decrease in accounts receivable of $3,018,000, a decrease in deferred income tax assets of $1,176,000, and a decrease in inventories of $1,140,000. In addition, depreciation and amortization expense of $2,065,000 and non-cash stock based compensation of $741,000 were added to income from continuing operations. The largest decrease in accounts receivable occurred at SLPE, which was primarily due to strong collections in the third quarter of 2015. The decrease in deferred income tax assets was primarily due to environmental payments in 2015 for environmental claims, remediation, and other services which were accrued for in prior years, which were partially offset by other accrued expenses accrued for in 2015. The largest decrease in inventories occurred at MTE, which is part of the High Power Group, which was primarily due to an increase in inventory at December 31, 2014 due to a large customer order which was fulfilled in the beginning of 2015 coupled with a decrease in purchases in 2015 in an effort to align inventory levels with current demand.

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The sources of cash from operating activities were partially offset by a decrease in accounts payable of $2,464,000, a decrease in accrued income taxes of $2,317,000, and an increase in other assets of $1,445,000. The largest decrease in accounts payable occurred at SL-MTI, which was primarily due to decreased inventory purchases during the third quarter of 2015. The decrease in accrued income taxes during 2015 was primarily due to a tax payment related to the gain from the sale of the company s RFL subsidiary, which was recognized during the fourth quarter of 2014. The increase in other assets was primarily due to an increase in TEAL s value-added tax receivable related to its operations in Mexico.

Net cash provided by operating activities from continuing operations during the nine month period ended September 30, 2014 was $11,518,000. The primary sources of cash from operating activities for the nine month period ended September 30, 2014 were income from continuing operations of $10,548,000, an increase in accrued income taxes of $2,888,000, an increase in accounts payable of $1,308,000, and a decrease in other assets of $1,245,000. In addition, depreciation and amortization expense of $1,608,000 and non-cash stock based compensation of $525,000 were added to income from continuing operations. The increase in accrued income taxes was primarily due to the timing of tax payments related to an increase in income from continuing operations before income taxes coupled with a realized gain from the sale of common stock classified as available-for-sale securities during 2014. All of the Company s operating segments from continuing operations recorded increases in accounts payable. The increase in accounts payable was primarily due to increased sales and related inventory purchases to meet customer demand during 2014. The decrease in other assets was primarily due to the sale of available-for-sale securities and the collection of prepaid value-added tax in China during 2014. These sources of cash from operating activities were partially offset by a $4,194,000 increase in accounts receivable, a gain from the sale of common stock classified as available-for-sale securities of $1,691,000, and a $1,442,000 increase in inventory. The largest increases in accounts receivable occurred at TEAL and MTE, which comprise The High Power Group, and SL-MTI. The increases at TEAL, MTE, and SL-MTI were primarily due to increases in sales during the third quarter of 2014 as compared to the fourth quarter of 2013. The increase at SL-MTI was also due to strong collections during December 2013. All of the Company s operating segments recorded increases in inventory. The increase in inventory was primarily due to increased purchases to meet anticipated customer demand during the remainder of 2014.

Net cash used in operating activities from discontinued operations during the nine month period ended September 30, 2015 was $7,619,000 as compared to net cash used in operating activities from discontinued operations of $3,862,000 during the nine month period ended September 30, 2014. Cash used in operating activities from discontinued operations during 2015 was primarily related to environmental remediation costs for OU-2 as well as a payment of $2,173,000, which included interest, for the EPA s past cost for OU-2 and a portion of the EPA s past cost for OU-1 according to the terms set forth in the Consent Decree (See Note 15 Commitments and Contingencies for the terms and conditions of the Consent Decree). The payments in 2014 were related to a payment of $2,211,000, which included interest, pursuant to the Consent Decree mentioned above and remediation costs, consulting fees, and legal expenses associated with the past operations of the Company s five environmental sites, which were partially offset by an add back of depreciation and amortization expense associated with the formerly owned RFL segment.

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Net cash used in investing activities during the nine month period ended September 30, 2015 was $31,690,000 as compared to net cash provided by investing activities of $2,042,000 during the nine month period ended September 30, 2014. Net cash used in investing activities during 2015 was related to the Davall Gears Acquisition of $20,207,000 and Torque Systems Acquisition of $9,000,000, purchases of property, plant and equipment of $2,243,000, and for the purchase of other assets of $240,000. Purchases of property, plant and equipment were primarily used to upgrade production capabilities and technology. Purchases of other assets were primarily related to the purchase of software. Cash used in investing activities from continuing operations during 2014 was primarily related to the acquisition of certain assets of Dynetic of $3,973,000, purchases of property, plant and equipment of $1,647,000 and for the purchase of other assets of $294,000, which were partially offset by the proceeds from the sale of common stock classified as available-for-sale securities of $4,054,000. Purchases of property, plant and equipment were primarily used to upgrade production capabilities and technology, and for leasehold improvements related to the relocation to a new manufacturing facility in Xianghe, China. Purchases of other assets were primarily related to the purchase of a patent from a third party at MTE and the purchase of software.

On July 27, 2015, the Company acquired all of the issued and outstanding stock of Davall pursuant to a Share Purchase Agreement for a purchase price of £13,035,000, which was approximately $20,207,000 at the exchange rates then in effect, subject to certain adjustments. The transaction was primarily funded through borrowings under the Company s 2012 Credit Facility.

On May 22, 2015, the Company acquired certain assets and assumed certain liabilities Torque Systems pursuant to an Asset Purchase Agreement for an initial purchase price of $9,000,000, plus a working capital adjustment of $169,000. The Torque Systems Acquisition was paid in cash on May 22, 2015 while the working capital adjustment was paid during the fourth quarter of 2015.

Net cash provided by financing activities during the nine month period ended September 30, 2015 was $3,725,000 as compared to net cash used in financing activities of $1,187,000 during the nine month period ended September 30, 2014. Net cash provided by financing activities during 2015 was primarily related to $13,500,000 of net borrowings under the 2012 Credit Facility, which were partially offset by the repurchase and retirement of common stock pursuant to the Company s Tender Offer of $6,796,000, including transaction costs, and $3,511,000 of payments made for the purchase of Company stock pursuant to the Company s 2014 Repurchase Plan (described in Part II, Item 2. Unregistered Sales of Equity Securities and Use of Proceeds). Cash used in financing activities during 2014 was primarily related to $1,000,000 of payments under the 2012 Credit Facility and the purchase of Company stock pursuant to the Company s 2010 share repurchase plan (2010 Repurchase Plan) in the amount of $106,000. The 2010 Repurchase Plan was superseded by the 2014 Repurchase Plan.

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On March 27, 2015, the Company announced the modified Dutch Auction Tender Offer to purchase up to $20 million of its common shares. The Company accepted for purchase approximately 160,000 shares of its common stock at a purchase price of $42.00 per share. These shares represented approximately 3.9% of the total common stock outstanding as of April 24, 2015, prior to the purchase of shares pursuant to the Tender Offer. Upon completion of the Tender Offer, the Company had approximately 3,934,000 shares of common stock outstanding at that time. The aggregate purchase price paid by the Company in connection with the Tender Offer was $6,734,000 excluding transaction costs. On April 27, 2015, the Company paid for the Tender Offer with available cash on hand.

On March 25, 2015, the Company entered into the Fourth Amendment to the 2012 Credit Facility. The Fourth Amendment amends the Credit Agreement in order to, among other things: (a) allow for permitted recapitalization distributions, and (b) provide greater flexibility with certain bank covenants, including with regard to EBITDA (as defined) and fixed charges.

On May 5, 2015, the Company entered into the Fifth Amendment to the 2012 Credit Facility. The Fifth Amendment amends the Credit Agreement in order to, among other things: (a) provide greater flexibility for acquisitions outside of the U.S., and (b) permit one of the Company s subsidiaries to participate in a quick pay discount program with a major customer.

In connection with the Davall Acquisition, on July 24, 2015, the Company entered into the Sixth Amendment to the 2012 Credit Facility. The Sixth Amendment amends the Credit Agreement in order to, among other things: (a) join Davall as a borrower under the 2012 Credit Facility, and (b) establish a $4,000,000 subline for loans funded in USD to be made available to Davall (see Note 12 for additional information).

As of September 30, 2015, the Company had an outstanding balance of $13,500,000 under the 2012 Credit Facility. As of December 31, 2014, the Company had no outstanding balance under the 2012 Credit Facility. At September 30, 2015 and December 31, 2014, the Company had total availability under the 2012 Credit Facility of $26,044,000 and $39,527,000, respectively. The Company s percentage of total debt to total shareholders equity was 18% as of September 30, 2015. The Company s current ratio was 1.41 to 1 at September 30, 2015 and 2.27 to 1 at December 31, 2014.

Capital expenditures from continuing operations were $2,243,000 in 2015, which represented an increase of $596,000 from the capital expenditure levels of 2014. The Company anticipates spending approximately $1,300,000 on property, plant and equipment, used primarily to upgrade production capabilities and upgrade technology during the remainder of 2015. The 2015 capital additions are expected to be funded through cash from operating activities and from borrowings under the 2012 Credit Facility.

With the exception of the segment reported as Unallocated Corporate Expenses (which consists primarily of corporate office expenses, financing activities, certain treasury costs, risk management costs, legal costs, litigation costs, public reporting costs, certain strategic costs, legacy costs and costs not specifically allocated to the reportable business segments), all of the Company s operating segments recorded income from operations during 2015 and 2014.

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Contractual Obligations

The following is a summary of the Company s contractual obligations at September 30, 2015 for the periods indicated:

	Less Than 1 Year	1 to 3 Years	3 to 5 Years	After 5 Years	Total
	(in thousands)				
Operating leases	$ 430	$ 2,305	$ 1,041	$ 502	$ 4,278
Payments to EPA [1]	2,173	2,157			4,330
Letters of credit[2]	456				456
	$ 3,059	$ 4,462	$ 1,041	$ 502	$ 9,064

(1) On May 28, 2013 a letter of credit was issued in favor of the EPA to provide financial assurance related to the Company s environmental payments in accordance with the terms of the Consent Decree reached with the DOJ and EPA related to its liability for both OU-1 and OU-2. In accordance with the Consent Decree, the Company has agreed to pay a fixed sum for the EPA s past cost for OU-2 and a portion of the EPA s past cost for OU-1. The payments are to be made in five equal payments of $2,141,000, for a total $10,705,000, plus interest. On June 1, 2015, the Company made the third payment related to its obligation under the Consent Decree in the amount of $2,173,000, which included interest. The remaining two payments will be made on the anniversary of the prior year s payment plus ten days in the same amount of $2,141,000, plus interest (See Note 15 Commitments and Contingencies for the terms and conditions of the Consent Decree).

(2) As of September 30, 2015, the Company was contingently liable for an outstanding letter of credit issued for casualty insurance requirements. The letter of credit has a maximum maturity of twelve months from the date of issuance.

The previous table excludes the Company s gross liability for uncertain tax positions of $915,000 including accrued interest and penalties, which totaled $113,000 as of September 30, 2015, since the Company cannot predict with reasonable reliability the timing or certainty of cash settlements to the respective taxing authorities.

Off-Balance Sheet Arrangements

It is not the Company s usual business practice to enter into off-balance sheet arrangements such as guarantees on loans and financial commitments, indemnification arrangements and retained interests in assets transferred to an unconsolidated entity for securitization purposes. Consequently, the Company has no off-balance sheet arrangements which have, or are reasonably likely to have, a material current or future effect on its financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources, except for operating lease commitments and letters of credit disclosed in the table above and inventory purchase commitments.

In an attempt to limit the volatility of copper costs, the Company has in the past, and may in the future, enter into purchase agreements for copper. As of September 30, 2015, inventory purchase commitments for copper totaled $739,000. As of September 30, 2015, no purchase commitments for copper were greater than six months.

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Restructuring Costs

Restructuring activity for the period ended September 30, 2015 was as follows: