COMMUNICATIONS SYSTEMS INC
Form 10-K
March 11, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2015

Commission File Number: 001-31588

COMMUNICATIONS SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

Minnesota	**41-0957999_**
(State or other jurisdiction of incorporation or organization)	(Federal Employer

Identification
No.)

10900 Red Circle Drive, Minnetonka, MN 55343

(Address of principal executive offices and zip code)

Registrant's telephone number, including area code: (952) 996-1674

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	**Name of each exchange on which registered**
Common Stock, $.05 par value	**NASDAQ**
Preferred Stock Purchase Rights	

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. YES NO

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES NO

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company.

See definition of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Act.

Large Accelerated Filer   Accelerated Filer   Non-Accelerated Filer   Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES NO

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the Registrant was approximately $72,920,000 based upon the closing sale price of the Company's common stock on the NASDAQ on June 30, 2015.

As of March 1, 2016 there were outstanding 8,761,000 shares of the Registrant's common stock.

Documents Incorporated by Reference:	Portions of the Company's Proxy Statement for its Annual Meeting of Shareholders to be held on May 19, 2016 are incorporated by reference into Part III of this Form 10-K.

PART I

ITEM 1. BUSINESS

(a) GENERAL DEVELOPMENT OF BUSINESS

Communications Systems, Inc. (herein collectively referred to as “CSI,” “our,” “we” or the “Company”) is a Minnesota corporation organized in 1969 that operates directly and through its subsidiaries located in the United States (U.S.), Costa Rica, and the United Kingdom (U.K.). CSI is principally engaged through its Suttle, Inc. subsidiary and business unit in the manufacture and sale of connectivity infrastructure products for broadband and voice communications, and through its Transition Networks, Inc. subsidiary and business unit in the manufacture and sale of core media conversion products for broadband networks. Through its JDL Technologies, Inc. subsidiary and business unit, CSI provides IT solutions including network design, computer infrastructure installations, IT service management, network security, and network operation services.

The Company maintains a website at www.commsystems.com. Our annual reports on Form 10-K, our quarterly reports on Form 10-Q and our periodic reports on Form 8-K (and any amendments to these reports) are available free of charge by linking from our website to the Securities and Exchange Commission website.

(b) FINANCIAL INFORMATION ABOUT INDUSTRY SEGMENTS

The Company classifies its businesses into three segments: *Suttle*, which manufactures connectivity infrastructure products for broadband and voice communications; *Transition Networks,* which designs and markets media conversion products, Ethernet switches, and other connectivity and data transmission products; and *JDL Technologies, (JDL*), which is an IT managed services provider and value-added reseller. Non-allocated general and administrative expenses are separately accounted for as “Other” in the Company’s segment reporting. Intersegment revenues are eliminated upon consolidation. Further information regarding these segments, including customer and industry concentration, is set forth in Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and in Note 12 of the Notes to Consolidated Financial Statements under Item 8.

(c) NARRATIVE DESCRIPTION OF BUSINESS

(1) <u>Information Regarding Business Segments</u>

(i) Suttle, Inc.

Suttle manufactures and markets a broad range of telecommunication products for outside plant and premise distribution under the Suttle brand name in the United States and internationally. The Company's customer-oriented approach provides right-sized solutions that leverage existing infrastructure and protect investments as markets and technologies grow and change. With over 100 years of knowledge and experience, Suttle is a reliable partner, delivering innovative, flexible, easy-to-use solutions, lower cost of ownership, and solid customer support. The Company manufactures 67% of its products at its plants in Hector, Minnesota (Suttle, Inc.) and San Jose, Costa Rica (Suttle Costa Rica, S.A.). The other 33% are purchased from offshore contract manufacturers. Segment sales were $50,082,000 in 2015 and $67,331,000 in 2014.

Products

The Company's products include Structured Cabling Products (enclosure systems to support premise distribution of broadband and other connectivity networks); FTTx Products (fiber optic management and connectivity solutions for access and premise networks); Modular Connecting Products (connecting products for copper telecommunications networks) and DSL Products (products that support broadband connectivity to copper networks).

Outside Plant Products:

Suttle's outside plant products (OSP) are designed to operate in challenging environments yet be easily accessible, extend the life of the existing network, enhance data speeds, and prevent loss.

Suttle OSP systems are designed for flexibility and scalability in real world applications for both copper and fiber networks. Suttle's FutureLink™ OSP Fiber solutions offer a range of products including terminals, patch-and-splice and splitter enclosures. For copper networks, Suttle's FutureLink™ OSP Copper solutions include building entrance terminals and enclosures.

Premise Distribution Products:

Suttle provides service distribution products for cost-effective solutions using existing wiring. These products reduce installation time and labor costs, and increase the provider's return on investment. In addition to reducing a service provider's up-front costs, Suttle's high throughput solutions help eliminate potential bottlenecks to "future-proof" the installation, reducing future costs.

Suttle's new MediaMAX™ premise distribution system provides for reliable brownfield and greenfield premise connectivity to meet the increasing demand for wired and wireless gigabit connectivity throughout the home and small office. Designed to optimize installation cost and practices while maximizing coverage and bandwidth at the point of use for multiple deployment topologies, this brand includes a premise connectivity and distribution system, featuring plastic modular enclosures and tool-less, snap-in modules to minimize wireless interference. MediaMAX™ replaces Suttle's SOHO™ brand products for premise distribution which have been sold for approximately the last 10 years.

Suttle's FutureLink™ product family provides solutions for higher speed, tool-less connectivity and lower cost of ownership, such as copper and fiber connectivity systems, enclosure systems, network interface devices (NIDs), splitters, and active technologies for voice, data and video communications. Active solutions distribute service inside the premise through electronic devices, and Suttle's active service solutions allow the distribution of service at higher speeds regardless of media, using technologies under FutureLink™ brand products.

Passive solutions provide connectivity for traditional telephony and broadband deployments. Through our highly recognized brands — SpeedStar™ and Corroshield® as well as our new FutureLink™ product family brand for higher speeds — Suttle provides the right solution for wired distribution.

Markets and Marketing

Suttle markets its outside plant and premise distribution products globally to telecommunications companies. Suttle has a solid history of offering long-term solutions to some of the largest global providers by understanding the customer's needs and providing innovative solutions coupled with strong customer support. Suttle also markets its products to service providers, residential builders, and low-voltage installers through distributors and the Company's sales staff. Suttle reaches its targeted customers through a variety of marketing media including trade shows, associations, advertising, social media, and the Suttle website.

Suttle recently changed its domain name for electronic communications to SuttleSolutions.com to emphasize our focus on end-to-end customer oriented solutions for communication service providers.

Customers

Suttle's customers include the major communication companies globally, including both telephone and cable service provider companies. The Company's major telephone company customers include Verizon, ATT, and CenturyLink. Suttle serves these major telephone companies directly by Suttle's sales staff and through a select group of distributors. Sales (including DSL) to the major telephone companies, as a group, both directly and through distribution, represented 79% of Suttle's sales in 2015 and 84% in 2014.

Other customers include smaller telephone companies, electrical/low-voltage contractors, home builders, and a nationwide network of distributors. Suttle serves these customers primarily through distributors, but also directly through its sales staff. Sales to cable customers and original equipment manufacturers (OEMs) are made through the nationwide network of distributors and through the Suttle sales staff. Sales to OEMs and other distributors were 6% of Suttle's sales in 2015 and 9% in 2014. Sales to international customers and other customers represented 15% of Suttle's sales in 2015 and 7% in 2014.

Competition

Suttle encounters strong competition in all its product lines and competes primarily on the basis of the broad lines of products offered, product performance, quality, price, delivery, and customer support. In addition, distributors of Suttle's products also market products for one or more of its competitors.

Order Book

Suttle manufactures its products on the basis of estimated customer requirements. Outstanding customer orders at March 1, 2016 were approximately $3,828,000 compared to approximately $2,356,000 at March 1, 2015. New orders are generally filled within 60 days. Suttle does not believe its order book is a significant indicator of longer term future results.

Manufacturing and Sources of Supply

Suttle manufactures its products using plastic or metal parts, wire sub-assemblies, fasteners, brackets, electronic circuit boards, and other components, most of which are fabricated by Suttle. There are multiple sources of supply for the materials and parts required and the Company is not dependent upon any single supplier, except that Suttle's corrosion-resistant products use a moisture-resistant gel-filled fig available only from Tyco Electronics Connectivity. Although Suttle has not generally experienced significant problems in obtaining its required supplies, from time to time it experiences spot shortages and additional order lead times are required from its offshore suppliers.

New Product Development; Patents and Intellectual Property

Suttle continually seeks to understand the needs of its customers and both develops new products for evolving customer requirements and enhances existing products to improve its existing product line. For competitive reasons, including duplication of its designs by foreign apparatus manufacturers, Suttle has adopted a policy to seek patent protection on innovative new products. Suttle applied for five patents in 2015 and expects to file for eight patents in 2016.

Research and development consists primarily of designing, prototyping, and testing of equipment and supplies associated with enhancing existing products and developing new products. Research and development costs are expensed when incurred and were $4,959,000 in 2015 compared to $3,670,000 in 2014.

Suttle and Suttle Solutions are important trademarks for its business. Suttle regularly supports these brand names by trade advertising and believes they are well known in the marketplace. Other important trademarks include FutureLink™ brand umbrella for end-to-end products for outside plant, connectivity and premise distribution; plastic MediaMAX™ and enclosures and modules; SpeedStar™ for passive premise connectivity; and CorroShield® brand gel that prevents network corrosion.

(ii) <u>Transition Networks, Inc.</u>

Transition Networks, Inc. (“Transition” or “Transition Networks”) is based in Minnetonka, Minnesota and also maintains operations in the U.K. Transition designs, assembles and markets media converters, NIDs, network interface cards (NICs), Ethernet switches, Small Form Factor Pluggable modules (SFP), and other connectivity products under the Transition Networks and MILAN brand names. Transition sells its products through distributors, resellers, integrators, and OEMs. These media converters, NIDs, and Ethernet Switch products allow network operators to transmit voice and data across networks and between copper-wired and fiber-optic equipment. Sales by Transition Networks were $42,570,000 in 2015 compared to $43,174,000 in 2014. International sales accounted for 27% of Transition’s sales, or $11,575,000 in 2015, compared to $11,645,000, or 27% of Transition’s sales in 2014.

Products

Transition Networks designs, assembles and sells media converter devices, NIDs, Ethernet switches and other connectivity products that make it possible to transmit telecommunications signals across networks and between systems using different types of media (for example, between copper and fiber optic networks). These products assist in resolving challenges in the areas of bandwidth constraints, security risks, and distance limitations as networks extend from local area to wide area networks and adapt to ever increasing end user demands. As enterprise networks are seemingly always in transition, our solutions enable customers to integrate fiber optics into their existing infrastructure as their networks grow, and extend advanced data services to customers at remote locations, including support of wireless networks and its backhaul requirements. Many of our products incorporate features for performing advanced levels of fault management and other benefits to aid in troubleshooting fiber optic and copper network infrastructure. Our growing Power-over-Ethernet (PoE) products provide support of remote devices such as cameras and wireless access points by passing electrical power along with data on Ethernet cabling, eliminating the need for local power in hard to reach locations.

Transition Networks products support a wide variety of protocols, including: 10 Gigabit Ethernet, Gigabit Ethernet, Fast Ethernet, Ethernet, T1/E1, DS3, Circuit Emulation Services (TDM or ISDN over Ethernet or IP), RS232, RS485, OC3, OC12, and more. Transition Networks develops product hardware and software internally, and expenses the related costs as they are incurred. In connection with the sale of its hardware products, Transition Networks provides its customers with a variety of software management options including powerful Orchestration and Element Management System (EMS) software for providing superior service provisioning and monitoring of next-generation Carrier Ethernet 2.0 Services. The Company has been developing and marketing Ethernet-based networking products for approximately 28 years. Transition Networks continues to develop products that address the enterprise, service provider, industrial, government, and security markets.

Manufacturing and Sources of Supply

Transition Networks uses contract manufacturers to manufacture its products in different geographical locations. In 2015, 62% of the total value of its products was manufactured in Asia while the remaining 38% was manufactured in the US. Offshore sources of supply are subject to certain risks, including political risk. The Company has alternate sources of supply for its products in different geographical locations and to date has not had problems obtaining necessary product.

Markets and Marketing

Transition Networks' products are used in a broad array of markets including the federal government, enterprise, service provider, industrial, and surveillance markets. Transition Networks has a broad customer base and its products are used in a variety of applications.

The media conversion product line is used in several applications. The ION and Point System™ chassis-based modular systems are used primarily in telecommunications closets for high-density applications and when multiple protocols need to be supported. Stand-alone media converters are used typically at a workstation or for lower density applications. The line of Ethernet switches is used in last mile access, backhaul, central closet and at the end user stations. The Carrier Ethernet NID line of products addresses the high quality access requirements for both business services and wireless backhaul data communications and telecommunications applications.

Marketing primarily consists of direct marketing using a sales force, tradeshows, trade magazine advertising, on-line advertising, website, email, social media and public relations activities. Transition Networks also provides and participates in advertising and cooperative marketing campaigns with distribution partners.

The Company's "Transition Networks" and "MILAN" brand names are important to its business. The Company regularly supports these names by trade advertising and believes them to be well known in the marketplace.

Research and Development

Transition Networks develops products for the federal government, enterprise, service provider, security and industrial markets. This includes developing converters for emerging protocols and existing protocols in new markets, as well as new industry standards. Some of these products include remote management devices built on the IEEE® 802.3AH, 802.3AG, ITU-T Y.1731 standards, Metro Ethernet Forum (MEF)® and MEF 2.0 standards, and Power Over Ethernet devices based on the IEEE® 802.3AF and IEEE® 802.3AT standards. Some design efforts are paced by the development of critical components such as integrated circuits and optical transceivers.

Research and development consists primarily of designing, prototyping, and testing of equipment and supplies associated with enhancing existing products and developing new products. Research and development costs are expensed when incurred and were $3,332,000 in 2015 compared to $4,166,000 in 2014.

Transition Networks' conducts its research and development operations in the United States, out of its Minnetonka, MN headquarters location. While this US location has primary engineering and product development responsibility, it will occasionally utilize third party design services and Original Design Manufacturers (ODM) to support specific product design requirements. In addition, Transition Networks' subsidiary TN EMEA, in the UK (renamed Net2Edge in 2016) has been engaged in developing a new line of Circuit Emulation products. In 2016 Net2Edge will be classified as a separate business segment.

Competition

Transition Networks faces strong competition across its entire product line. A large number of competitors exist for high volume products in the Fast Ethernet and Gigabit Ethernet families, as well as the NIDs. Low cost competitors from China and Taiwan are strongest in Asian, European, Middle Eastern, and African (EMEA) and South American markets, with limited success in the North American market for the media converter products. Transition Networks also faces new competitors as it enters new markets for industrial products, security market, and higher performance devices for the service provider market.

Order Book

Outstanding customer orders for Transition Networks products were approximately $4,485,000 at March 1, 2016 and $1,683,000 at March 1, 2015. Transition Networks orders are fulfilled on a relatively short-term basis and therefore the Company does not consider the order book as a significant indicator of longer term future results.

(iii) JDL Technologies, Inc.

JDL Technologies, Inc. ("JDL Technologies" or "JDL"), based in Fort Lauderdale, Florida, is a managed service provider and value-added reseller, supplying information technology (IT) solutions focused on IT service and support management; network design, deployment and integration; cloud, hosted and virtualized services; and network operations center management. JDL's 2015 sales were $15,672,000 compared to 2014 sales of $8,567,000. Project revenue totaled $12,176,000 in 2015 or 78% of JDL sales compared to $6,836,000 in 2014 or 80% of JDL sales. Managed services revenues grew to $3,496,000 in 2015 from $1,731,000 in 2014.

Competitive Strategy

The Florida technology market includes a number of managed service providers (MSPs) and value-added resellers (VARs), and is a microcosm of the burgeoning managed services industry in the U.S. JDL continues to differentiate itself in strategic ways and in early response to market shifts, and is well qualified to help organizations optimize their technologies in order to meet business objectives and regulatory requirements.

JDL partners with organizations to provide complete support for their information technology, from servers to applications down to the network and desktop levels. Under a typical managed services agreement, JDL maintains corporate IT, resolves issues, supports the client's user community, and adds new value to the client's businesses. JDL's key avenues for delivering on this commitment—and its competitive advantages—include JDL's on-premise managed services operations center and secure, state-of-the-art hosted datacenter. The managed services operations center leverages the best available tools, applications, practices and resources to deliver a consistent, quality customer experience. JDL Technologies was named to the 2015 Elite 150 Managed Service Providers in North America, part of The Channel Company's 2015 MSP 500 list. JDL also holds the MSP Trustmark credential from CompTIA and is a member of the MSP Alliance.

JDL's portfolio of technology solutions reflects the regular introduction of new technologies and delivery methodologies and the increasing demand among businesses for innovative solutions to strengthen their competitive edge and continuity. With its team of professionally certified engineers, more than 475 years of technical experience, and talented leadership, JDL Technologies develops best-of-breed IT solutions that effectively meet these demands. To sustain its leading-edge position, JDL maintains robust partnerships with strategic manufacturers and is a McKesson Platinum Partner, Microsoft Gold Partner, HP Enterprise Gold Partner, 3CX VoIP Gold Partner and Citrix Silver Partner. In recognition of its standing, JDL was named to the 2015 Fast Growth 150 Solution Providers by The Channel Company.

In June 2015, JDL Technologies completed its first strategic acquisition to expand into the Southeastern U.S. and strengthen its healthcare portfolio by acquiring Twisted Technologies, a small IT firm in Atlanta focused on practice management and electronic medical records solutions for healthcare organizations. JDL is aggressively leveraging the benefits of this alliance, including an enhanced partnership with McKesson, and continues to explore additional strategic acquisitions. Organically, the company also grew substantially in response to increasing demand for managed services across industries.

These combined factors reflect a stronger, more focused, more mature JDL Technologies. The company continues to win large, multi-state managed services clients, and to earn significant incremental business as well as large new infrastructure and virtualization opportunities. JDL remains focused on growth.

Targeted Vertical Markets

The year 2015 was significant for JDL Technologies for vertical specialization and branding. The company developed three related brands, JDL HealthTech, JDL EduTech, and JDL TechWatch, to identify its healthcare, education and commercial business verticals, and launched corresponding websites to further sharpen its vertical market focus.

Education:

Since JDL Technologies was established in 1995, its largest client has been the School Board of Broward County, Florida (SBBC), the sixth largest public school system in the United States. JDL staffs and manages the SBBC network operations center, which monitors all network elements (servers, switches, routers) and more than 100,000 computers in 265 buildings. In March 2015, JDL was awarded a five-year contract by the SBBC to provide Local Area Network, Wireless Local Area Network and data center upgrades, as well as other IT services, to several hundred public K-12 schools in the district. JDL began providing services under the contract in the second quarter of 2015.

Healthcare:

Under its JDL HealthTech brand, JDL continues to penetrate the $1.3 billion healthcare market in Florida, offering an array of services that address HIPAA Security Rule and Privacy Rule compliance requirements, including McKesson practice management and revenue cycle management services. JDL's strategic segmentation of the healthcare market by organization size and specialization began to bear fruit in 2015, with JDL supporting a robust and growing managed services practice whose clients range from single-office practices to multi-location regional specialists to their regulated suppliers and business associates.

Commercial:

JDL Technologies continues to build a solid roster of diverse commercial clients under its JDL TechWatch brand, delivering dramatic growth in 2015 in recurring revenues from managed services as well as incremental revenues from additional project work. A sampling of these clients includes:

- A 60-year-old Florida financial institution with two dozen branches and more than $4 billion in assets;
- A global fitness program whose 14 million followers take weekly classes in over 100,000 locations;
- The largest private international bank in South America;
- Several of the largest private investment firms in Florida;
- A large family-owned tobacco corporation headquartered in Florida since 1962;
- A well-funded non-profit organization with 19 locations in the continental U.S.

Technology Solutions

As a managed service provider and value-added reseller, JDL Technologies specializes in delivering technology solutions that free organizations to focus on the strategic business activities that are critical to their financial success. JDL's technology solutions encompass an extensive range of networking, virtualization, cloud and infrastructure services, most of which are available under JDL managed services contracts. As technology continues its move to the cloud, JDL aggressively built its portfolio of cloud-based service offerings in 2015, and continues to ensure that its engineers are trained and certified in the newest cloud and other technology solutions.

Managed Services:

JDL Technologies continues to expand in breadth and depth as a managed service provider, more than doubling monthly recurring revenues each year since establishing the program in early 2013. The company serves a diverse base of clients with locations throughout the United States, offering managed service programs designed specifically for the healthcare, commercial and education markets. These robust programs meet HIPAA compliance standards and, while the majority is supported remotely, independent of geographic borders, the company is also able to provide on-site network management and help desk support for key enterprise clients in South Florida. The company's managed services include network management, availability assurance, event alerting and incident management services; server, workstation, mobile device and other asset management services; security services including software patching, firewall, antivirus, antimalware and intrusion detection and prevention services; help desk support for client users; SIP trunking, voice over IP and office management services; migration, conversion and vendor management; and technical consulting services and training.

Cloud Solutions:

JDL Technologies continued to build its portfolio of cloud service offerings in 2015, leading this trend in the Florida and Georgia healthcare markets with services supporting HIPAA compliance. Wireless as a service, infrastructure as a service, and Citrix as a service are among the most popular cloud offerings, with others including backup, storage, voice over IP, firewall and email as cloud or hosted services. The benefits to clients are numerous and include vertical and horizontal scalability, internal bandwidth conservation, and simplification of IT management within client organizations. All JDL cloud offerings are billable as monthly recurring revenue under its managed service model, and JDL is committed to bringing the benefits of cloud services to all clients.

Network Services:

JDL's roots are in network services; these services remain central to the company's role as a managed service provider and value-added reseller. The JDL team has extensive experience and professional certifications in assessing, designing and implementing wired and wireless networks as well as entire technology infrastructures. Networking services also include MPLS, private line and IP communications, network and endpoint security, network tuning and cabling/wiring services. Public school districts and healthcare organizations, in particular, are actively leveraging wireless networks to simplify their communications systems, reduce their technology footprint in confined spaces, and lower maintenance costs. With funding of wireless as a service available through the modernized E-Rate program, wireless networking deployments have become top priority for many public school systems. One example is the School Board of Broward County, which in 2015 awarded JDL a new contract to provide wireless network upgrades throughout the district in addition to other network services.

Virtualization:

Using virtualization across an organization's IT infrastructure delivers greater agility, mobility and efficiency. JDL's virtualization engineers assess, design, deploy, and manage virtualization programs that ensure user access to any workload, anytime, anywhere, on any device. JDL's virtualization services encompass desktops, servers, applications, storage, and any combination thereof, including connectivity and software licensing. As JDL clients continue to adopt virtualization, they experience the economies of scale, reduced capital requirements, enhanced security, and disaster recovery protections that are inherent in virtualized environments.

<u>Order Book and Recent Orders</u>

Outstanding customer orders and contracts for JDL products and services were approximately $6,009,000 at March 1, 2016 and $3,448,000 at March 1, 2015. The Company does not consider current outstanding orders and contracts as a significant indicator of longer term future results.

(2) <u>Employment Levels</u>

As of March 1, 2016 the Company employed 674 people. Of this number, 488 were employed by Suttle (including 117 in Hector, Minnesota, 371 in Costa Rica and 2 in the U.K.), 103 by Transition Networks, Inc., 18 by Net2Edge in the U.K., 54 by JDL Technologies, Inc., and 11 corporate general and administrative positions.

(3) <u>Executive Officers of Registrant</u>

The executive officers of the Company and their ages at March 1, 2016 are set forth below. See Item 9B of this Form 10-K for additional information on the Company's management.

Name	Age	Position[1]
Roger H.D. Lacey	65	Vice-Chairman of the Board and Chief Executive Officer [2014][2]
Edwin C. Freeman	60	Vice President, Treasurer and Chief Financial Officer [2013][3]
Bruce Blackwood	53	President and General Manager,

		Suttle, Inc. [2007][4]
Scott Otis	54	President and General Manager, Transition Networks, Inc. [2013][5]
Scott Fluegge	46	President and General Manager, JDL Technologies, Inc [2011][6]
George Wakileh	50	Chief Technology Office, and Suttle Vice President of Technology Development, [2009] [7]
Kristin A. Hlavka	34	Corporate Controller [2011][8]

1 Dates in brackets indicate year in which officers began serving in such capacity. Executive officers serve at the pleasure of the Board of Directors.

2 Mr. Lacey has been a director of the Company since 2008, was appointed Vice Chair in September 2013, and was appointed Interim Chief Executive Officer in June 2014. On February 27, 2015 he was appointed as the Company's Chief Executive Officer. Mr. Lacey was Senior Vice President of Strategy and Corporate Development for 3M Corporation from 2009 until his retirement in 2013. In addition, from 2000 until his retirement, he was 3M Corporation's Chief Strategy Officer and head of mergers and acquisitions.

3 Mr. Freeman was appointed Chief Financial Officer in September 2013. From March 1992 to September 2013, he held management positions within operations and finance at Bro-Tex Co., Inc., a private company that distributes non-woven materials, most recently serving as the Vice President and Chief Financial Officer. Prior to his appointment as Chief Financial Officer, he served as a director of CSI since 1988.

4 Mr. Blackwood was appointed Vice President and General Manager of Suttle in December 2007, and was named President and General Manager in September 2013. From July 2001 to November 2007 he served as Suttle's Vice President of Sales. Prior to July 2001 he was Vice President of Sales for Americable.

5 Mr. Otis was appointed President and General Manager of Transition Networks in September 2013. From December 2010 to June 2011 he served as Vice President, Operations - Professional Services for TE Connectivity, Inc. Prior to December 2010, he was the Vice President, Marketing and Business Development – ADC Professional Services.

6 Mr. Fluegge was appointed Vice President and General Manager of JDL Technologies in December 2011, and was named President and General Manager in September 2013. Prior to this, he was the Vice President of Workload Automation at GSS AMERICA / GSS INFOTECH / INFOSPECTRUM CONSULTING.

7 Mr. Wakileh has been Suttle's Global Vice President of Technology and Business Development since 2009. In addition, in June 2014 he was designated as the Company's Corporate Scientist, with responsibility for developing strategy for and leading technology development throughout the Company. Mr. Wakileh has over 20 years' experience in telecommunications technology development and strategy.

8 Ms. Hlavka was appointed Corporate Controller in May 2011. From July 2008 to April 2011, she served as the Assistant Corporate Controller. Prior to July 2008, she was an auditor for Deloitte and Touche LLP.

(d) FINANCIAL INFORMATION ABOUT FOREIGN AND DOMESTIC OPERATIONS AND EXPORT SALES

Financial information about domestic and foreign operations and export sales may be obtained by reference to Note 12 of the "Notes to Consolidated Financial Statements" under Item 8 herein.

ITEM 1A. RISK FACTORS

Forward Looking Statements

Certain statements contained in this Annual Report on Form 10-K are "forward-looking" statements within the meaning of and in reliance on the Private Securities Litigation Reform Act of 1995, which provides a "safe harbor" for forward-looking statements. Actual events and results may differ materially from those expressed or forecasted in forward-looking statements due to a number of factors. The principal important risk factors that could cause our actual performance and future events and actions to differ materially from these forward-looking statements include, but are not limited to, the risk factors discussed below.

Risks Related to Our Business

The primary markets we serve are highly competitive, and our ability to compete requires continual focus on delivering high-quality, competitively priced products and services and the regular introduction of new products and services that meet evolving customer requirements.

Competition in the markets for voice and data communications products is intense. Our ability to compete with other manufacturers of these products depends primarily on our engineering, manufacturing and marketing skills; the price, quality and reliability of our products; our delivery and service capabilities; and our control of operating expenses. Our JDL subsidiary also experiences intense competition from other providers of IT products and services. We have experienced, and anticipate continuing to experience, pricing pressures from our customers as well as our competitors. The markets we serve are characterized by rapid technological advances and evolving industry standards. These markets can be significantly affected by new product introductions and marketing activities of industry participants. Some of our competitors and potential competitors have greater financial, technological, manufacturing, marketing, and personnel resources than we. Present and future competitors may be able to identify new markets and develop new products that are superior to those developed by us. They may also adapt new technologies faster, devote greater resources to research and development, promote products more aggressively, and price products more competitively than we. We cannot ensure that competition will not intensify or that we will be able to compete effectively in the markets in which we compete.

We face many challenges in maintaining acceptable margins, and our level of gross margin may not be sustainable.

Gross margins among our products and services vary and are subject to fluctuation from quarter to quarter. The factors that may affect our gross margins adversely are numerous and include:

- Changes in customer, geographic, or product mix;
- Our ability to reduce product costs;
- Increases in material or labor costs;
- Expediting costs incurred to meet customer delivery requirements;
- Excess inventory and inventory carrying charges;
- Obsolescence charges;
- Changes in shipment volume;
- Changes in component pricing;
- Increased price competition;
- Changes in distribution channels;
- Lower margins on competitive-bid contracts;
- Increased warranty cost; and
- Our ability to manage the impact of foreign currency exchange rate fluctuations.

Consolidation among our customers has occurred and further consolidation may occur, resulting in the loss of some customers and reducing revenue during the pendency of business combinations and related integration activities.

We believe future consolidation may occur among our customers as they attempt to increase market share and achieve greater economies of scale. Consolidation has affected our business as our customers focus on completing business combinations and integrating their operations. In some instances, customers integrating large-scale acquisitions have reduced their purchases of our products as they integrate.

The business impact to us of significant customer mergers is likely to be unclear until sometime after these transactions are completed. After a consolidation occurs, a customer may choose to reduce the number of vendors from which it purchases equipment and may choose one of our competitors as its preferred vendor. We cannot ensure that we will continue to supply equipment to the surviving communications service provider after a business combination is completed.

Our financial results could be adversely affected if one or more of our key customers substantially reduces orders for our products.

Traditionally, we have derived a large portion of our revenues from a relatively small number of customers, with our top ten customers accounting for 67%, 72% and 83% of net sales for 2015, 2014 and 2013, respectively. In fiscal 2015, 2014 and 2013, one Suttle customer accounted for approximately 16%, 33% and 24% of consolidated sales, respectively. In fiscal 2015 and 2013, a JDL customer accounted for 11% and 18% of our consolidated sales, respectively. The loss of or a substantial reduction in purchases by any one or more of our top customers could have a material adverse effect on our business, financial position and results of operations.

Our market is subject to rapid technological change and, to compete effectively, we must continually introduce new products that achieve market acceptance.

The communications equipment industry is characterized by rapid technological changes, evolving industry standards, changing market conditions, short product life cycles and rapidly changing customer requirements and frequent new product and service introductions and enhancements. The introduction of products using new technologies or the adoption of new industry standards can make our existing products, or products under development, obsolete or unmarketable. Our future success will depend on our ability to enhance our existing products, to introduce new products to meet changing customer requirements and emerging technologies, and to demonstrate the performance advantages and cost-effectiveness of our products over competing products. Our failure to modify our products to support new alternative technologies or failure to achieve widespread customer acceptance of these modified products could cause us to lose market share and cause our revenues to decline.

We may not predict technological trends or the success of new products in the communications equipment market accurately. New product development often requires forecasting of market trends, development and implementation of new technologies and processes and substantial capital commitments. We do not know whether other new products we develop will gain market acceptance or result in profitable sales.

Some competitors have greater engineering and product development resources than we have. Although we expect to continue to invest significant resources in product development activities, our efforts to achieve and maintain profitability will require us to be selective and focused with our research and development expenditures. If we fail to anticipate or respond in a cost-effective and timely manner to technological developments, changes in industry standards or customer requirements, or if we experience any significant delays in product development or introduction, our business, operating results and financial condition could be affected adversely.

We may experience delays in developing and marketing product enhancements or new products that respond to technological change, evolving industry standards and changing customer requirements. We cannot ensure that we will not experience difficulties that could delay or prevent the successful development, introduction, and marketing of these products or product enhancements, or that our new products and product enhancements will adequately meet the requirements of the marketplace and achieve any significant or sustainable degree of market acceptance in existing or additional markets. In addition, the future introductions or announcements of products by us or one of our competitors embodying new technologies or changes in industry standards or customer requirements could render our then-existing products obsolete or unmarketable. We cannot ensure that the introduction or announcement of new product offerings by us or one or more of our competitors will not cause customers to defer their purchase of our existing products, which could cause our revenues to decline.

Our business units are dependent upon federal government spending.

Our JDL Technologies and Transition Networks business units are involved in projects that receive much of their funding from the United States federal government. To the extent that federal government spending is delayed or curtailed by government actions, our revenues and operating results may be adversely affected.

We evaluate and frequently pursue acquisitions, but we may not successfully close these acquisitions and, if these acquisitions are completed, we may have difficulty integrating the acquired businesses with our existing operations.

We regularly consider the acquisition of complementary companies and product lines. We cannot, however, ensure that we will be able to find appropriate candidates for acquisitions, reach agreement to acquire them, or obtain requisite shareholder or regulatory approvals needed to close strategic acquisitions, despite the effort and management attention invested.

The impact of future acquisitions on our business, operating results and financial condition is uncertain. In the case of businesses we may acquire in the future, we may have difficulty assimilating these businesses and their products, services, technologies and personnel into our operations. These difficulties could disrupt our ongoing business, distract our management and workforce, increase our expenses and materially adversely affect our operating results and financial condition. Also, we may not be able to retain key management and other critical employees after an acquisition. We may also acquire unanticipated liabilities. In addition to these risks, we may not realize all of the anticipated benefits of these acquisitions.

Our operating results fluctuate from quarter to quarter.

Our operating results are difficult to predict and may fluctuate significantly from quarter to quarter. Fluctuations in our quarterly operating results may be caused by many factors, including the following:

- the volume of customer orders and our ability to fulfill those orders in a timely manner;
- the overall level of capital expenditures by our customers;
- work stoppages and other developments affecting the operations of our customers;
- the timing of and our ability to obtain new customer contracts;
- the timing of revenue recognition;
- the timing of new product and service introductions;
- the availability of products and services;
- market acceptance of new and enhanced versions of our products and services;
- variations in the mix of products and services we sell;
- the timing of federal and state government funding of projects;
- the location and utilization of our production capacity and employees; and
- the availability and cost of key components of our products.

Our expense levels are based in part on expectations of future revenues. If revenue levels in a particular quarter are lower than expected, our operating results will be affected adversely.

We depend on manufacturing relationships and on limited-source suppliers and any disruptions in these relationships may cause damage to our customer relationships.

We procure all parts and certain services involved in the production of our products from, and subcontract much of our product manufacturing to outside firms that specialize in these services. Although most of the components of our products are available from multiple vendors, we have several single-source supplier relationships, either because alternative sources are not available or because the relationship is advantageous to us. We cannot ensure that our suppliers will be able to meet our future requirements for products and components in a timely fashion. In addition, the availability of many of these components to us is dependent in part on our ability to provide our suppliers with accurate forecasts of our future requirements. Delays or lost sales could be caused by other factors beyond our control, including defects in the quality of components or products supplied by others.

We are dependent upon our senior management and other critical employees.

Like all communications technology companies, our success is dependent on the efforts and abilities of our senior management personnel and other critical employees, including those in sales, marketing and product development functions. Our ability to attract, retain and motivate these employees is critical to our success. In addition, because we may acquire one or more businesses in the future, our success will depend, in part, upon our ability to retain and integrate our own personnel with personnel from acquired entities that are necessary to the continued success or the successful integration of the acquired businesses.

Managing our inventory is complex and may include write-downs of excess or obsolete inventory.

Managing our inventory of components and finished products is complicated by a number of factors, including the need to maintain a significant inventory of finished goods for orders we anticipate but may not be received. These issues may cause us to purchase and maintain significant amounts of inventory. If this inventory is not used as expected based on anticipated requirements, it may become excess or obsolete. The existence of excess or obsolete inventory can result in sales price reductions or inventory write-downs, which could adversely affect our business and results of operations.

We face risks associated with expanding our sales outside of the United States.

We believe that our future growth depends in part upon our ability to increase sales in international markets. These sales are subject to a variety of risks, including fluctuations in currency exchange rates, tariffs, import restrictions and other trade barriers, unexpected changes in regulatory requirements, longer accounts receivable payment cycles and potentially adverse tax consequences, and export license requirements. In addition, we are subject to the risks inherent in conducting business internationally, including political and economic instability and unexpected changes in diplomatic and trade relationships. We cannot ensure that one or more of these factors will not have a material adverse effect on our business strategy and financial condition.

Compliance with internal control requirements is expensive and poses certain risks.

We expect to incur significant continuing costs, including accounting fees and staffing costs, in order to maintain compliance with the internal control requirements of the Sarbanes-Oxley Act of 2002. Expansion of our business, particularly internationally, will necessitate ongoing changes to our internal control systems, processes and information systems. In addition, if we complete acquisitions in the future, our ability to integrate operations of the acquired company could impact our compliance with Section 404 of the Sarbanes-Oxley Act. We cannot be certain that as our business changes, our current design for internal control over financial reporting will be sufficient to enable management to determine that our internal controls are effective for any period, or on an ongoing basis.

In the future, if we fail to complete the annual Section 404 evaluation in a timely manner, we could be subject to regulatory scrutiny and a loss of public confidence in our internal controls. In addition, any failure to implement required new or improved controls, or difficulties encountered in their implementation, could harm our operating results or cause us to fail to meet our reporting obligations.

Product defects or the failure of our products to meet specifications could cause us to lose customers and revenue or to incur unexpected expenses.

If our products do not meet our customers' performance requirements, our customer relationships may suffer. Also, our products may contain defects or fail to meet product specifications. Any failure or poor performance of our products could result in:

- delayed market acceptance of our products;

- delayed product shipments;
- unexpected expenses and diversion of resources to replace defective products or identify and correct the source of errors;
- damage to our reputation and our customer relationships;
- delayed recognition of sales or reduced sales; and
- product liability claims or other claims for damages that may be caused by any product defects or performance failures.

Our sales and operations may continue to be impacted adversely by current global economic conditions.

Over the past several years, financial markets globally have experienced periods of extreme disruption. These have included, among other things, extreme volatility in securities prices, severely diminished liquidity and credit availability, ratings downgrades of some investments and declining valuations of others. The frequency, severity and duration of these disruptions in the financial markets and the global economy are unknown. We cannot ensure that there will not be a further deterioration in financial markets and in business conditions generally. These economic developments have adversely affected our business in a number of ways and will likely continue to adversely affect our business during the foreseeable future.

Risks Related to Our Common Stock

Our stock price has been volatile historically and the price of our common stock may fluctuate significantly in the future.

The trading price of our common stock has been and may continue to be subject to wide fluctuations. Our stock price may fluctuate in response to a number of events and factors, such as quarterly variations in operating results, announcements of technological innovations or new products by us or our competitors, the operating and stock price performance of other companies that investors may deem comparable to us, and new reports relating to trends in our markets or general economic conditions.

In addition, the stock market in general, and prices for companies in our industry in particular, have experienced extreme volatility that often has been unrelated to the operating performance of these companies. These broad market and industry fluctuations may adversely affect the price of our common stock, regardless of our operating performance.

Anti-takeover provisions in our charter documents, our shareholder rights agreement and Minnesota law could prevent or delay a change in control of our company.

Provisions of our articles of incorporation and bylaws, our shareholder rights agreement (also known as a "poison pill") and Minnesota law may discourage, delay or prevent a merger or acquisition that a shareholder may consider favorable, and could limit the price that investors are willing to pay for our common stock. These provisions include the following:

- advance notice requirements for shareholder proposals;
- authorization for our board of directors to issue preferred stock without shareholder approval;
- authorization for our board of directors to issue preferred stock purchase rights upon a third party's acquisition of 16.5% or more of our outstanding shares of common stock;
- limitations on business combinations with interested shareholders; and
- a super majority vote by shareholders is required to approve certain corporate actions, including merger transactions.

Some of these provisions may discourage a future acquisition of our company even though our shareholders would receive an attractive value for their shares, or a significant number of our shareholders believe such a proposed transaction would be in their best interest.

ITEM 1B. UNRESOLVED STAFF COMMENTS
None.

ITEM 2. PROPERTIES

CSI conducts administrative, manufacturing and engineering functions at the following facilities:

- In Minnetonka, Minnesota, the Company owns a 105,000 square foot building where its executive and administrative offices are located. In addition, Transition Networks uses this facility for its warehouse, assembly, engineering and administrative operations, JDL Technologies, Inc. uses this facility for some administrative operations, and Suttle uses this facility for its sales, marketing and product development.

- Suttle’s manufacturing is conducted at two locations. At Hector, Minnesota, the Company owns three plants totaling 109,000 square feet of manufacturing space. The Company leases 40,000 square feet of manufacturing space in San Jose, Costa Rica.

- Austin Taylor Communications, Ltd. owns a 40,000 square foot facility in Bethesda, Wales, U.K. This was sold in January 2016. See Note 15 of the consolidated financial statements for further information.

- Transition Networks leases 7,000 square feet of office space in the U.K. for its Transition Networks, EMEA operations.

CSI believes these facilities will be adequate to accommodate its administrative, manufacturing and distribution needs for the foreseeable future.

ITEM 3. LEGAL PROCEEDINGS

The Company is subject to claims and lawsuits that have been filed in the ordinary course of business. From time to time, the Company brings suit against others to enforce contract rights or property rights, or to collect debts in the ordinary course of business. Management believes that the resolution or settlement of currently pending litigation will not have a material adverse effect on the results of operations or liquidity of the Company.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASE OF EQUITY SECURITIES

(a) MARKET INFORMATION

The Company's common stock trades on the NASDAQ under the trading symbol JCS.

The table below presents the price range of high and low trades of the Company's common stock for each quarterly period indicated as reported by NASDAQ for 2015 and 2014.

	2015		**2014**	
	High	**Low**	**High**	**Low**
First	$12.40	$10.08	$13.92	$10.78
Second	11.78	10.40	13.50	10.75
Third	10.86	8.13	13.09	10.68
Fourth	9.22	7.25	12.15	10.00

(b) HOLDERS

At March 1, 2016 there were approximately 566 registered holders of record of Communications Systems, Inc. common stock.

(c) DIVIDENDS

Communications Systems, Inc. paid regular quarterly dividends to its shareholders on the dates and at the rates indicated below:

Payment Date	**Dividend per Share**
January 1, 2016	$ .16
October 1, 2015	.16
July 1, 2015	.16
April 1, 2015	.16
January 1, 2015	.16
October 1, 2014	.16
July 1, 2014	.16
April 1, 2014	.16
January 1, 2014	.16

The payment of future dividends will be determined at the discretion of the Board of Directors.

(d) INFORMATION REGARDING EQUITY COMPENSATION PLANS

The following table presents information about the Company's equity compensation plans, under which equity securities of the Company are authorized for issuance, as of December 31, 2015:

Securities Authorized for Issuance Under Equity Compensation Plans

Plan Category (1)	**Number of shares of common stock to be issued upon exercise of outstanding options, warrants and rights**	**Weighted-average exercise price of outstanding options warrants and rights**	**Number of shares of common stock available for future issuance under equity compensation plans (excluding shares in column (a))**
Equity compensation plans approved by security holders:			
1992 Stock Plan-Employee Plan	22,008	$ 14.15	—
1992 Stock Plan-Nonemployee Director Plan	75,000	$ 10.63	—
1990 Employee Stock Purchase Plan	6,450	$ 6.60	101,240
2011 Executive Incentive Compensation Plan	784,159	$ 11.66	1,120,376

Equity compensation plans not approved by security holders:

None

(1) The Company does not have individual compensation arrangements involving the grant of options, warrants and rights.

(e) FIVE YEAR PERFORMANCE GRAPH

The following graph presents, at the end of each of the Company's last five fiscal years, the cumulative total return on the common stock of the Company as compared to the cumulative total return reported for the NASDAQ (U.S.), and the NASDAQ Telecommunications Index. Company information and each index assume the investment of $100 on the last business day before January 1, 2009 and the reinvestment of all dividends.

Comparison of Five-Year Cumulative Total Return

Company or Index	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
Communications Systems, Inc.	$100.000	$104.081	$81.532	$92.631	$92.157	$72.880
NASDAQ US	100.000	100.312	116.793	155.899	175.326	176.169
NASDAQ TELCOM	100.000	105.626	127.317	144.379	148.323	153.652

(f) RECENT SALES OF UNREGISTERED SECURITIES

Not applicable.

(g) PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS

During the three months ended December 31, 2015 the Company repurchased shares of stock as follows:

ISSUER PURCHASES OF EQUITY SECURITIES

Period	**Total Number of Shares (or Units) Purchased (1)**	**Average Price Paid per Share (or Unit)**	**Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs**	**Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs (2)**
October 2015	163	$ 8.74	—	411,910
November 2015	164	8.50	—	411,910
December 2015	—	—	—	411,910
Total	327	$ 8.62	—	411,910

(1) The shares in this column represent shares that were surrendered to us by plan participants to satisfy withholding tax obligations related to share-based compensation.

(2) Shares represent remaining amount of a 500,000 share repurchase authorization approved by the Company’s Board in October 2008 and publicly announced in November 2008.

ITEM 6. SELECTED FINANCIAL DATA

The following selected financial data has been derived from our consolidated financial statements and should be read in conjunction with the Consolidated Financial Statements and related notes thereto set forth in Item 8 and with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in Item 7 of this Annual Report on Form 10-K.

COMMUNICATIONS SYSTEMS, INC. AND SUBSIDIARIES

SELECTED FINANCIAL INFORMATION

(in thousands, except per share amounts)

	Year Ended December 31				
	2015	2014	2013	2012	2011
Selected Income Statement Data					
Sales	$107,670	$119,071	$131,320	$104,250	$143,775
Costs and Expenses:					
Cost of sales	76,123	76,913	86,421	62,753	84,880
Selling, general and administrative expenses	40,830	38,628	36,743	38,101	40,108
Pension settlement costs	1,222	—	—	—	—
Impairment loss	—	—	5,850	—	1,272
Restructuring expense	—	238	1,149	—	—
Total Costs and Expenses	118,175	115,779	130,163	100,854	126,260
Operating (Loss) Income	(10,505)	3,292	1,157	3,396	17,515
Other Income (Expense), Net	104	(112)	(53)	2	105
(Loss) Income Before Income Taxes	(10,401)	3,180	1,104	3,398	17,620
Income Tax (Benefit) Expense	(753)	1,219	2,061	1,160	7,822
Net (Loss) Income	$(9,648)	$1,961	$(957)	$2,238	$9,798
Basic Net (Loss) Income Per Share	$(1.11)	$0.23	$(0.11)	$0.26	$1.16
Diluted Net (Loss) Income Per Share	$(1.11)	$0.23	$(0.11)	$0.26	$1.15
Cash Dividends Declared Per Share	$0.64	$0.64	$0.64	$0.64	$0.60
Average Dilutive Shares Outstanding	8,720	8,640	8,531	8,519	8,496
Selected Balance Sheet Data					
Total Assets	$87,916	$100,286	$103,533	$112,535	$116,659
Property, Plant and Equipment, Net	17,468	18,153	14,941	14,475	14,019
Long-term Liabilities	290	1,271	1,838	3,298	3,741
Stockholders’ Equity	72,185	86,020	88,622	93,995	97,531

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ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

Communications Systems, Inc. provides physical connectivity infrastructure products and services for global deployments of broadband networks through the following business units:

Suttle

Founded in 1910, today Suttle is a leader in innovative network solutions that meet service providers' needs from the central office all the way to the premise through OSP and premise distribution offerings for voice, data and video. Suttle's product portfolio incorporates the best available technology, leveraging existing infrastructure, and laying the foundation for future growth. Products are designed to comply with the most stringent industry standards. Quality management systems are ISO 9001 and TL9000 certified. Suttle's best known brands include SOHO Access™—a premise distribution system with a full line of wiring components —and the new FutureLink™ brand of high-speed and tool-less wired and wireless solutions that lower the service providers' cost of ownership. The newest MediaMAX™ brand premise distribution system provides optimized wired and wireless gigabit connectivity for home and small office structured distribution and will replace SOHO Access™ in 2016.

Transition Networks

With over 25 years of growth and expertise in hardware and software development, Transition Networks offers customers the ability to affordably integrate the benefits of fiber optics into any data network, in any application, and in any environment. Offering support for multiple protocols, any interface, and a multitude of hardware platforms, Transition Networks' portfolio gives customers the power to deliver and manage network traffic reliably over fiber. Based in Minneapolis, Minnesota, Transition Networks distributes hardware-based connectivity solutions exclusively through a network of resellers in over 90 countries.

JDL Technologies

JDL Technologies provides technology services and infrastructure to the education, healthcare, government and commercial market segments. The company's portfolio of technology solutions includes managed services, virtualization, wired and wireless network design and implementation services, and converged infrastructure configuration and deployment. In addition JDL has been providing many of these technology solutions to the School Board of Broward County, Florida, the sixth largest public school district in the U.S., for more than a decade and has managed its Network Operations Center, which monitors all network elements (servers, switches, routers) and more than 100,000 computers in 265 buildings throughout the district.

Key 2015 Developments

- The Company's 2015 sales were $107.7 million, a 10% decrease from 2014 sales of $119.1 million.

- The Company's 2015 net loss was $9.6 million, or ($1.11) per diluted share, compared to net income of $2.0 million or $0.23 per diluted share in fiscal 2014.

- At 2015 year end, the Company had cash, cash equivalents and investments of $21.3 million and positive working capital of $46.4 million compared to $56.9 million at December 31, 2014.

- Suttle sales decreased 26% to $50.1 million in 2015 from $67.3 million in 2014, primarily due to reduced sales to and price reductions imposed by a major customer. Suttle had an operating loss of $6.4 million in 2015 compared to operating income of $6.6 million in 2014.

- Transition Networks sales decreased 1% to $42.6 million in 2015 compared to $43.2 million in 2014. Transition had an operating loss of $4.0 million in 2015 compared to $2.4 million in 2014.

- Sales by JDL Technologies increased 83% to $15.7 million in 2015 compared to $8.6 million in 2014. JDL had operating income of $1.2 million in 2015 compared to an operating loss of $0.9 million in 2014.

- The Company’s R&D investment in 2015 was $8.3 million, or 7.7% of consolidated sales, compared to $7.8 million in 2014.

Forward Looking Statements

In this report and from time to time, in reports filed with the Securities and Exchange Commission, in press releases, and in other communications to shareholders or the investing public, we may make “forward looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. We may make these forward looking statements concerning possible or anticipated future financial performance, business activities, plans, pending claims, investigations or litigation, which are typically preceded by the words “believes,” “expects,” “anticipates,” “intends” or similar expressions. For these forward-looking statements, the Company claims the protection of the safe harbor for forward-looking statements contained in federal securities laws. Shareholders and the investing public should understand that these forward looking statements are subject to risks and uncertainties that could cause actual performance, activities, anticipated results, outcomes or plans to differ significantly from those indicated in the forward-looking statements. For a detailed discussion of a number of such risk factors, please see Item 1A above.

Critical Accounting Policies

Inventory Valuation: We value inventories at the lower of cost or market. Reserves for overstock and obsolescence are estimated and recorded to reduce the carrying value to estimated net realizable value. The amount of the reserve is determined based on historical usage, projected sales information, plans for discontinued products and other factors. Though management considers these reserves adequate and proper, changes in sales volumes due to unexpected economic or competitive conditions are among the factors that could materially affect the adequacy of this reserve.

Income Taxes: In the preparation of the Company’s consolidated financial statements, management calculates income taxes. This includes estimating the Company’s current tax liability as well as assessing temporary differences resulting from different treatment of items for tax and book accounting purposes. These differences result in deferred tax assets and liabilities, which are recorded on the balance sheet. These assets and liabilities are analyzed regularly and management assesses the likelihood it will realize these deferred assets from future taxable income. We determine the valuation allowance for deferred income tax benefits based upon the expectation of whether the benefits are more likely than not to be realized. The Company records interest and penalties related to income taxes as income tax expense in the Consolidated Statements of Income.

Revenue Recognition: The Company recognizes revenue when the earnings process is complete, evidenced by persuasive evidence of an agreement, delivery has occurred or services have been rendered, the price is fixed or determinable, and collectability is reasonably assured. In the Suttle and Transition Networks segments, the earning process completion is evidenced through the shipment of goods, based on the sales terms of these segments, the risk of loss is transferred upon shipment or delivery to customers and there are no significant obligations subsequent to that point. There are not significant estimates related to revenue recognition for these segments.

JDL Technologies records revenue on hardware, software and related equipment sales and installation contracts when the revenue recognition criteria are met and the products are installed and accepted by the customer. JDL records revenue on service contracts on a straight-line basis over the contract period, unless evidence suggests that the revenue is earned in a different pattern. Each contract is individually reviewed to determine when the earnings process is complete.

Results of Operations

2015 Compared to 2014

Consolidated sales were $107,670,000 in 2015, a 10% decrease from sales of $119,071,000 in 2014. Consolidated operating loss was $10,506,000 in 2015 as compared to income of $3,293,000 in 2014. Net loss in 2015 was $9,648,000, or ($1.11) per share compared to net income of $1,962,000 or $0.23 per share in 2014.

Suttle Results

Suttle sales decreased 26% to $50,082,000 in 2015 compared to $67,331,000 in 2014. Sales by product groups in 2015 and 2014 were:

	Suttle Sales by Product Group	
	2015	**2014**
Structured cabling and connecting system products	$42,552,000	$61,004,000
DSL and other products	7,530,000	6,327,000
	$50,082,000	$67,331,000

Suttle's sales by customer groups in 2015 and 2014 were:

	Suttle Sales by Customer Group	
	2015	**2014**
Telecommunication customers	$39,626,000	$56,681,000
Distributors	2,980,000	5,882,000
International	7,278,000	4,530,000
Other	198,000	238,000
	$50,082,000	$67,331,000

The decrease in sales is due primarily to increased pricing pressure and volume declines in Suttle's legacy product lines. Sales to the telecommunication customers decreased 30% to $39,626,000 in 2015 compared to $56,681,000 in 2014 due to a disrupted order cycle at a major customer that significantly curtailed its 2015 purchasing, and overall decline in legacy product lines. Sales to these customers accounted for 79% of Suttle's sales in 2015 compared to 84% of sales in 2014. Sales to distributors decreased 49% and accounted for 6% of sales in 2015 compared to 9% in 2014.

International sales accounted for 15% of Suttle’s 2015 sales and increased 61% compared to 2014 due to the ordering cycle of DSL products and introduction of new products used in FTTx deployments for a major customer.

Sales of structured cabling and connecting system products decreased 30% primarily due to reduced demand from major customers and shifts in technology. Sales of DSL and other products increased 19% due to increased orders from a major international customer.

Suttle’s gross margin decreased 58% to $8,850,000 in 2015 compared to $20,992,000 in 2014. The gross margin percentage decreased to 18% in 2015 as compared to 31% in 2014 due to increased pricing pressure at a major customer and high production variances due to decreased demand, as well as continued investment into production capabilities to support new FTTx product platforms.

Selling, general and administrative expenses increased $896,000, or 6% to $15,285,000, or 30.5% of sales, in 2015 compared to $14,389,000 in 2014, or 21.4% of sales, due to investment into fiber and active capabilities to support new product platforms.

Suttle had an operating loss of $6,435,000 in 2015 compared to income of $6,603,000 in 2014.

Transition Networks

Transition Networks develops, markets, and sells active networking hardware devices. Characteristics of the business include a rapid pace of change in technologies and alternative solutions to our products. Transition Networks derives the majority of its revenues from one-time network upgrade projects. The core markets for these products are enterprise, service providers, government, and industrial users. Roughly 73% of Transition Networks revenue comes from North America, but we continue to see opportunity for long-term growth outside of North America and we will invest resources in sales, marketing, and infrastructure to grow that business.

Transition Networks sales decreased 1% to $42,570,000 in 2015 compared to $43,174,000 in 2014. Transition Networks organizes its sales force by vertical markets and segments its customers geographically. Sales by customer groups in 2015 and 2014 were:

	Transition Networks Sales by Region	
	2015	**2014**
North America	$30,995,000	$31,529,000
EMEA	4,417,000	4,291,000
Rest of world	7,158,000	7,354,000
	$42,570,000	$43,174,000

The following table summarizes Transition Networks' 2015 and 2014 sales by product group:

	Transition Networks Sales by Product Group	
	2015	**2014**
Media converters	$26,914,000	$28,362,000
Ethernet switches	4,972,000	4,727,000
Ethernet adapters	4,169,000	3,939,000
Other products	6,515,000	6,146,000
	$42,570,000	$43,174,000

Sales in North America decreased 2% or $534,000 compared to 2014 due primarily to delays in federal government purchases. International sales decreased $70,000, or 1%, due to slower sales in parts of Latin America and Asia, partially offset by gains in EMEA.

Gross margin decreased 4% to $18,482,000 in 2015 compared to $19,199,000 in 2014. Gross margin as a percentage of sales decreased to 43% in 2015 compared to 44% in 2014 due to unfavorable product mix.

Selling, general and administrative expenses increased 5% to $22,495,000, or 52.8% of sales, in 2015 from $21,393,000 in 2014, or 49.6% of sales due to increased selling and engineering expenses. Operating loss was $4,013,000 in 2015 compared to an operating loss of $2,432,000 in 2014.

Transition Networks continues to develop products based on market needs as well as by following industry standards set by such organizations as the Institute of Electrical and Electronics Engineers (IEEE) and the Metro Ethernet Forum (MEF). It also continues to invest in sales and marketing to grow revenues in our target markets and expand sales outside of North America.

JDL Technologies, Inc.

Sales by JDL Technologies, Inc. increased 83% to $15,672,000 in 2015 compared to $8,567,000 in 2014. The following table summarizes JDL's revenues by customer group in 2015 and 2014:

	JDL Revenue by Customer Group	
	2015	**2014**
Broward County FL schools	$11,691,000	$6,504,000
Miami-Dade County FL schools	0	119,000
Healthcare and commercial customers	3,981,000	1,944,000
	$15,672,000	$8,567,000

Revenues earned in Broward County FL schools increased $5,187,000 or 80% in 2015 as work began on a new multimillion dollar contract to deliver enhanced technology, modern IT infrastructure and expanded wireless coverage to the district.

JDL recognized no revenues from Miami-Dade County Public Schools due to completion of that district's wireless classroom initiative, which had been funded under the E-Rate program.

Revenue from JDL Technologies' sales to small and medium sized commercial businesses (SMBs) increased by 105% or $2,037,000 primarily due to continued robust sales of the company's managed services as well as the revenue generated through the acquisition of Twisted Technologies in June of 2015.

JDL gross margin increased 144% to $4,806,000 in 2015 compared to $1,968,000 in 2014. Gross margin as a percentage of sales increased to 31% in 2015 from 23% in 2014. This reflects, in part, JDL's success in providing more profitable services for the commercial sector and its continuing evolution away from typically narrow margin E-Rate funded projects for smaller or rural school districts.

Selling, general and administrative expenses increased 28% in 2015 to $3,635,000, or 23.2% of sales, compared to $2,846,000 in 2014, or 33.2% of sales, due to strategic investments in staff, systems and product development to support growth and client retention. JDL reported operating income of $1,171,000 in 2015 compared to an operating loss of $878,000 in 2014.

Federal and local funding for public school district investments in IT infrastructure and services varies substantially from year to year, and JDL Technologies expects to continue to experience notable swings in quarterly and annual revenues as a result.

To reduce dependence on government funding and its characteristic volatility, JDL Technologies is focused on opportunities to provide managed services, cloud migration and virtualization services, HIPAA-compliant IT services, and other network and infrastructure services to the commercial and healthcare markets. To this end, JDL leverages several important competitive advantages, including strategic product development, robust gold-level partnerships with technology leaders, extensive staff professional certifications, and maintenance of its status as a HIPAA-compliant healthcare business associate.

Income Taxes

The Company's loss before income taxes was $10,402,000 in 2015 compared to income before income taxes of $3,181,000 in 2014. The Company's effective income tax rate was 7% in 2015 compared to 38% in 2014. The 2015 effective rate differs from the standard rate of 35% due to state income taxes, foreign losses not deductible for U.S. income tax purposes, the effect of operations conducted in lower foreign tax rate jurisdictions, federal research and development credits, and an increase in our valuation allowance as explained in Note 11 to the consolidated financial statements. The 2014 effective rate was higher than the standard rate of 35% due to state income taxes, foreign losses not deductible for U.S. income tax purposes, and the effect of operations conducted in lower foreign tax rate jurisdictions.

2014 Compared to 2013

Sales were $119,071,000 in 2014, a 9% decrease from sales of $131,320,000 in 2013. Operating income increased 185% to $3,293,000 in 2014 as compared to $1,156,000 in 2013. Income before income taxes increased 188% to $3,181,000 from $1,103,000 in 2013. Net income increased 305% to $1,962,000 in 2014 compared to a net loss of $958,000 in 2013.

Suttle Results

Suttle sales increased 24% to $67,331,000 in 2014 compared to $54,346,000 in 2013. Sales by product groups in 2014 and 2013 were:

	Suttle Sales by Product Group	
	2014	2013
Structured cabling and connecting system products	$61,004,000	$45,421,000
DSL and other products	6,327,000	8,925,000
	$67,331,000	$54,346,000

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Suttle's sales by customer groups in 2014 and 2013 were:

	Suttle Sales by Customer Group	
	2014	**2013**
Telecommunication customers	$56,681,000	$43,296,000
Distributors	5,882,000	5,938,000
International	4,530,000	4,547,000
Other	238,000	565,000
	$67,331,000	$54,346,000

The increase in sales is due primarily to increased sales to Suttle's domestic telecommunication customers. Sales to the telephone companies increased 31% to $56,681,000 in 2014 compared to $43,296,000 in 2013 due to growth in high-speed copper connectivity products and success in securing new business in multiple FTTx domains. Sales to these customers accounted for 84% of Suttle's sales in 2014 compared to 80% of sales in 2013. Sales to distributors decreased 1% and accounted for 9% of sales in 2014 compared to 11% in 2013. International sales accounted for 7% of Suttle's 2014 sales and remained stable compared to 2013.

Sales of structured cabling and connecting system products increased 34% due to increased spending by telecommunication customers on new products partially offset by decreased spending due to shifts in technology. Sales of DSL and other products decreased 29% due primarily to the maturation of the market and increased pricing pressures.

Suttle's gross margin increased 33% to $20,992,000 in 2014 compared to $15,812,000 in 2013. The gross margin percentage increased to 31% in 2014 as compared to 29% in 2013 due to introduction of new FTTx products, focused value engineering and cost optimization efforts, and economies of scale.

Selling, general and administrative expenses increased $2,520,000, or 21% to $14,389,000, or 21.4% of sales, in 2014 compared to $11,869,000 in 2013, or 21.8% of sales, due to investment and recruitment of expertise in sales, operations, technology, product management, and engineering as well as increased expenses associated with the implementation of a new ERP system.

Suttle's operating income increased 78% to $6,603,000 in 2014 from $3,716,000 in 2013.

Transition Networks

Transition Networks develops, markets, and sells active networking hardware devices. Characteristics of the business include a rapid pace of change in technologies and alternative solutions to our products. Transition Networks derives the majority of its revenues from one-time network upgrade projects. The core markets for these products are enterprise, service providers, government, and industrial users. Roughly 73% of Transition Networks revenue comes from North America.

Transition Networks sales decreased 2% to $43,174,000 in 2014 compared to $43,857,000 in 2013. Transition Networks organizes its sales force by vertical markets and segments its customers geographically. Sales by customer groups in 2014 and 2013 were:

	Transition Networks Sales by Region	
	2014	**2013**
North America	$31,529,000	$30,661,000
EMEA	4,291,000	5,145,000
Rest of world	7,354,000	8,051,000
	$43,174,000	$43,857,000

The following table summarizes Transition Networks' 2014 and 2013 sales by product group:

	Transition Networks Sales by Product Group	
	2014	**2013**
Media converters	$28,362,000	$28,979,000
Ethernet switches	4,727,000	4,394,000
Ethernet adapters	3,939,000	4,165,000
Other products	6,146,000	6,319,000
	$43,174,000	$43,857,000

Sales in North America increased 3% or $868,000 compared to 2013 due to increased sales into the Federal government channel. International sales decreased $1,551,000, or 12%, due mainly to continued sluggish economic activity in Europe.

Gross margin decreased 14% to $19,199,000 in 2014 compared to $22,419,000 in 2013. Gross margin as a percentage of sales decreased to 44% in 2014 compared to 51% in 2013 due to unfavorable product mix and competitive prices.

Selling, general and administrative expenses decreased 1% to $21,393,000, or 49.6% of sales, in 2014 from $21,581,000 in 2013, or 49.2% of sales. Operating loss decreased 51% to $2,432,000 in 2014 compared to an operating loss of $5,791,000 in 2013 due to the write off of goodwill totaling $5,850,000 in the third quarter of 2013.

Transition Networks continues to develop products based on market needs as well as by following industry standards set by such organizations as the Institute of Electrical and Electronics Engineers (IEEE) and the Metro Ethernet Forum (MEF). It also continues to invest in sales and marketing to grow revenues in our target markets and expand sales outside of North America.

JDL Technologies, Inc.

Sales by JDL Technologies, Inc. decreased 74% to $8,567,000 in 2014 compared to $33,117,000 in 2013. The following table summarizes JDL's revenues by customer group in 2014 and 2013:

	JDL Revenue by Customer Group	
	2014	**2013**
Broward County FL schools	$6,504,000	$7,928,000
Miami Dade County FL schools	119,000	22,988,000
All other	1,944,000	2,201,000
	$8,567,000	$33,117,000

Revenues earned in Broward County FL decreased $1,424,000 or 18% in 2014 due to the Federal government's decision to withhold all priority two E-Rate funding for the current fiscal year, which required the district to find alternate funding sources for planned projects. Revenues earned in Miami Dade County in 2013 and 2014 were derived from a large E-Rate funded infrastructure project. This was completed in the first quarter of 2014. Revenue from JDL Technologies' sales to small and medium sized commercial businesses (SMBs) decreased by 12% or $257,000 as there were fewer large infrastructure transactions completed during the year due to a combination of market trends and JDL's ongoing emphasis on higher margin managed services growth.

JDL gross margin decreased 70% to $1,968,000 in 2014 compared to $6,669,000 in 2013. Gross margin as a percentage of sales increased to 23% in 2014 from 20% in 2013 reflecting the fact that a significant portion of its 2013 revenue was hardware-based, rather than its more traditional value-added service.

Selling, general and administrative expenses decreased 14% in 2014 to $2,846,000, or 33.2% of sales, compared to $3,292,000 in 2013, or 9.9% of sales, due to a decrease in internal costs associated with the higher revenue achieved in the previous year's E-Rate driven business. Selling, general and administrative expenses as a percentage of sales were much higher in the 2014 period as JDL's non-variable general and administrative expenses constituted a much higher percentage of the lower 2014 sales. JDL reported an operating loss of $878,000 in 2014 compared to operating income of $3,232,000 in 2013.

Federal and local funding for public school district investments in IT infrastructure and services varies substantially from year to year, and JDL Technologies expects to continue to experience notable swings in quarterly and annual revenues as a result.

To reduce dependence on government funding and its characteristic volatility, JDL Technologies is focused on opportunities to provide managed services, cloud migration and virtualization services, HIPAA-compliant IT services, and other network and infrastructure services to the commercial and healthcare markets. To this end, JDL leverages several important competitive advantages, including strategic product development, robust gold-level partnerships with technology leaders, extensive staff professional certifications, and maintenance of its status as a HIPAA-compliant healthcare business associate.

Income Taxes

Income before income taxes increased 188% to $3,181,000 in 2014 compared to $1,103,000 in 2013. The Company's effective income tax rate was 38% in 2014 compared to 187% in 2013. The 2014 effective rate was higher than the standard rate of 35% due to state income taxes, foreign losses not deductible for U.S. income tax purposes, and the effect of operations conducted in lower foreign tax rate jurisdictions. The 2013 effective rate was higher than the standard rate of 35% due to state income taxes, foreign losses not deductible for U.S. income tax purposes, provisions for interest charges for uncertain income tax positions, the effect of operations conducted in lower foreign tax rate jurisdictions, and the goodwill impairment not deductible for income tax purposes.

Acquisitions and Dispositions

The Company is a growth-oriented manufacturer of telecommunications connecting and networking devices. The Company continually searches for acquisition candidates with products that will enable the Company to better serve its target markets.

Effects of Inflation

Inflation has not had a significant effect on operations in recent years. The Company does not have long-term production or procurement contracts and has historically been able to adjust pricing and purchasing decisions to respond to inflationary pressures.

Liquidity and Capital Resources

As of December 31, 2015, the Company had approximately $21,335,000 in cash, cash equivalents and investments. Of this amount, $1,944,000 was invested in short-term money market funds that are not considered to be bank deposits and are not insured or guaranteed by the FDIC or other government agency. These money market funds seek to preserve the value of the investment at $1.00 per share; however, it is possible to lose money investing in these funds. The remainder in cash and cash equivalents is operating cash and certificates of deposit, which are fully insured through the FDIC. The Company also had $11,522,000 in investments consisting of certificates of deposit and corporate notes and bonds that are traded on the open market and are classified as available-for-sale at December 31, 2015.

The Company had working capital of $46,449,000, consisting of current assets of approximately $61,890,000 and current liabilities of $15,441,000 at December 31, 2015 compared to working capital of $56,911,000, consisting of current assets of $69,906,000 and current liabilities of $12,995,000 at the end of 2014. The Company's working capital at December 31, 2015 decreased from the prior year-end as the Company made a concerted effort to decrease inventory.

Cash flow provided by operating activities was approximately $840,000 in 2015 compared to $12,172,000 provided by operations in 2014. Significant working capital changes from 2014 to 2015 included a decrease in inventories due to a concerted effort to increase productivity and reduce excess inventory offset by an increase in receivables of $4.0 million due to a slight increase in revenues in the fourth quarter of 2015 as compared to 2014 and an increase in days sales outstanding at Suttle for a couple of significant customers.

Cash provided by investing activities was $1,395,000 of cash in 2015 compared to cash used of $12,048,000 in 2014. The Company continued to make capital investments in 2015, primarily to Suttle's manufacturing operations. The Company also acquired Twisted Technologies, Inc. during the second quarter of 2015 and paid $1,000,000 in initial consideration, with an estimated $442,000 to be paid out in deferred and contingent consideration.

Net cash used by financing activities was $6,006,000 in 2015 compared to $6,301,000 in 2014. Cash dividends paid on common stock increased to $5,622,000 in 2015 ($0.64 per common share) from $5,572,000 in 2014 ($0.64 per common share). Proceeds from common stock issuances, principally shares sold to the Company's Employee Stock Ownership Plan and under the Company's Employee Stock Purchase Plan, totaled approximately $146,000 in 2015 and $246,000 in 2014 net of acquisitions of Company stock from employees in order to satisfy withholding tax obligations related to share-based compensation, pursuant to terms of Board and shareholder-approved compensation plans. The Company did not repurchase any shares in 2015 or 2014 under the Board authorized program. At December 31, 2015, Board of Director authority to purchase approximately 411,910 additional shares remained in effect.

As part of the acquisition of the new Minnetonka headquarters building in July 2007, the Company assumed an outstanding mortgage of $4,380,000. The mortgage is payable in monthly installments and carries an interest rate of 6.83%. The mortgage was fully paid in March of 2016. Mortgage payments on principal totaled $524,000 during 2015. The outstanding balance on the mortgage was $104,000 at December 31, 2015.

The Company had no outstanding obligations under its line of credit at December 31, 2015 and 2014, and the Company's entire credit line ($10,000,000 at March 1, 2015) is available for use. Interest on borrowings on the credit line is at LIBOR plus 1.5% (1.9% at December 31, 2015). The credit agreement expires October 31, 2016 and is secured by assets of the Company. In the opinion of management, based on the Company's current financial and operating position and projected future expenditures, sufficient funds are available to meet the Company's anticipated operating and capital expenditure needs.