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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549**

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**FORM 10-Q**

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

**For the quarterly period ended December 31, 2013**

Or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-1000

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**Sparton Corporation**

(Exact name of registrant as specified in its charter)

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Ohio  
(State or other jurisdiction of  
incorporation or organization)

425 N. Martingale Road, Suite 2050,  
Schaumburg, Illinois  
(Address of principal executive offices)

38-1054690  
(I.R.S. Employer  
Identification No.)

60173-2213  
(Zip code)

(847) 762-5800  
(Registrant's telephone number, including zip code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

(Do not check if a smaller reporting company)

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

As of January 31, 2014, there were 10,124,422 shares of common stock, \$1.25 par value per share, outstanding.

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**TABLE OF CONTENTS**

PART I	<a href="#"><u>FINANCIAL INFORMATION</u></a>	<a href="#"><u>3</u></a>
ITEM 1.	<a href="#"><u>FINANCIAL STATEMENTS</u></a>	<a href="#"><u>3</u></a>
	<a href="#"><u>CONDENSED CONSOLIDATED BALANCE SHEETS AS OF DECEMBER 31, 2013 AND JUNE 30, 2013 (UNAUDITED)</u></a>	<a href="#"><u>3</u></a>
	<a href="#"><u>CONDENSED CONSOLIDATED STATEMENTS OF INCOME FOR THE THREE AND SIX MONTHS ENDED DECEMBER 31, 2013 AND 2012 (UNAUDITED)</u></a>	<a href="#"><u>4</u></a>
	<a href="#"><u>CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME FOR THE THREE AND SIX MONTHS ENDED DECEMBER 31, 2013 AND 2012 (UNAUDITED)</u></a>	<a href="#"><u>5</u></a>
	<a href="#"><u>CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE SIX MONTHS ENDED DECEMBER 31, 2013 AND 2012 (UNAUDITED)</u></a>	<a href="#"><u>6</u></a>
	<a href="#"><u>CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY FOR THE SIX MONTHS ENDED DECEMBER 31, 2013 AND 2012 (UNAUDITED)</u></a>	<a href="#"><u>7</u></a>
	<a href="#"><u>NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS</u></a>	<a href="#"><u>8</u></a>
ITEM 2.	<a href="#"><u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u></a>	<a href="#"><u>25</u></a>
ITEM 3.	<a href="#"><u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u></a>	<a href="#"><u>39</u></a>
ITEM 4.	<a href="#"><u>CONTROLS AND PROCEDURES</u></a>	<a href="#"><u>39</u></a>
PART II	<a href="#"><u>OTHER INFORMATION</u></a>	<a href="#"><u>39</u></a>
ITEM 1.	<a href="#"><u>LEGAL PROCEEDINGS</u></a>	<a href="#"><u>39</u></a>
ITEM 1A.	<a href="#"><u>RISK FACTORS</u></a>	<a href="#"><u>40</u></a>
ITEM 1A.	<a href="#"><u>OTHER INFORMATION</u></a>	<a href="#"><u>41</u></a>
ITEM 6.	<a href="#"><u>EXHIBITS</u></a>	<a href="#"><u>41</u></a>
	<a href="#"><u>SIGNATURES</u></a>	<a href="#"><u>42</u></a>
	CERTIFICATIONS	

**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements.**

**SPARTON CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(UNAUDITED)**

(Dollars in thousands, except per share amounts)

	December 31, 2013	June 30, 2013 (a)
<b>Assets</b>		
<b>Current Assets:</b>		
Cash and cash equivalents	\$ 1,009	\$ 6,085
Accounts receivable, net of allowance for doubtful accounts of \$107 and \$61, respectively	44,806	49,572
Inventories and cost of contracts in progress, net	52,393	46,334
Deferred income taxes	3,054	2,951
Prepaid expenses and other current assets	3,844	1,731
<b>Total current assets</b>	<b>105,106</b>	<b>106,673</b>
Property, plant and equipment, net	28,627	28,904
Goodwill	30,156	14,767
Other intangible assets, net	11,756	10,713
Deferred income taxes — non-current	3,931	4,075
Other non-current assets	2,980	790
<b>Total assets</b>	<b>\$ 182,556</b>	<b>\$ 165,922</b>
<b>Liabilities and Shareholders' Equity</b>		
<b>Current Liabilities:</b>		
Current portion of long-term debt	\$ 141	\$ 136
Accounts payable	16,885	19,596
Accrued salaries and wages	6,648	6,329
Accrued health benefits	1,586	1,793
Performance based payments on customer contracts	19,111	20,902
Other accrued expenses	7,180	6,733
<b>Total current liabilities</b>	<b>51,551</b>	<b>55,489</b>
Pension liability — non-current portion	275	274
Long-term debt — non-current portion	26,331	11,403
Environmental remediation — non-current portion	2,541	2,684
<b>Total liabilities</b>	<b>80,698</b>	<b>69,850</b>
Commitments and contingencies		
<b>Shareholders' Equity:</b>		
Preferred stock, no par value; 200,000 shares authorized, none issued	—	—
Common stock, \$1.25 par value; 15,000,000 shares authorized, 10,124,422 and 10,095,716 shares issued and outstanding, respectively	12,656	12,619
Capital in excess of par value	18,689	18,751
Retained earnings	71,727	65,957
Accumulated other comprehensive loss	(1,214)	(1,255)
<b>Total shareholders' equity</b>	<b>101,858</b>	<b>96,072</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$ 182,556</b>	<b>\$ 165,922</b>

(a) Derived from the Company's audited financial statements as of June 30, 2013.

See Notes to unaudited condensed consolidated financial statements.

**SPARTON CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME**  
**(UNAUDITED)**

(Dollars in thousands, except per share amounts)

	For the Three Months Ended		For the Six Months Ended	
	December 31, 2013	December 31, 2012	December 31, 2013	December 31, 2012
<b>Net sales</b>	\$ 84,562	\$ 67,254	\$ 158,760	\$ 118,055
Cost of goods sold	69,585	55,159	131,589	97,960
<b>Gross profit</b>	14,977	12,095	27,171	20,095
<b>Operating Expense:</b>				
Selling and administrative expenses	8,687	7,375	16,332	12,847
Internal research and development expenses	402	243	791	548
Amortization of intangible assets	636	273	1,234	375
Restructuring charges	—	—	188	—
Other operating expenses	(5)	4	(8)	(6)
Total operating expense, net	9,720	7,895	18,537	13,764
<b>Operating income</b>	5,257	4,200	8,634	6,331
<b>Other income (expense):</b>				
Interest expense	(202)	(173)	(360)	(254)
Interest income	—	23	2	51
Other, net	165	59	337	169
Total other expense, net	(37)	(91)	(21)	(34)
<b>Income before provision for income taxes</b>	5,220	4,109	8,613	6,297
Provision for (benefit from) income taxes	1,736	(732)	2,843	(1)
<b>Net income</b>	\$ 3,484	\$ 4,841	\$ 5,770	\$ 6,298
<b>Income per share of common stock:</b>				
Basic	\$ 0.34	\$ 0.47	\$ 0.57	\$ 0.62
Diluted	\$ 0.34	\$ 0.47	\$ 0.57	\$ 0.62
<b>Weighted average shares of common stock outstanding:</b>				
Basic	10,115,255	10,229,320	10,093,973	10,185,464
Diluted	10,147,518	10,248,424	10,123,542	10,206,913

See Notes to unaudited condensed consolidated financial statements.

**SPARTON CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
**(UNAUDITED)**  
(Dollars in thousands)

	For the Three Months Ended		For the Six Months Ended	
	December 31, 2013	December 31, 2012	December 31, 2013	December 31, 2012
<b>Net income</b>	\$ 3,484	\$ 4,841	\$ 5,770	\$ 6,298
Other comprehensive income (loss) - Change in unrecognized pension costs, net of tax:				
Amortization of unrecognized net actuarial loss, net of tax benefit of \$7 and \$30 for the three months ended December 31, 2013 and 2012, respectively, and net of tax benefit of \$23 and \$34 for the six months ended December 31, 2013 and 2012, respectively	11	51	41	58
Pro rata recognition of lump-sum settlements, net of tax expense of \$10 for the three months ended December 31, 2012	—	(15)	—	—
<b>Other comprehensive income, net of tax</b>	<b>11</b>	<b>36</b>	<b>41</b>	<b>58</b>
<b>Comprehensive income</b>	<b>\$ 3,495</b>	<b>\$ 4,877</b>	<b>\$ 5,811</b>	<b>\$ 6,356</b>

**SPARTON CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED)**  
(Dollars in thousands)

	For the Six Months Ended	
	December 31, 2013	December 31, 2012
<b>Cash Flows from Operating Activities:</b>		
Net income	\$ 5,770	\$ 6,298
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	3,640	1,472
Deferred income tax expense	239	760
Stock-based compensation expense	917	597
Gross profit effect of capitalized profit in inventory from acquisition	108	566
Excess tax benefit of stock-based compensation	(496)	—
Other	44	47
Changes in operating assets and liabilities:		
Accounts receivable	8,097	(4,306)
Inventories and cost of contracts in progress	2,441	(1,845)
Prepaid expenses and other assets	(1,702)	(2,798)
Performance based payments on customer contracts	(1,791)	(6,592)
Accounts payable and accrued expenses	(4,791)	(3,128)
Net cash provided by (used in) operating activities	12,476	(8,929)
<b>Cash Flows from Investing Activities:</b>		
Purchase of Onyx	—	(43,250)
Purchase of certain assets of Creonix	105	—
Purchase of certain assets and liabilities of Aydin Displays, Inc.	(15,000)	—
Purchase of Beckwood	(15,300)	—
Purchases of property, plant and equipment	(1,412)	(1,602)
Change in restricted cash	—	(535)
Proceeds from sale of property, plant and equipment	68	—
Net cash used in investing activities	(31,539)	(45,387)
<b>Cash Flows from Financing Activities:</b>		
Short-term bank borrowings, net	—	14,000
Borrowings of long-term debt	41,000	—
Repayment of long-term debt	(26,071)	(70)
Payment of debt financing costs	—	(408)
Repurchase of stock	(1,559)	(234)
Proceeds from the exercise of stock options	121	144
Excess tax benefit from stock-based compensation	496	—
Net cash provided by financing activities	13,987	13,432
Net decrease in cash and cash equivalents	(5,076)	(40,884)
<b>Cash and cash equivalents at beginning of period</b>	<b>6,085</b>	<b>46,950</b>
<b>Cash and cash equivalents at end of period</b>	<b>\$ 1,009</b>	<b>\$ 6,066</b>
<b>Supplemental disclosure of cash flow information:</b>		
Cash paid for interest	\$ 320	\$ 258
Cash paid for income taxes	\$ 2,963	\$ 1,603
<b>Supplemental disclosure of non-cash investing activities:</b>		
Accounts payable recognized in relation to acquisition purchase consideration adjustments	\$ 393	\$ 2,188

See Notes to unaudited condensed consolidated financial statements.

**SPARTON CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**  
**(UNAUDITED)**  
(Dollars in thousands)

	Six Months Ended December 31, 2013					
	Common Stock		Capital	Retained	Accumulated	Total
	Shares	Amount	In Excess of Par		Earnings	
			Value	Comprehensive Loss		
Balance at June 30, 2013	10,095,716	\$ 12,619	\$ 18,751	\$ 65,957	\$ (1,255)	\$ 96,072
Issuance of stock	94,811	119	(119)	—	—	—
Forfeiture of restricted stock	(3,344)	(4)	4	—	—	—
Repurchase of stock	(76,880)	(96)	(1,463)	—	—	(1,559)
Exercise of stock options	14,119	18	103	—	—	121
Stock-based compensation	—	—	917	—	—	917
Excess tax benefit from stock-based compensation	—	—	496	—	—	496
Comprehensive income, net of tax				5,770	41	5,811
Balance at December 31, 2013	10,124,422	12,656	18,689	71,727	(1,214)	101,858

	Six Months Ended December 31, 2012					
	Common Stock		Capital	Retained	Accumulated	Total
	Shares	Amount	In Excess of Par		Earnings	
			Value	Comprehensive Loss		
Balance at June 30, 2012	10,105,759	\$ 12,632	\$ 19,579	\$ 51,995	\$ (1,718)	\$ 82,488
Cumulative impact of change in accounting principle	—	—	—	492	—	492
Balance at June 30, 2012 - as adjusted	10,105,759	12,632	19,579	52,487	(1,718)	82,980
Issuance of stock	159,433	199	(199)	—	—	—
Forfeiture of restricted stock	(39,811)	(50)	50	—	—	—
Repurchase of stock	(20,564)	(25)	(209)	—	—	(234)
Exercise of stock options	24,304	30	114	—	—	144
Stock-based compensation	—	—	597	—	—	597
Comprehensive income, net of tax	—	—	—	6,298	58	6,356
Balance at December 31, 2012	10,229,121	12,786	19,932	58,785	(1,660)	89,843

See Notes to unaudited condensed consolidated financial statements.



**SPARTON CORPORATION AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(1) Business and Basis of Presentation**

Sparton Corporation and subsidiaries (the “Company” or “Sparton”) has been in continuous existence since 1900. It was last reorganized in 1919 as an Ohio corporation. The Company is a provider of complex and sophisticated electromechanical devices with capabilities that include concept development, design and manufacturing engineering, production, distribution, and field service. The Company serves the Medical & Biotechnology, Military & Aerospace and Industrial & Commercial markets through three reportable business segments; Medical Device (“Medical”), Complex Systems (“CS”) and Defense & Security Systems (“DSS”). Financial information by segment is presented in Note 16. All of the Company's facilities are registered to ISO standards, including 9001 or 13485, with most having additional certifications. The Company's products and services include products for Original Equipment Manufacturers (“OEM”) and Emerging Technology (“ET”) customers that are microprocessor-based systems that include transducers, printed circuit boards and assemblies, sensors, and electromechanical components, as well as development and design engineering services relating to these product sales. Sparton also develops and manufactures sonobuoys, anti-submarine warfare (“ASW”) devices used by the United States Navy and other free-world countries. Many of the physical and technical attributes in the production of sonobuoys are similar to those required in the production of the Company's other electrical and electromechanical products and assemblies.

The unaudited condensed financial statements and related footnotes have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. The financial information presented herein should be read in conjunction with the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2013, which includes information and disclosures not presented herein. All significant intercompany accounts and transactions have been eliminated in consolidation. Certain reclassifications of prior period amounts have been made to conform to the current year presentation. Subsequent events have been evaluated through the date these financial statements were issued. In the opinion of management, the unaudited condensed consolidated financial statements contain all of the adjustments, consisting of normal recurring adjustments, necessary to present fairly, in summarized form, the consolidated financial position, results of operations and cash flows of the Company. The results of operations for the three and six months ended December 31, 2013 are not necessarily indicative of the results that may be expected for the full fiscal year 2014.

**(2) Change in Accounting Principle**

In the first quarter of fiscal 2014, the Company voluntarily changed its revenue recognition policy related to DSS sonobuoy sales to the U.S. Navy and foreign government customers under long-term contracts that require lot acceptance testing. The new policy continues to recognize revenue under the percentage of completion method, but changes the measurement of progress under these contracts from a completed units accepted basis (whereby revenue was recognized for each lot of sonobuoys produced when that lot was formally accepted by the customer) to a units-of-production basis (whereby revenue is recognized when production and internal testing of each lot of sonobuoys is completed). The Company now has significant experience in producing sonobuoys to customer specifications and internal testing to assess compliance with those specifications and, as such, now has an adequate history of continuous customer acceptance of all sonobuoys produced. Accordingly, the Company believes the new method is preferable primarily because it eliminates delays in revenue and related cost of goods sold recognition due to timing of customer testing and acceptance delays. Such delays commonly occur due to customer circumstances that are unrelated to the product produced. Under the new policy, the revenue and related costs of goods sold of these manufactured sonobuoy lots will more closely match the period in which the product was produced and the related revenue earned, thereby better reflecting the economic activity of the DSS segment. Additionally, this new method provides better matching of periodic operating expenses incurred during production.

For the three months ended December 31, 2013, this change in accounting policy decreased DSS and consolidated net sales and gross profit by \$2.5 million and \$0.7 million, respectively, and basic and diluted income per share each by \$0.04. For the six months ended December 31, 2013, this change in accounting policy (decreased) increased DSS and consolidated net sales and gross margin by \$(0.3) million and \$0.4 million, respectively, and increased basic and diluted income per share each by \$0.03. The following tables present the effects of the retrospective application of this voluntary change in accounting principle (Dollars in thousands, except share amounts):

**Consolidated Statement of Income Data:**

	For the Three Months Ended December 31, 2012		
	As Originally		
	Reported	Adjustment	As Restated
Net Sales	\$ 65,979	\$ 1,275	\$ 67,254
Cost of goods sold	54,571	588	55,159
Gross profit	11,408	687	12,095
Income before provision for income taxes	3,422	687	4,109
Provision for (benefit from) income taxes	(979)	247	(732)
Net income	4,401	440	4,841
Income per share of common stock - Basic	0.43	0.04	0.47
Income per share of common stock - Diluted	0.43	0.04	0.47
Weighted average shares outstanding - Basic	10,229,320		10,229,320
Weighted average shares outstanding - Diluted	10,248,424		10,248,424

**Consolidated Statement of Income Data:**

	For the Six Months Ended December 31, 2012		
	As Originally		
	Reported	Adjustment	As Restated
Net Sales	\$ 114,999	\$ 3,056	\$ 118,055
Cost of goods sold	96,378	1,582	97,960
Gross profit	18,621	1,474	20,095
Income before provision for income taxes	4,823	1,474	6,297
Provision for (benefit from) income taxes	(531)	530	(1)
Net income	5,354	944	6,298
Income per share of common stock - Basic	0.53	0.09	0.62
Income per share of common stock - Diluted	0.52	0.10	0.62
Weighted average shares outstanding - Basic	10,185,464		10,185,464
Weighted average shares outstanding - Diluted	10,206,913		10,206,913

**Consolidated Balance Sheet Data:**

	As of June 30, 2013		
	As Originally		
	Reported	Adjustment	As Restated
Inventory	\$ 46,334	\$ —	\$ 46,334
Deferred income taxes	3,167	(216)	2,951
Performance based payments on customer contracts	21,504	(602)	20,902
Retained earnings	65,571	386	65,957

**(3) Acquisitions**

**Beckwood Services, Inc.** — On December 11, 2013, the Company completed the acquisition of Beckwood Services, Inc. ("Beckwood") in a \$15.3 million all-cash transaction, subject to certain post-closing adjustments and financed through the use of cash on hand and borrowings under the Company's Credit Facility. At December 31, 2013, the Company has recorded additional estimated contingent consideration of accounts receivable of less than \$0.1 million in relation to a post-closing working capital adjustment, which is expected to be settled in the third quarter of the Company's fiscal 2014 year. The transaction includes an approximate \$1.5 million escrowed holdback which is available to fund the working capital adjustment and potential seller indemnification obligations in relation to the acquisition agreement.

The acquired business, which is part of the Company's Complex Systems segment and which is expected to add \$18 million in annualized revenue, develops electronic or electro-mechanical controls and electronic assemblies. Their customer profile includes international Fortune 1000 manufacturers of industrial control systems, analytical instruments, measuring and detecting equipment and military, defense and Homeland Security equipment.

The Company is in the process of obtaining valuations of certain tangible and intangible assets and liabilities and expects to complete the purchase price allocation in fiscal year 2014 after these valuations are finalized. The following table represents the preliminary allocation of the total consideration to assets acquired and liabilities assumed in the acquisition of Beckwood based on Sparton's preliminary estimate of their respective fair values (in thousands):

Total purchase consideration:	
Cash	\$ 15,300
Estimated additional consideration payable for post-closing working capital adjustment	36
Total purchase consideration	<u>\$ 15,336</u>
Assets acquired and liabilities assumed:	
Accounts receivable, net	\$ 1,157
Inventory	2,008
Deferred income taxes	213
Other current assets	122
Property, plant and equipment	110
Goodwill	13,353
Deferred income taxes - non-current	7
Other long-term assets	8
Accounts payable	(977)
Other current liabilities	(665)
Total assets acquired and liabilities assumed	<u>\$ 15,336</u>

Total purchase consideration has been allocated to the tangible assets acquired and liabilities assumed based on their provisionally estimated fair values at the acquisition date. It is possible that acquired assets may additionally include customer relationships and the Beckwood name. The Company was unable at December 31, 2013 to assign provisionally estimated fair values to these potential assets. The Beckwood acquisition has preliminarily resulted in approximately \$13 million of goodwill, which will be adjusted downward or upward based on the final values assigned to all acquired assets and liabilities. The Company believes that any goodwill remaining after the valuations are finalized will primarily relate to strategic fit, resulting synergies and the acquired workforce that this business brings to existing operations. Goodwill associated with this acquisition is not expected to be deductible for tax purposes and has been assigned entirely to the Company's Complex Systems segment.

Included in the Company's Condensed Consolidated Statements of Income for the three and six months ended December 31, 2013 are net sales of approximately \$0.8 million and income before provision from income taxes of approximately \$0.1 million, resulting from the acquisition of Beckwood since December 11, 2013.

The Company incurred legal, professional and other costs related to this acquisition aggregating approximately \$0.1 million. These costs were recognized as selling and administrative expenses in the three months ended December 31, 2013.

**Aydin Displays, Inc.** — On August 30, 2013, the Company completed the acquisition of certain assets and liabilities of Aydin Displays, Inc. ("Aydin Displays" or "Aydin") in a \$15.0 million all-cash transaction, subject to certain post-closing adjustments and financed through the use of borrowings under the Company's Credit Facility. At December 31, 2013, the Company has recorded additional estimated contingent consideration of accounts receivable of \$0.4 million in relation to a post-closing working capital adjustment, which is expected to be settled during the Company's fiscal 2014 year. Additional acquisition consideration of up to \$6.6 million is contingent upon Aydin attaining certain performance thresholds during the twelve month period following the transaction. The transaction includes an approximate \$1.2 million escrowed holdback which is available to fund the working capital adjustment and potential seller indemnification obligations in relation to the acquisition agreement.

The acquired business, which is part of the Company's DSS segment and which is expected to add \$18 million in annualized revenue, develops enhanced flat panel display and touch-screen solutions with application-critical performance criteria including ruggedization, high resolution, color accuracy, response/refresh times, sunlight readability and other criteria such as magnetic interference and emanations security for the Military & Aerospace and Civil Marine markets. These products are currently specified in the U.S. Navy P8A Poseidon ASW aircraft behind-the-cockpit control center, the command and control centers of many U.S. Navy ships, Federal Aviation Administration air traffic control systems, and cockpit command centers for various civil marine applications. The acquired business will continue to operate as Aydin Displays.

The following table represents the preliminary allocation of the total consideration to assets acquired and liabilities assumed in the acquisition of Aydin based on Spartan's preliminary estimate of their respective fair values (in thousands):

Total purchase consideration:	
Cash	\$ 15,000
Estimated additional consideration payable for post-closing working capital adjustment	357
Total purchase consideration	<u>\$ 15,357</u>
Assets acquired and liabilities assumed:	
Accounts receivable, net	\$ 2,279
Inventory	6,601
Other current assets	895
Property, plant and equipment	582
Intangible asset - customer relationships	1,500
Intangible asset - trade names and trademarks	180
Intangible asset - unpatented technology	650
Goodwill	2,036
Other long-term assets - favorable leasehold	590
Other long-term assets	1,702
Accounts payable	(1,215)
Other current liabilities	(443)
Total assets acquired and liabilities assumed	<u>\$ 15,357</u>

Total purchase consideration has been preliminarily allocated to the tangible assets acquired and liabilities assumed based on their provisionally estimated fair values at the acquisition date. Additional acquisition consideration of up to \$6.6 million is contingent upon Aydin attaining certain performance thresholds. The Company has assigned no fair value to this contingent liability. The Aydin acquisition has preliminarily resulted in approximately \$2 million of goodwill, which is expected to be deductible for tax purposes and has been assigned entirely to the Company's DSS segment. The Company believes goodwill primarily relates to strategic fit, resulting synergies and the acquired workforce that this business brings to existing operations. The provisional fair values of acquired identifiable assets have been determined to be Level 3 under the fair value hierarchy and have been estimated based on projected future cash flows and customer attrition rates, discounted using an estimated weighted average cost of capital. The customer relationships are being amortized using an accelerated methodology over fifteen years. Trade names and trademarks are being amortized using a straight-line methodology over ten years. The unpatented technology is being amortized using an accelerated methodology over seven years. The favorable leasehold is reflected in other long-term assets on the consolidated balance sheet and is being amortized on a straight-line basis over the five year life of the lease. Amortization related to Aydin unpatented technology and favorable leasehold is reflected within cost of goods sold on the consolidated statement of income.

Included in the Company's Condensed Consolidated Statements of Income for the three and six months ended December 31, 2013 are net sales of approximately \$4.0 million and \$5.2 million, respectively, and loss before benefit from income taxes of less than \$0.1 million and approximately \$0.1 million, respectively, resulting from the acquisition of Aydin since August 30, 2013.

The Company incurred legal, professional and other costs related to this acquisition aggregating approximately \$0.0 million and \$0.2 million for the three and six months ended December 31, 2013, respectively. These costs were recognized as selling and administrative expenses.

A portion of Aydin's revenue is derived from contracts to manufacture video displays and other related products to a buyer's specification under long-term contracts. Revenue and profit is recognized under these contracts using the percentage of completion method based on units shipped to estimated total costs at completion. Certain upfront engineering costs in relation to long-term contracts are capitalized and amortized over the life of the contract.

**Creonix, LLC** — On June 6, 2013, the Company completed the acquisition of certain assets related to the contract manufacturing business of Creonix, LLC ("Creonix") in a \$2.0 million all-cash transaction, after settlement of a \$0.1 million working capital adjustment during the second quarter of the Company's fiscal 2014 year. The transaction was financed through the use of borrowings under the Company's credit facility. The transaction includes an approximate \$0.3 million escrowed holdback which is available to fund the working capital adjustment and potential seller indemnification obligations in relation to the acquisition agreement.

The acquired business, which is reported in the Company's Complex Systems segment, provides the Company with the capability of cable and wire harness engineering and assembly. Additionally, the acquisition provides further expansion into the Industrial and Military & Aerospace markets, diversifies Sparton's customer base and increases utilization of the Company's existing assets through the expected consolidation of this business into Complex Systems's Brooksville, Florida plant during the first six months of fiscal 2014. Creonix primarily manufactures products and components for battery monitoring, high speed optical imaging, neuromuscular incapacitation, imaging and wiring assemblies for military applications, and electrical grid transformer protection systems.

During the six months ended December 31, 2013, the Company finalized the inventory adjustment under the Creonix asset purchase agreement resulting in a decrease in the previously recorded related receivable from the seller. This measurement period increase in total purchase consideration resulted in the retrospective elimination of the previously recognized gain on acquisition recorded in the fourth quarter of fiscal 2013 of less than \$0.1 million and resulting in the recognition of approximately \$0.1 million of goodwill. The Company's June 30, 2013 balance sheet has been restated to reflect this adjustment. The following table presents the final allocation of the total consideration to assets acquired and liabilities assumed from Creonix based on Sparton's estimate of their respective fair values (in thousands):

Total purchase consideration:	
Cash	\$ 2,100
Reduction in cash consideration in relation to working capital adjustment	(105)
Total purchase consideration	<u>\$ 1,995</u>
Assets acquired and liabilities assumed:	
Inventory	\$ 1,321
Equipment	304
Intangible assets — customer relationships	270
Goodwill	100
Total assets acquired and liabilities assumed	<u>\$ 1,995</u>

**Pro Forma Results** — The following table summarizes, on a pro forma basis, the combined results of operations of the Company and the acquired businesses of Aydin and Beckwood as though the acquisitions had occurred as of July 1, 2012. The pro forma amounts presented are not necessarily indicative of either the actual consolidated results had the acquisition occurred as of July 1, 2012 or of future consolidated operating results (in thousands, except per share amounts):

	For the Three Months Ended		For the Six Months Ended	
	December 31, 2013	December 31, 2012	December 31, 2013	December 31, 2012
Net sales	\$ 87,662	\$ 76,519	\$ 168,743	\$ 138,059
Income before provision for income taxes	\$ 5,625	\$ 4,800	\$ 9,710	\$ 7,636
Net income	\$ 3,749	\$ 5,391	\$ 6,516	\$ 7,429
Net income per share — basic	\$ 0.37	\$ 0.53	\$ 0.65	\$ 0.73
Net income per share — diluted	\$ 0.37	\$ 0.53	\$ 0.64	\$ 0.73

Pro forma results presented above reflect: (1) incremental depreciation relating to fair value adjustments to property, plant and equipment; (2) amortization adjustments relating to fair value estimates of intangible assets; (3) elimination of Aydin and Beckwood interest expense relating to debt paid off in conjunction with the transaction; and (4) incremental interest expense on assumed indebtedness and amortization of capitalized financing costs incurred in connection with the transactions as though the transactions occurred as of July 1, 2012.

Additionally, acquisition related expenses of approximately \$0.3 million recognized as selling and administrative expenses in the six months ended December 31, 2013 are reflected in the pro forma results above as though they were recognized during the six months ended December 31, 2012 and have been removed from the pro forma results for the year ended June 30, 2013. Similarly, the capitalization of approximately \$0.3 million of gross profit recognized as part of the purchase accounting for Aydin, of which \$0.1 million has been recognized as additional cost of goods sold during the six months ended December 31, 2013, is reflected in the pro forma results above as though it was recognized during fiscal 2013 and has been removed from the pro forma results for the six months ended December 31, 2013.

Pro forma adjustments described above have been tax effected using Sparton's effective rate during the respective periods.

#### (4) Inventories and Cost of Contracts in Progress

The following are the major classifications of inventory, net of interim billings, at December 31, 2013 and June 30, 2013 (in thousands):

	December 31, 2013	June 30, 2013
Raw materials	\$ 42,344	\$ 43,550
Work in process	15,434	10,170
Finished goods	8,368	7,793
Total inventory and cost of contracts in progress, gross	66,146	61,513
Inventory to which the U.S. government has title due to interim billings	(13,753)	(15,179)
Total inventory and cost of contracts in progress, net	\$ 52,393	\$ 46,334

The Company recorded inventory write-downs of approximately \$0.2 million for both of the three and six months ended December 31, 2013. For the three and six months ended December 31, 2012, the Company recorded inventory write-downs of approximately \$0.5 million. These charges are included in cost of goods sold for the periods presented.

**(5) Property, Plant and Equipment, Net**

Property, plant and equipment, net consists of the following at December 31, 2013 and June 30, 2013 (in thousands):

	December 31, 2013	June 30, 2013
Land and land improvements	\$ 1,429	\$ 1,405
Buildings and building improvements	25,695	24,920
Machinery and equipment	29,035	27,183
Construction in progress	827	767
Total property, plant and equipment	56,986	54,275
Less accumulated depreciation	(28,359)	(25,371)
Total property, plant and equipment, net	\$ 28,627	\$ 28,904

**(6) Goodwill and Other Intangible Assets**

Goodwill represents the excess of purchase price over the fair value of the net assets acquired in conjunction with the Company's purchases of Astro Instrumentation, LLC ("Astro") in May 2006, Byers Peak, Incorporated ("Byers Peak") in March 2011, Onyx EMS, LLC ("Onyx") in November 2012, Creonix in June 2013, Aydin in August 2013 and Beckwood in December 2013. Goodwill related to Astro, Byers Peak and Onyx is reflected within the Company's Medical operating segment. Goodwill related to Creonix and Beckwood are reflected within the Company's Complex Systems operating segment. Goodwill related to Aydin Displays is reflected within the Company's DSS operating segment. Changes in the carrying value of goodwill for the six months ended December 31, 2013 and year ended June 30, 2013 and the ending composition of goodwill as of December 31, 2013 and June 30, 2013 are as follows (in thousands):

	December 31, 2013			
	Medical	CS	DSS	Total
Goodwill, beginning of period	\$ 14,667	\$ 100	\$ —	\$ 14,767
Additions to goodwill during the period	—	13,353	2,036	15,389
Goodwill, end of period	\$ 14,667	\$ 13,453	\$ 2,036	\$ 30,156

	June 30, 2013			
	Medical	CS	DSS	Total
Goodwill, beginning of period	\$ 7,472	\$ —	\$ —	\$ 7,472
Additions to goodwill during the period	7,195	100	—	7,295
Goodwill, end of period	\$ 14,667	\$ 100	\$ —	\$ 14,767

	December 31, 2013			
	Medical	CS	DSS	Total
Acquired Goodwill	\$ 27,820	\$ 13,453	\$ 2,036	\$ 43,309
Accumulated impairment	(13,153)	—	—	(13,153)
Goodwill	\$ 14,667	\$ 13,453	\$ 2,036	\$ 30,156

	June 30, 2013			
	Medical	CS	DSS	Total
Acquired Goodwill	\$ 27,820	\$ 100	\$ —	\$ 27,920
Accumulated impairment	(13,153)	—	—	(13,153)
Goodwill	\$ 14,667	\$ 100	\$ —	\$ 14,767

Other intangible assets represent the values assigned to customer relationships acquired in conjunction with the Company's purchases of Astro, Byers Peak, Onyx, Creonix and Aydin, values assigned to non-compete agreements acquired in conjunction with the Company's purchase of Onyx and values assigned to Trademarks and tradenames and unpatented technology acquired with the Company's purchase of Aydin. The amortization periods, gross carrying amounts, accumulated amortization, accumulated impairments and net carrying values of intangible assets at December 31, 2013 and June 30, 2013 are as follows (in thousands):

	Amortization Period in Months	Gross Carrying Amount	Accumulated Amortization	Accumulated Impairments	Net Carrying Value
<b>December 31, 2013</b>					
<b>Amortized intangible assets:</b>					
Non-compete agreements	12	\$ 200	\$ (200)	\$ —	\$ —
Customer relationships	120 -180	19,870	(5,221)	(3,663)	10,986
Trademarks/Tradenames	120	180	(6)	—	174
Unpatented Technology	84	650	(54)	—	596
		<u>\$ 20,900</u>	<u>\$ (5,481)</u>	<u>\$ (3,663)</u>	<u>\$ 11,756</u>
<b>June 30, 2013</b>					
<b>Amortized intangible assets:</b>					
Non-compete agreements	12	\$ 358	\$ (274)	\$ —	\$ 84
Customer relationships	120 -180	18,370	(4,078)	(3,663)	10,629
		<u>\$ 18,728</u>	<u>\$ (4,352)</u>	<u>\$ (3,663)</u>	<u>\$ 10,713</u>

Sparton did not incur any significant costs to renew or alter the term of its intangible assets during the six months ended December 31, 2013. Amortization expense for the three months ended December 31, 2013 and 2012 was approximately \$0.6 million and \$0.3 million, respectively. Amortization expense for the six months ended December 31, 2013 and 2012 was approximately \$1.2 million and \$0.4 million, respectively. Aggregate amortization expense relative to existing intangible assets for the periods shown is currently estimated to be as follows (in thousands):

<b>Fiscal Year Ending June 30,</b>	
	2014 \$ 2,468
	2015 2,190
	2016 1,927
	2017 1,665
	2018 1,402
Thereafter	3,391
<b>Total</b>	<b>\$ 13,043</b>

## (7) Debt

Debt consists of the following at December 31, 2013 and June 30, 2013 (in thousands):

	<b>December 31, 2013</b>	<b>June 30, 2013</b>
Industrial revenue bonds, face value	\$ 1,552	\$ 1,623
Less unamortized purchase discount	(80)	(84)
Industrial revenue bonds, carrying value	1,472	1,539
Borrowings under revolving credit facilities	25,000	10,000
<b>Total debt</b>	<b>26,472</b>	<b>11,539</b>
Less: current portion	(141)	(136)
<b>Long-term debt, net of current portion</b>	<b>\$ 26,331</b>	<b>\$ 11,403</b>



### **Industrial Revenue Bonds**

In connection with its acquisition of Astro in May 2006, the Company assumed repayment of principal and interest on bonds originally issued to Astro by the State of Ohio. These bonds are Ohio State Economic Development Revenue Bonds, series 2002-4. Astro originally entered into the loan agreement with the State of Ohio for the issuance of these bonds to finance the construction of the Company's Ohio operating facility. The principal amount, including premium, was issued in 2002 and totaled approximately \$2.9 million. These bonds have interest rates which vary, dependent on the maturity date of the bonds ranging from 5.00% to 5.45%. Due to an increase in interest rates since the original issuance of the bonds, a discount amounting to approximately \$0.2 million on the date of assumption by Sparton was recorded.

The bonds carry certain sinking fund requirements generally obligating the Company to make monthly deposits of one twelfth of the annual obligation plus accrued interest. The purchase discount is being amortized ratably over the remaining term of the bonds. The Company also has an irrevocable letter of credit in the amount of approximately \$0.3 million, which is renewable annually, to secure repayment of a portion of the bonds.

Short-term debt at December 31, 2013 and June 30, 2013 reflects the current portion of the Company's industrial revenue bonds.

### **Revolving Credit Facility**

On November 15, 2012, the Company replaced its previous revolving line-of-credit facility with a new \$65 million credit facility with BMO Harris Bank N.A., consisting of a \$35 million revolving line-of-credit facility (the "Revolving Credit") to support the Company's working capital needs and other general corporate purposes, and a \$30 million acquisition loan commitment (the "Acquisition Facility" and together with the Revolving Credit, the "Credit Facility") to finance permitted acquisitions.

The Credit Facility expires on November 15, 2017, is secured by substantially all assets of the Company and provides for up to an additional \$35 million in uncommitted loans available for additional Revolving Credit loans or Acquisition loans.

Advances under the Acquisition Facility are available until November 15, 2014. Loans under the Acquisition Facility amortize in two tranches, such that loans outstanding on November 15, 2013 begin amortizing in quarterly installments equal to 2.5% of the principal amount outstanding on such date, and advances made after November 15, 2013 and outstanding on November 15, 2014 begin amortizing on the same basis.

Outstanding borrowings under the Credit Facility bear interest, at the Company's option, at either LIBOR, fixed for interest periods of one, two, three or six month periods, plus 1.25% to 2.00%, or at the bank's base rate, as defined, plus 0.25% to 1.00%, based upon the Company's Total Funded Debt/EBITDA Ratio, as defined. The Company is also required to pay commitment fees on unused portions of the Credit Facility ranging from 0.25% to 0.375%, based on the Company's Total Funded Debt/EBITDA Ratio, as defined. The effective interest rate on outstanding borrowings under the Credit Facility was 1.67% at December 31, 2013.

As a condition of the Credit Facility, the Company is subject to certain customary covenants, which it was in compliance with at December 31, 2013. The Company had \$25.0 million of borrowings drawn against the Credit Facility at December 31, 2013 and additionally had certain letters of credit outstanding totaling \$0.5 million.

### **(8) Fair Value Measurements**

The Company's long-term debt instruments, consisting of industrial revenue bonds, are carried at historical cost. As of December 31, 2013 and June 30, 2013, the fair value of the industrial revenue bonds was approximately \$1.8 million and \$2.0 million, respectively, compared to carrying values of approximately \$1.5 million and \$1.5 million, respectively. These fair values, which were derived from discounted cash flow analyses based on the terms of the contracts and observable market data, and adjustment for nonperformance risk, are classified as Level 3 in the fair value hierarchy. The fair value of the Company's Credit Facility debt at December 31, 2013 and June 30, 2013 approximated its carrying value of \$25.0 million and \$10.0 million, respectively, as the rates on these borrowings are variable in nature. In relation to the acquisition of Creonix, Aydin and Beckwood, the Company estimated the fair value of the assets acquired and liabilities assumed at acquisition date. See Note 3 for a further discussion of these estimated fair values. The fair value of accounts receivable and accounts payable approximated their carrying values at both December 31, 2013 and June 30, 2013.

**(9) Income Taxes**

The Company recognized income tax provisions of approximately \$1.7 million and \$2.8 million, or approximately 33.3% and 33.0% of income before provision for income taxes, for the three and six months ended December 31, 2013, respectively. During the three months ended December 31, 2012, the Company recognized a \$2.1 million income tax benefit from claiming a worthless stock and bad debt deduction with respect to its investments and advances to its 100% owned Canadian subsidiary, Sparton of Canada, Ltd. Sparton of Canada, Ltd. is the legal entity that held the Company's Canadian operations until these operations were ceased during fiscal 2009. Excluding this discrete tax benefit, the Company recognized income tax provisions of approximately \$1.4 million and \$2.1 million, or approximately 32.7% and 32.9%, respectively, of income before provision for income taxes, for the three and six months ended December 31, 2012. The Company's effective income tax rate for the interim periods presented is based on management's estimate of the Company's effective tax rate for the applicable year and differs from the Federal statutory income tax rate primarily due to applicable permanent differences, foreign income taxes and state income taxes.

**(10) Defined Benefit Pension Plan**

Approximately 400 employees and retirees of the Company are covered by a defined benefit pension plan. Effective April 1, 2009, participation and the accrual of benefits in this pension plan were frozen, at which time all participants became fully vested and all prior service costs were recognized. The components of net periodic pension expense are as follows for the three and six months ended December 31, 2013 and 2012 (in thousands):

	For the Three Months Ended		For the Six Months Ended	
	December 31, 2013	December 31, 2012	December 31, 2013	December 31, 2012
Service cost	\$ —	\$ —	\$ —	\$ —
Interest cost	91	67	177	171
Expected return on plan assets	(133)	(117)	(262)	(257)
Amortization of prior service cost	—	—	—	—
Amortization of unrecognized net actuarial loss	18	81	64	92
Net pension expense (income)	(24)	31	(21)	6
Pro rata recognition of lump-sum settlements	—	(25)	—	—
Total pension expense (income)	\$ (24)	\$ 6	\$ (21)	\$ 6

The Company's policy is to fund the plan based upon legal requirements and tax regulations. During each of the six months ended December 31, 2013 and 2012, less than \$0.1 million was contributed to the pension plan. For further information on future funding projections and other pension disclosures see Part II, Item 8, Note 9 "Employee Retirement Benefit Plans" of the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2013.

**(11) Commitments and Contingencies**

**Environmental Remediation** — Sparton has been involved with ongoing environmental remediation since the early 1980's related to one of its former manufacturing facilities, located in Albuquerque, New Mexico ("Coors Road"). Although the Company entered into a long-term lease of the Coors Road property that was accounted for as a sale of property during fiscal 2010, it remains responsible for the remediation obligations related to its past operation of this facility. At December 31, 2013, Sparton had accrued approximately \$2.9 million as its estimate of the remaining minimum future undiscounted financial liability with respect to this matter, of which approximately \$0.4 million is classified as a current liability and included on the balance sheet in other accrued expenses. The Company's minimum cost estimate is based upon existing technology and excludes certain legal costs, which are expensed as incurred. The Company's estimate includes equipment and operating and maintenance costs for onsite and offsite pump and treat containment systems, as well as continued onsite and offsite monitoring. It also includes periodic reporting requirements.

In fiscal 2003, Sparton reached an agreement with the United States Department of Energy (“DOE”) and others to recover certain remediation costs. Under the settlement terms, Sparton received cash and obtained some degree of risk protection as the DOE agreed to reimburse Sparton for 37.5% of certain future environmental expenses in excess of \$8.4 million incurred from the date of settlement, if any, of which approximately \$4.9 million has been expended as of December 31, 2013 toward the \$8.4 million threshold. Uncertainties associated with environmental remediation contingencies are pervasive and often result in wide ranges of reasonably possible outcomes. Estimates developed in the early stages of remediation can vary significantly. Normally a finite estimate of cost does not become fixed and determinable at a specific point in time. Rather, the costs associated with environmental remediation become estimable over a continuum of events and activities that help to frame and define a liability. Factors which cause uncertainties for the Company include, but are not limited to, the effectiveness of the current work plans in achieving targeted results and proposals of regulatory agencies for desired methods and outcomes. It is possible that cash flows and results of operations could be materially affected by the impact of changes associated with the ultimate resolution of this contingency. At December 31, 2013, the Company estimates that it is reasonably possible, but not probable, that future environmental remediation costs associated with the Company’s past operations at the Coors Road property, in excess of amounts already recorded and net of DOE reimbursement, could be up to \$2.4 million before income taxes over the next seventeen years.

The Company and its subsidiaries are also involved in certain existing compliance issues with the EPA and various state agencies, including being named as a potentially responsible party at several sites. Potentially responsible parties (“PRP’s”) can be held jointly and severally liable for the clean-up costs at any specific site. The Company’s past experience, however, has indicated that when it has contributed relatively small amounts of materials or waste to a specific site relative to other PRPs, its ultimate share of any clean-up costs has been minor. Based upon available information, the Company believes it has contributed only small amounts to those sites in which it is currently viewed as a PRP and that reasonably possible losses related to these compliance issues are immaterial.

**Litigation** — On September 24, 2013, L-3 Communications Corporation, doing business as L-3 Linkabit (“Linkabit”) filed a complaint in the United States District Court for the Middle District of Florida, Orlando Division, alleging, among other things, that the Company failed to follow Linkabit drawings for the manufacture and assembly of certain products and that the Company changed its manufacturing process resulting in shipment of defective products to Linkabit. Linkabit seeks damages for breach of contract, breach of covenants, breach of warranties and negligence. In response to the Company’s motion to dismiss on January 10, 2014, Linkabit filed its first amended complaint deleting the alleged negligence claims. The Company believes that its defenses to the claims are very strong and it intends to defend this action vigorously. Given the stage of the litigation and the unresolved remaining questions of fact, the Company cannot estimate any loss, or range of loss, with confidence at this time.

**U.S. Government Audits** — Federal government agencies, including the Defense Contract Audit Agency (“DCAA”) and the Defense Contract Management Agency (“DCMA”), routinely audit and evaluate government contracts and government contractors’ administrative processes and systems. These agencies review the Company’s performance on contracts, pricing practices, cost structure, financial capability and compliance with applicable laws, regulations and standards. They also review the adequacy of the Company’s internal control systems and policies, including the Company’s purchasing, accounting, estimating, compensation and management information processes and systems.

The Company implemented a new enterprise resource planning system in November 2012 and currently remains eligible to receive cost reimbursable contracts from the U.S. Government. The Company responded in June 2013 to DCAA review comments received in the fourth quarter of fiscal 2013 regarding corrective actions to improve the reliability for accumulating costs under government contracts. While the Company’s corrective actions remain open for further review, the Company remains confident formal resolution of DCAA cost accounting practices findings will not have a material adverse impact on the Company’s financial results.

**Other** — In addition to the foregoing, from time to time, the Company is involved in various legal proceedings relating to claims arising in the ordinary course of business. The Company is not currently a party to any other such legal proceedings, the adverse outcome of which, individually or in the aggregate, is expected to have a material adverse effect on our business, financial condition or results of operations.

## **(12) Stock-Based Compensation**

The Company has two long-term incentive plans. The Sparton Corporation Stock Incentive Plan, as amended and restated (the “2001 Plan”) was approved by the Company’s shareholders on October 24, 2001. The Sparton Corporation 2010 Long-Term Incentive Plan (the “2010 Plan”) was approved by the Company’s shareholders on October 28, 2009.

**2001 Plan.** Under the 2001 Plan, the Company may grant to employees and non-employee directors incentive and non-qualified stock options, stock appreciation rights, restricted stock and other stock-based awards. All of the stock options issued to date under the 2001 Plan have either three, five or ten-year lives with either immediate vesting or vesting on an annual basis over four years beginning one year after grant date. Restricted stock awards granted to date to employees under the 2001 Plan vest annually over periods ranging from approximately 2.5 to 4.0 years, in some cases subject to achievement of certain financial performance metrics in addition to the service requirements. Unrestricted stock awards granted to date under the 2001 Plan represent annual stock grants to directors as a component of their overall compensation. The 2001 Plan's termination date with respect to the granting of new awards was October 24, 2011. The total number of shares authorized to be granted under the 2001 Plan was 970,161 shares of the Company's common stock, which equals the number of underlying awards previously made under the 2001 Plan.

**2010 Plan.** Under the 2010 Plan, the Company may grant to employees, officers and directors of the Company or its subsidiaries incentive and non-qualified stock options, stock appreciation rights, restricted stock or restricted stock units, performance awards and other stock-based awards, including grants of shares. Restricted stock awards granted to date to employees under the 2010 Plan vest annually over four years, subject to achievement of certain financial performance metrics in addition to the service requirements. Unrestricted stock awards granted to date under the 2010 Plan represent annual stock grants to directors as a component of their overall compensation. The 2010 Plan has a term of ten years. The total number of shares that may be awarded under the 2010 Plan is 1,000,000 shares of common stock, of which amount, 500,952 shares remain available for awards as of December 31, 2013.

The following table shows stock-based compensation expense by type of share-based award for the three and six months ended December 31, 2013 and 2012, respectively, included in the condensed consolidated statements of income (in thousands):

	For the Three Months Ended		For the Six Months Ended	
	December 31, 2013	December 31, 2012	December 31, 2013	December 31, 2012
Fair value expense of stock option awards	\$ —	\$ —	\$ —	\$ —
Restricted and unrestricted stock	620	333	917	597
Total stock-based compensation	\$ 620	\$ 333	\$ 917	\$ 597

The following table shows the total remaining unrecognized compensation cost related to restricted stock grants and the fair value expense of stock option awards, as well as the weighted average remaining required service period over which such costs will be recognized as of December 31, 2013:

	Total Remaining Unrecognized Compensation Cost (in thousands)	Weighted Average Remaining Required Service Period (in years)
Fair value expense of stock option awards	\$ —	0
Restricted stock	2,059	2.03
	\$ 2,059	2.03

The following is a summary of options outstanding and exercisable at December 31, 2013:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding at June 30, 2013	55,418	\$ 8.56		
Granted	—	—		
Exercised	(14,119)	8.54		
Forfeited	—	—		
Expired	—	—		
Outstanding and exercisable at December 31, 2013	41,299	\$ 8.57	1.33	\$ 800

The intrinsic value of options exercised during the six months ended December 31, 2013 and 2012 was \$0.2 million and \$0.1 million, respectively.

The following is a summary of activity for the six months ended December 31, 2013 related to shares granted under the Company's long-term incentive plans:

	Shares	Weighted Average Grant Date Fair Value
Restricted shares at June 30, 2013	311,253	\$ 8.34
Granted	94,811	21.80
Vested	(87,576)	8.54
Forfeited	(3,344)	14.39
Restricted shares at December 31, 2013	315,144	\$ 12.27

The total fair value of restricted stock vested in the six months ended December 31, 2013 and 2012 was approximately \$1.6 million and \$1.0 million, respectively.

### (13) Earnings Per Share Data

Basic earnings per share is based on the weighted average number of common shares and participating securities outstanding during the period. Diluted earnings per share include the dilutive effect of additional potential common shares issuable under our stock-based compensation plan and are determined using the treasury stock method. Unvested restricted stock awards, which contain non-forfeitable rights to dividends whether paid or unpaid, are included in the number of shares outstanding for both basic and diluted earnings per share calculations. In the event of a net loss, unvested restricted stock awards are excluded from the calculation of both basic and diluted loss per share.

Earnings per share calculations, including weighted average number of shares of common stock outstanding used in calculating basic and diluted income per share, for the three and six months ended December 31, 2013 and 2012 are as follows:

	For the Three Months Ended		For the Six Months Ended	
	December 31, 2013	December 31, 2012	December 31, 2013	December 31, 2012
Net income (in thousands)	\$ 3,484	\$ 4,841	\$ 5,770	\$ 6,298
Weighted average shares outstanding – Basic	10,115,255	10,229,320	10,093,973	10,185,464
Net effect of dilutive stock options	32,263	19,104	29,569	21,449
Weighted average shares outstanding – Diluted	10,147,518	10,248,424	10,123,542	10,206,913
Net income per share:				
Basic	\$ 0.34	\$ 0.47	\$ 0.57	\$ 0.62
Diluted	\$ 0.34	\$ 0.47	\$ 0.57	\$ 0.62

For the three months ended December 31, 2013 and 2012, 315,144 and 346,783, respectively, unvested restricted shares were included in determining both basic and diluted earnings per share. For the six months ended December 31, 2013 and 2012, 315,144 and 346,783, respectively, unvested restricted shares were included in determining both basic and diluted earnings per share. No potential shares of common stock were excluded from diluted income per share computations for either of the three or six months ended December 31, 2013 or 2012.

### (14) Stock Repurchase Plan

On May 1, 2013, the Company's Board of Directors approved a repurchase by the Company of up to \$3.0 million of shares of its common stock over a 12-month period. The Company has been authorized to purchase shares from time to time in open market, block transactions and privately negotiated transactions at prices deemed appropriate by management, depending on market conditions, applicable laws and other factors. The stock repurchase program does not require the Company to repurchase any specific number of shares and can be modified, extended or terminated by the Board of Directors at any time.

Pursuant to this stock repurchase program, during the three months ended September 30, 2013, the Company purchased 47,119 shares of its common stock at an average price of \$18.51 per share for approximately \$0.9 million. Previously, during the year ended June 30, 2013, the Company purchased 128,158 shares of its common stock at an average price of \$16.55 per share for approximately \$2.1 million. Total shares purchased pursuant to this stock repurchase program total 175,277 at an average price of \$17.08. Shares purchased under the plan were cancelled upon repurchase. As of December 31, 2013, all authorized funds under the stock repurchase program have been expended.

**(15) Restructuring Activities****Creonix Acquisition Related Restructuring**

In conjunction with the Creonix acquisition, the Company consolidated the Creonix operations into the Company's Brooksville, Florida facility. These restructuring activities consisted primarily of approximately \$0.2 million of workforce severance and retention costs, less than \$0.1 million of production transfer costs and less than \$0.1 million of facility closing costs. Inception to date restructuring charges recognized within the Complex Systems segment of approximately \$0.2 million were incurred as of September 30, 2013 related to these acquisition related restructuring activities. The Company does not expect to recognize any additional costs related to these restructuring activities. All cash expenditures related to these activities have been made as of December 31, 2013.

**Summary of Restructuring Charges**

The table below summarizes the nature and amount of all restructuring actions for the six months ended December 31, 2013 (in thousands):

	Workforce Reduction (principally severance and retention bonuses)	Production Transfer	Facility Closing	Total
Accrual balance at June 30, 2013	44	—	—	44
Restructuring charges	111	68	9	188
Less: cash payments	(155)	(68)	(9)	(232)
Restructuring reversals	—	—	—	—
Accrual balance at December 31, 2013	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>

**(16) Business Segments**

The Company is a provider of complex and sophisticated electromechanical devices with capabilities that include concept development, design and manufacturing engineering, production, distribution, and field service. Reportable segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or group, in assessing performance and allocating resources. The Company serves the Medical & Biotechnology, Military & Aerospace and Industrial & Commercial markets through three reportable business segments; Medical Device ("Medical"), Complex Systems ("CS") and Defense & Security Systems ("DSS").

The Company uses an internal management reporting system, which provides important financial data to evaluate performance and allocate the Company's resources on a segment basis. Net sales are attributed to the segment in which the product is manufactured or service is performed. A segment's performance is evaluated based upon its operating income (loss). A segment's operating income (loss) includes its gross profit on sales less its selling and administrative expenses, including allocations of certain corporate operating expenses. Certain corporate operating expenses are allocated to segment results based on the nature of the service provided. Other corporate operating expenses, including certain administrative, financial and human resource activities as well as items such as interest expense, interest income, other income (expense) and income tax expense (benefit), are not allocated to operations and are excluded from segment profit. These costs are not allocated to the segments, as management excludes such costs when assessing the performance of the segments. Inter-segment transactions are generally accounted for at amounts that approximate arm's length transactions. Identifiable assets by segments are those assets that are used in each segment's operations. The accounting policies for each of the segments are the same as for the Company taken as a whole.

**Medical segment** operations are comprised of contract design, manufacturing, and aftermarket repair and refurbishment of sophisticated medical and biotechnology devices and sub-assemblies. Customers include industry leaders, emerging technologies companies and start-ups. In manufacturing devices for its customers, this business unit follows specific design and manufacturing processes to assure product reliability and safety in accordance with Food and Drug Administration ("FDA") guidelines and approvals. This group specializes in technologies, systems and processes required by medical OEM and ET customers primarily in the diagnostic, therapeutic, surgical and laboratory device segments of the medical and biotechnology marketplaces. The Medical segment also includes environmental monitoring and industrial systems and controls customers.

**Complex Systems segment** operations are comprised of manufacturing and aftermarket repair and refurbishment of sophisticated printed circuit card assemblies, sub-assemblies, full product assemblies, and cable/wire harnesses. Customers include military and aerospace, as well as industrial and commercial OEM's. In manufacturing for its customers, this segment adheres to very strict military and aerospace specifications in addition to product and process certifications. Customers are primarily engaged in applications that include: flight controls, cockpit displays, fuel system controls, secure communications, early warning detection, security systems, satellite communications, and audio.

**Defense & Security Systems segment** operations are comprised of design, development and production of products for both domestic and foreign defense as well as commercial needs. Sparton designs and manufactures anti-submarine warfare ("ASW") devices known as sonobuoys for the U.S. Navy and foreign governments that meet Department of State licensing requirements. This segment also performs an engineering development function for the United States military and prime defense contractors for advanced technologies ultimately leading to future defense products as well as replacements for existing products. The sonobuoy product line is built to stringent military specifications. These products are restricted by International Tariff and Arms Regulations ("ITAR") and qualified by the U.S. Navy, which limits opportunities for competition. Sparton is also a provider of ruggedized flat panel display systems for military panel PC workstations, air traffic control and industrial applications. Ruggedized displays are manufactured for prime contractors to specific military grade specifications. Additionally, this business unit internally develops and markets commercial products for underwater acoustics and microelectromechanical ("MEMS")-based inertial measurement.

Operating results and certain other financial information about the Company's three reportable segments for the three and six months ended December 31, 2013 and 2012 and as of December 31, 2013 and June 30, 2013 were as follows (in thousands):

	For the Three Months Ended December 31, 2013					
	Medical	CS	DSS	Other Unallocated	Eliminations	Total
Sales	\$ 44,316	\$ 18,304	\$ 26,078	\$ —	\$ (4,136)	\$ 84,562
Gross profit	\$ 6,824	\$ 1,944	\$ 6,209	\$ —	\$ —	\$ 14,977
Operating income (loss)	\$ 3,663	\$ 1,019	\$ 3,590	\$ (3,015)	\$ —	\$ 5,257
Selling and administrative expenses	\$ 2,606	\$ 913	\$ 2,148	\$ 3,020	\$ —	\$ 8,687
Internal research and development expenses	\$ —	\$ —	\$ 402	\$ —	\$ —	\$ 402
Restructuring Charges	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Depreciation/amortization	\$ 1,225	\$ 204	\$ 390	\$ 100	\$ —	\$ 1,919
Capital expenditures	\$ 352	\$ 66	\$ 324	\$ 196	\$ —	\$ 938
	For the Three Months Ended December 31, 2012					
	Medical	CS	DSS	Other Unallocated	Eliminations	Total
Sales	\$ 34,804	\$ 14,059	\$ 22,677	\$ —	\$ (4,286)	\$ 67,254
Gross profit	\$ 4,344	\$ 1,428	\$ 6,323	\$ —	\$ —	\$ 12,095
Operating income (loss)	\$ 1,803	\$ 777	\$ 4,830	\$ (3,210)	\$ —	\$ 4,200
Selling and administrative expenses	\$ 2,268	\$ 651	\$ 1,250	\$ 3,206	\$ —	\$ 7,375
Internal research and development expenses	\$ —	\$ —	\$ 243	\$ —	\$ —	\$ 243
Depreciation/amortization	\$ 634	\$ 148	\$ 153	\$ 58	\$ —	\$ 993
Capital expenditures	\$ 335	\$ 20	\$ 132	\$ 57	\$ —	\$ 544
	For the Six Months Ended December 31, 2013					
	Medical	CS	DSS	Other Unallocated	Eliminations	Total
Sales	\$ 86,324	\$ 36,569	\$ 43,971	\$ —	\$ (8,104)	\$ 158,760
Gross profit	\$ 13,802	\$ 3,812	\$ 9,557	\$ —	\$ —	\$ 27,171
Operating income (loss)	\$ 7,604	\$ 1,904	\$ 4,874	\$ (5,748)	\$ —	\$ 8,634
Selling and administrative expenses	\$ 5,057	\$ 1,696	\$ 3,823	\$ 5,756	\$ —	\$ 16,332
Internal research and development expenses	\$ —	\$ —	\$ 791	\$ —	\$ —	\$ 791
Restructuring charges	\$ —	\$ 188	\$ —	\$ —	\$ —	\$ 188
Depreciation/amortization	\$ 2,462	\$ 422	\$ 564	\$ 192	\$ —	\$ 3,640
Capital expenditures, net	\$ 420	\$ 66	\$ 619	\$ 307	\$ —	\$ 1,412
	For the Six Months Ended December 31, 2012					
	Medical	CS	DSS	Other Unallocated	Eliminations	Total
Sales	\$ 62,863	\$ 26,406	\$ 37,664	\$ —	\$ (8,878)	\$ 118,055
Gross profit	\$ 8,538	\$ 2,524	\$ 9,033	\$ —	\$ —	\$ 20,095
Operating income (loss)	\$ 4,425	\$ 1,163	\$ 6,155	\$ (5,412)	\$ —	\$ 6,331
Selling and administrative expenses	\$ 3,738	\$ 1,361	\$ 2,330	\$ 5,418	\$ —	\$ 12,847
Internal research and development expenses	\$ —	\$ —	\$ 548	\$ —	\$ —	\$ 548
Depreciation/amortization	\$ 807	\$ 291	\$ 297	\$ 77	\$ —	\$ 1,472
Capital expenditures	\$ 344	\$ 726	\$ 256	\$ 276	\$ —	\$ 1,602



	As of December 31, 2013					
	Medical	CS	DSS	Other Unallocated	Eliminations	Total
Total assets	\$ 91,609	\$ 50,939	\$ 26,927	\$ 13,081	\$ —	\$ 182,556
	As of June 30, 2013					
	Medical	CS	DSS	Other Unallocated	Eliminations	Total
Total assets	\$ 95,776	\$ 36,039	\$ 16,952	\$ 17,155	\$ —	\$ 165,922

**(17) New Accounting Standards**

In July 2013, the Financial Accounting Standards Board (the "FASB") issued authoritative guidance under Accounting Standards Update No. 2013-11 ("ASU 2013-11"), which provides guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss ("NOL") carryforward, a similar tax loss, or a tax credit carryforward exists. ASU 2013-11 requires entities to present an unrecognized tax benefit as a reduction of a deferred tax asset for a NOL or tax credit carryforward whenever the NOL or tax credit carryforward would be available to reduce the additional taxable income or tax due if the tax position is disallowed. This accounting standard update requires entities to assess whether to net the unrecognized tax benefit with a deferred tax asset as of the reporting date. ASU 2013-11 will be effective for the Company's first quarter of fiscal 2015. The Company is currently evaluating the impact of this accounting standard update on its consolidated financial statements.

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

The following is management’s discussion and analysis of certain significant events affecting Sparton Corporation’s (the “Company” or “Sparton”) results of operations and financial condition during the periods included in the accompanying financial statements. Additional information regarding the Company can be accessed via Sparton’s website at [www.sparton.com](http://www.sparton.com). Information provided at the website includes, among other items, the Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Quarterly Earnings Releases, News Releases, and the Code of Business Conduct and Ethics, as well as various corporate charters and documents.

The Private Securities Litigation Reform Act of 1995 reflects Congress’ determination that the disclosure of forward-looking information is desirable for investors and encourages such disclosure by providing a safe harbor for forward-looking statements by corporate management. This report on Form 10-Q contains forward-looking statements within the scope of the Securities Act of 1933 and the Securities Exchange Act of 1934. The words “expects,” “anticipates,” “believes,” “intends,” “plans,” “will,” “shall,” and similar expressions, and the negatives of such expressions, are intended to identify forward-looking statements. In addition, any statements which refer to expectations, projections or other characterizations of future events or circumstances are forward-looking statements. The Company undertakes no obligation to publicly disclose any revisions to these forward-looking statements to reflect events or circumstances occurring subsequent to filing this Form 10-Q with the Securities and Exchange Commission (“SEC”). These forward-looking statements are subject to risks and uncertainties, including, without limitation, those discussed below. Accordingly, Sparton’s future results may differ materially from historical results or from those discussed or implied by these forward-looking statements. The Company notes that a variety of factors could cause the actual results and experience to differ materially from anticipated results or other expectations expressed in the Company’s forward-looking statements.

### **Business Overview**

#### ***General***

Sparton is a provider of complex and sophisticated electromechanical devices with capabilities that include concept development, design and manufacturing engineering, production, distribution, and field service. The Company serves the Medical & Biotechnology, Military & Aerospace and Industrial & Commercial markets through three reportable business segments; Medical Device (“Medical”), Complex Systems (“CS”) and Defense & Security Systems (“DSS”).

All of the Company’s facilities are registered to ISO standards, including 9001 or 13485, with most having additional certifications. The Company’s products and services include products for Original Equipment Manufacturers (“OEM”) and Emerging Technology (“ET”) customers that are microprocessor-based systems that include transducers, printed circuit boards and assemblies, sensors, and electromechanical components, as well as development and design engineering services relating to these product sales. Sparton also develops and manufactures sonobuoys, anti-submarine warfare (“ASW”) devices used by the United States Navy and other free-world countries. Many of the physical and technical attributes in the production of sonobuoys are similar to those required in the production of the Company’s other electrical and electromechanical products and assemblies.

The Company uses an internal management reporting system, which provides important financial data to evaluate performance and allocate the Company’s resources on a segment basis. Net sales are attributed to the segment in which the product is manufactured or service is performed. A segment’s performance is evaluated based upon its operating income (loss). A segment’s operating income (loss) includes its gross profit on sales less its selling and administrative expenses, including allocations of certain corporate operating expenses. Certain corporate operating expenses are allocated to segment results based on the nature of the service provided. Other corporate operating expenses, including certain administrative, financial and human resource activities as well as items such as interest expense, interest income, other income (expense) and income tax expense (benefit), are not allocated to operations and are excluded from segment profit. These costs are not allocated to the segments, as management excludes such costs when assessing the performance of the segments. Inter-segment transactions are generally accounted for at amounts that approximate arm’s length transactions. Identifiable assets by segments are those assets that are used in each segment’s operations. The accounting policies for each of the segments are the same as for the Company taken as a whole.

### ***Medical Segment***

Medical segment operations are comprised of contract design, manufacturing, and aftermarket repair and refurbishment of sophisticated medical and biotechnology devices and sub-assemblies. Customers include industry leaders, emerging technologies companies and start-ups. In manufacturing devices for its customers, this business unit follows specific design and manufacturing processes to assure product reliability and safety in accordance with Food and Drug Administration ("FDA") guidelines and approvals. This group specializes in technologies, systems and processes required by medical OEM and ET customers primarily in the diagnostic, therapeutic, surgical and laboratory device segments of the medical and biotechnology marketplaces. The Medical segment also includes environmental monitoring and industrial systems and controls customers.

### ***Complex Systems Segment***

Complex Systems segment operations are comprised of manufacturing and aftermarket repair and refurbishment of sophisticated printed circuit card assemblies, sub-assemblies, full product assemblies, and cable/wire harnesses. Customers include military and aerospace, as well as industrial and commercial OEM's. In manufacturing for its customers, this segment adheres to very strict military and aerospace specifications in addition to product and process certifications. Customers are primarily engaged in applications that include: flight controls, cockpit displays, fuel system controls, secure communications, early warning detection, security systems, satellite communications, and audio.

### ***DSS Segment***

Defense & Security segment operations are comprised of design, development and production of products for both domestic and foreign defense as well as commercial needs. Sparton designs and manufactures anti-submarine warfare ("ASW") devices known as sonobuoys for the U.S. Navy and foreign governments that meet Department of State licensing requirements. This segment also performs an engineering development function for the United States military and prime defense contractors for advanced technologies ultimately leading to future defense products as well as replacements for existing products. The sonobuoy product line is built to stringent military specifications. These products are restricted by International Tariff and Arms Regulations ("ITAR") and qualified by the U.S. Navy, which limits opportunities for competition. Sparton is also a provider of ruggedized flat panel display systems for military panel PC workstations, air traffic control and industrial applications. Ruggedized displays are manufactured for prime contractors to specific military grade specifications. Additionally, this business unit internally develops and markets commercial products for underwater acoustics and microelectromechanical ("MEMS")-based inertial measurement.

### ***Risks and Uncertainties***

Sparton, as a high-mix, low to medium volume supplier, provides rapid product turnaround for customers. High-mix describes customers needing multiple product types with generally low to medium volume manufacturing runs. As a contract manufacturer with customers in a variety of markets, the Company has substantially less visibility of end user demand and, therefore, forecasting sales can be problematic. Customers may cancel their orders, change production quantities and/or reschedule production for a number of reasons. Depressed economic conditions may result in customers delaying delivery of product, or the placement of purchase orders for lower volumes than previously anticipated. Unplanned cancellations, reductions, or delays by customers may negatively impact the Company's results of operations. As many of the Company's costs and operating expenses are relatively fixed within given ranges of production, a reduction in customer demand can disproportionately affect the Company's gross margins and operating income. The majority of the Company's sales have historically come from a limited number of customers. Significant reductions in sales to, or a loss of, one of these customers could materially impact our operating results if the Company were not able to replace those sales with new business.

Other risks and uncertainties that may affect our operations, performance, growth forecasts and business results include, but are not limited to, timing and fluctuations in U.S. and/or world economies, sharp volatility of world financial markets over a short period of time, competition in the overall contract manufacturing business, availability of production labor and management services under terms acceptable to the Company, Congressional budget outlays for sonobuoy development and production, Congressional legislation, uncertainties associated with the outcome of litigation, changes in the interpretation of environmental laws and the uncertainties of environmental remediation and customer labor and work strikes. Further risk factors are the availability and cost of materials, as well as non-cancelable purchase orders we have committed to in relation to customer forecasts that can be subject to change. A number of events can impact these risks and uncertainties, including potential escalating utility and other related costs due to natural disasters, as well as political uncertainties such as the unrest in Africa and the Middle East. Additional trends, risks and uncertainties include dependence on key personnel, risks surrounding acquisitions, uncertainties surrounding the global economy, U.S. healthcare legislation, U.S. budget sequestration and debt ceiling negotiations and the effects of those uncertainties on OEM behavior, including heightened inventory management, product development cycles and outsourcing strategies. Finally, the Sarbanes-Oxley Act, and more recently the Dodd-Frank Act, have required or will require changes in, and formalization of, some of the Company's corporate governance and compliance practices. The SEC and the New York Stock Exchange have also passed or will pass related rules and regulations requiring additional compliance activities, including those implementing the conflict minerals provisions of the Dodd-Frank Act. Compliance with these rules has increased administrative costs and may increase these costs further in the future. A further discussion of the Company's risk factors has been included in Part I, Item 1A, "Risk Factors", of this Annual Report on Form 10-K. Management cautions readers not to place undue reliance on forward-looking statements, which are subject to influence by the enumerated risk factors as well as unanticipated future events.

#### **Acquisition of Beckwood Services, Inc.**

On December 11, 2013, the Company completed the acquisition of Beckwood Services, Inc. ("Beckwood") in a \$15.3 million all-cash transaction, subject to certain post-closing adjustments and financed through the use of cash on hand and borrowings under the Company's Credit Facility. At December 31, 2013, the Company has recorded additional estimated contingent consideration of accounts receivable of less than \$0.1 million in relation to a post-closing working capital adjustment, which is expected to be settled in the third quarter of the Company's fiscal 2014 year. The transaction includes an approximate \$1.5 million escrowed holdback which is available to fund the working capital adjustment and potential seller indemnification obligations in relation to the acquisition agreement.

The acquired business, which is part of the Company's Complex Systems segment and which is expected to add \$18 million in annualized revenue, develops electronic or electro-mechanical controls and electronic assemblies. Their customer profile includes international Fortune 1000 manufacturers of industrial control systems, analytical instruments, measuring and detecting equipment and military, defense and Homeland Security equipment.

Total purchase consideration has been allocated to the tangible assets acquired and liabilities assumed based on their provisionally estimated fair values at the acquisition date. It is possible that acquired assets may additionally include customer relationships and the Beckwood name. The Company was unable at December 31, 2013 to assign provisionally estimated fair values to these potential assets. The Beckwood acquisition has preliminarily resulted in approximately \$13 million of goodwill, which will be adjusted downward or upward based on the final values assigned to all acquired assets and liabilities. The Company believes that any goodwill remaining after the valuations are finalized will primarily relate to strategic fit, resulting synergies and the acquired workforce that this business brings to existing operations. Goodwill associated with this acquisition is not expected to be deductible for tax purposes and has been assigned entirely to the Company's Complex Systems segment.

Included in the Company's Condensed Consolidated Statements of Income for the three and six months ended December 31, 2013 are net sales of approximately \$0.8 million and income before provision from income taxes of approximately \$0.1 million, resulting from the acquisition of Beckwood since December 11, 2013.

The Company incurred legal, professional and other costs related to this acquisition aggregating approximately \$0.1 million. These costs were recognized as selling and administrative expenses in the three months ended December 31, 2013.

### **Acquisition of Aydin Displays, Inc.**

On August 30, 2013, the Company completed the acquisition of certain assets and liabilities of Aydin Displays, Inc. ("Aydin Displays" or "Aydin") in a \$15.0 million all-cash transaction, subject to certain post-closing adjustments and financed through the use of borrowings under the Company's Credit Facility. At December 31, 2013, the Company has recorded additional estimated contingent consideration of accounts receivable of \$0.4 million in relation to a post-closing working capital adjustment, which is expected to be settled during the Company's fiscal 2014 year. Additional acquisition consideration of up to \$6.6 million is contingent upon Aydin attaining certain performance thresholds during the twelve month period following the transaction. The transaction includes an approximate \$1.2 million escrowed holdback which is available to fund the working capital adjustment and potential seller indemnification obligations in relation to the acquisition agreement.

The acquired business, which is part of the Company's DSS segment and which is expected to add \$18 million in annualized revenue, develops enhanced flat panel display and touch-screen solutions with application-critical performance criteria including ruggedization, high resolution, color accuracy, response/refresh times, sunlight readability and other criteria such as magnetic interference and emanations security for the Military & Aerospace and Civil Marine markets. These products are currently specified in the U.S. Navy P8A Poseidon ASW aircraft behind-the-cockpit control center, the command and control centers of many U.S. Navy ships, Federal Aviation Administration air traffic control systems, and cockpit command centers for various civil marine applications. The acquired business will continue to operate as Aydin Displays.

Total purchase consideration has been preliminarily allocated to the tangible assets acquired and liabilities assumed based on their provisionally estimated fair values at the acquisition date. Additional acquisition consideration of up to \$6.6 million is contingent upon Aydin attaining certain performance thresholds. The Company has assigned no fair value to this contingent liability. The Aydin acquisition has preliminarily resulted in approximately \$2 million of goodwill, which is expected to be deductible for tax purposes and has been assigned entirely to the Company's DSS segment. The Company believes goodwill primarily relates to strategic fit, resulting synergies and the acquired workforce that this business brings to existing operations. The provisional fair values of acquired identifiable assets have been determined to be Level 3 under the fair value hierarchy and have been estimated based on projected future cash flows and customer attrition rates, discounted using an estimated weighted average cost of capital. The customer relationships are being amortized using an accelerated methodology over fifteen years. Trade names and trademarks are being amortized using a straight-line methodology over ten years. The unpatented technology is being amortized using an accelerated methodology over seven years. The favorable leasehold is reflected in Other long-term assets on the consolidated balance sheet and is being amortized on a straight-line basis over the five year life of the lease. Amortization related to Aydin unpatented technology and favorable leasehold is reflected within Cost of goods sold on the consolidated statement of income.

Included in the Company's Condensed Consolidated Statements of Income for the three and six months ended December 31, 2013 are net sales of approximately \$4.0 million and \$5.2 million, respectively, and loss before benefit from income taxes of less than \$0.1 million and approximately \$0.1 million, respectively, resulting from the acquisition of Aydin since August 30, 2013.

The Company incurred legal, professional and other costs related to this acquisition aggregating approximately \$0.0 million and \$0.2 million for the three and six months ended December 31, 2013, respectively. These costs were recognized as selling and administrative expenses.

A portion of Aydin's revenue is derived from contracts to manufacture video displays and other related products to a buyer's specification under long-term contracts. Revenue and profit is recognized under these contracts using the percentage of completion method based on units shipped to estimated total costs at completion. Certain upfront engineering costs in relation to long-term contracts are capitalized and amortized over the life of the contract.

## Consolidated Results of Operations

Presented below is comparative data and discussions regarding our consolidated results of operations for the three and six months ended December 31, 2013 compared to the three and six months ended December 31, 2012. Results of operations for any period less than one year are not necessarily indicative of results of operations that may be expected for a full year. The following discussion should be read in conjunction with the Unaudited Condensed Consolidated Financial Statements and Notes thereto included in Item 1 of this report.

### *For the Three Months Ended December 31, 2013 compared to the Three Months Ended December 31, 2012*

The following table presents selected consolidated statement of income data for the three months ended December 31, 2013 and 2012 (in thousands):

	2013		2012	
	Total	% of Sales	Total	% of Sales
Net sales	\$ 84,562	100.0 %	\$ 67,254	100.0 %
Cost of goods sold	69,585	82.3	55,159	82.0
Gross profit	14,977	17.7	12,095	18.0
Selling and administrative expenses	8,687	10.3	7,375	11.0
Internal research and development expenses	402	0.5	243	0.4
Amortization of intangible assets	636	0.7	273	0.4
Restructuring charges	—	—	—	—
Other operating (income) expense, net	(5)	—	4	—
Operating income	5,257	6.2	4,200	6.2
Total other expense, net	(37)	—	(91)	(0.1)
Income before provision for income taxes	5,220	6.2	4,109	6.1
Provision for (benefit from) income taxes	1,736	2.1	(732)	(1.1)
Net income	\$ 3,484	4.1 %	\$ 4,841	7.2 %

The following table presents net sales for the three months ended December 31, 2013 and 2012 (in thousands):

SEGMENT	2013		2012		% Change
	Total	% of Total	Total	% of Total	
Medical	\$ 44,316	52.4 %	\$ 34,804	51.8 %	27.3 %
CS	18,304	21.6	14,059	20.9	30.2
DSS	26,078	30.8	22,677	33.7	15.0
Eliminations	(4,136)	(4.8)	(4,286)	(6.4)	(3.5)
Totals	\$ 84,562	100.0 %	\$ 67,254	100.0 %	25.7

The following table presents gross profit and gross profit as a percent of net sales for the three months ended December 31, 2013 and 2012 (in thousands):

SEGMENT	2013		2012	
	Total	GP%	Total	GP%
Medical	\$ 6,824	15.4%	\$ 4,344	12.5%
CS	1,944	10.6	1,428	10.2
DSS	6,209	23.8	6,323	27.9
Totals	\$ 14,977	17.7	\$ 12,095	18.0

The following table presents operating income and operating income as a percent of net sales for the three months ended December 31, 2013 and 2012 (in thousands):

SEGMENT	2013		2012	
	Total	% of Sales	Total	% of Sales
Medical	\$ 3,663	8.3%	\$ 1,803	5.2%
CS	1,019	5.6	777	5.5
DSS	3,590	13.8	4,830	21.3
Other unallocated	(3,015)	—	(3,210)	—
Totals	\$ 5,257	6.2	\$ 4,200	6.2

### *Medical*

Included in the results for the Company's Medical segment for the three months ended December 31, 2013 are net sales of approximately \$13.1 million resulting from the acquisition of Onyx compared to \$6.1 million in net sales from the acquisition of Onyx in the prior year quarter. Excluding the \$7.0 million from the incremental sales from the acquisition of Onyx, legacy Medical sales increased approximately \$2.5 million, or 9%, in the three months ended December 31, 2013 as compared with the prior year quarter. Reflected within this increase in legacy sales is \$4.4 million of increased sales to three customers, including this business unit's largest customer, reflecting relative demand for these customers' products. Offsetting these increases were decreased sales to one customer totaling \$1.6 million, reflecting a supplier issue this customer is having with a subcomponent of their product unrelated to that supplied by the Company. Fenwal Blood Technologies contributed 18% and 20% of consolidated company net sales during the three months ended December 31, 2013 and 2012, respectively. Medical backlog was approximately \$70.1 million at December 31, 2013 compared to \$67.4 at December 31, 2012. Commercial orders, in general, may be rescheduled or cancelled without significant penalty, and, as a result, may not be a meaningful measure of future sales. A majority of the December 31, 2013 Medical backlog is currently expected to be realized in the next 12 months.

Gross profit varies from period to period and can be affected by a number of factors, including product mix, production efficiencies, capacity utilization, and costs associated with new program introduction. The gross profit percentage on Medical sales increased to 15.4% from 12.5% for the three months ended December 31, 2013 and 2012, respectively. This increase in margin percentage on Medical sales primarily reflects certain favorable product mix between the two periods, partially offset by the impact of increased depreciation at the Onyx facility.

Selling and administrative expenses relating to the Medical segment were \$2.6 million and \$2.3 million for the three months ended December 31, 2013 and 2012, respectively. The current year quarter includes \$0.6 million of incremental direct and allocated incremental expenses related to Onyx operations.

Amortization of intangible assets was \$0.6 million and \$0.3 million for the three months ended December 31, 2013 and 2012, respectively. The increase relates to amortization of customer relationships and non-compete agreements acquired as part of the Onyx transaction.

### *Complex Systems*

Included in the results for the Company's Complex Systems segment for the three months ended December 31, 2013 are net sales of approximately \$3.1 million resulting from the acquisitions of Creonix, LLC ("Creonix") and Beckwood. Excluding these sales and a decrease in intercompany sales of \$0.1 million, CS sales to legacy external customers for the three months ended December 31, 2013 increased \$1.3 million, or 13%, as compared with the same quarter last year, primarily reflecting \$2.4 million of increased sales to three customers, reflecting relative increased demand for each of these customers' products. Partially offsetting these increases was decreased sales of \$0.9 million to one customer reflecting this customer's disengagement during fiscal 2014. CS intercompany sales result primarily from the production of circuit boards that are then utilized in DSS product sales. These intercompany sales are eliminated in consolidation. CS backlog was approximately \$42.8 million at December 31, 2013 compared to \$35.1 million at December 31, 2012. Commercial orders, in general, may be rescheduled or cancelled without significant penalty, and, as a result, may not be a meaningful measure of future sales. A majority of the December 31, 2013 CS backlog is currently expected to be realized in the next 12 months.

The gross profit percentage on CS sales increased to 10.6% for the three months ended December 31, 2013 compared to 10.2% for the three months ended December 31, 2012, primarily reflecting increased capacity utilization, partially offset by unfavorable product mix between the comparative periods.

Selling and administrative expenses relating to the CS segment were \$0.9 million and \$0.7 million for the three months ended December 31, 2013 and 2012, respectively, primarily due to the inclusion of operating expenses of Creonix and Beckwood.

There were no additional restructuring charges related to the CS segment for the three months ended December 31, 2013. For a further discussion of this restructuring activity see Note 15, Restructuring Activities, of the "Notes to Unaudited Consolidated Financial Statements" in this Quarterly Report on Form 10-Q.

### ***Defense and Security Systems***

Included in the results for the Company's Defense and Security Systems segment for the three months ended December 31, 2013 are net sales of approximately \$4.0 million resulting from the acquisition of Aydin. Excluding the fiscal year 2014 incremental sales from the acquisition of Aydin, DSS legacy sales decreased approximately \$0.6 million, or 3%, in the three months ended December 31, 2013 as compared with the same quarter last year, reflecting decreased sonobuoy sales to foreign governments, partially offset by increased U.S. Navy sonobuoy sales. Total sales to the U.S. Navy in the three months ended December 30, 2013 and 2012 was approximately \$17.2 million and \$12.8 million, or 20% and 19%, respectively, of consolidated Company net sales for those periods. Sonobuoy sales to foreign governments were \$4.3 million and \$9.1 million in the three months ended December 31, 2013 and 2012, respectively. DSS backlog was approximately \$78.8 million at December 31, 2013 compared to \$109.0 million at December 31, 2012. A majority of the December 31, 2013 DSS backlog is currently expected to be realized in the next 14 months.

The gross profit percentage on DSS sales decreased to 23.8% for the three months ended December 31, 2013 compared to 27.9% for the three months ended December 31, 2012. Gross profit percentage was negatively affected in the current year quarter by decreased foreign sonobuoy sales as compared to the prior year quarter.

Selling and administrative expenses relating to the DSS segment were \$2.1 million and \$1.2 million for the three months ended December 31, 2013 and 2012, respectively, reflecting incremental expenses related to Aydin operations.

Internal research and development expenses reflect costs incurred for the internal development of technologies for use in navigation, oil and gas exploration and flat panel display technology. These costs include salaries and related expenses, contract labor and consulting costs, materials and the cost of certain research and development specific equipment. The Company incurred \$0.4 million and \$0.2 million of internally funded research and development expenses in the three months ended December 31, 2013 and 2012, respectively.

### ***Other Unallocated***

Total corporate selling and administrative expenses were \$5.2 million and \$5.0 million for the three months ended December 30, 2013 and 2012, respectively, or 6.2% and 7.5% of consolidated sales, respectively, reflecting relative economies of scale achieved due to the Company's growth between the two comparative quarters. Of these costs, \$2.2 million and \$1.8 million, respectively, were allocated to segment operations in each of these periods. Allocations of corporate selling and administrative expenses are based on the nature of the service provided and can fluctuate from period to period.

Interest expense consists of interest and fees on the Company's outstanding debt and revolving credit facility, including amortization of financing costs. Interest expense was \$0.2 million for each of the three months ended December 31, 2013 and 2012. See Note 7, Debt, of the "Notes to Unaudited Condensed Consolidated Financial Statements" in this Quarterly Report on Form 10-Q for a further discussion of debt.

The Company recognized an income tax provision of approximately \$1.7 million, or approximately 33.3% of income before provision for income taxes, for the three months ended December 31, 2013. During the three months ended December 31, 2012, the Company recognized a \$2.1 million income tax benefit with respect to the Company's investments in a Canadian subsidiary that held the Company's Canadian operations until these operations were ceased during fiscal 2009. Excluding this discrete tax benefit, the Company recognized an income tax provision of approximately \$1.4 million, or approximately 32.7% of income before provision for income taxes, for the three months ended December 31, 2012. See Note 9, Income Taxes, of the "Notes to Unaudited Condensed Consolidated Financial Statements" in this Quarterly Report on Form 10-Q for a further discussion of income taxes.

Due to the factors described above, the Company reported net income of \$3.5 million (\$0.34 per share, basic and diluted) for the three months ended December 31, 2013, compared to net income of \$4.8 million (\$0.47 per share, basic and diluted) for the corresponding quarter last year.





**For the Six Months Ended December 31, 2013 compared to the Six Months Ended December 31, 2012**

The following table presents selected consolidated statement of income data for the six months ended December 31, 2013 and 2012 (in thousands):

	2013		2012	
	Total	% of Sales	Total	% of Sales
Net sales	\$ 158,760	100.0 %	\$ 118,055	100.0 %
Cost of goods sold	131,589	82.9	97,960	83.0
Gross profit	27,171	17.1	20,095	17.0
Selling and administrative expenses	16,332	10.3	12,847	10.9
Internal research and development expenses	791	0.5	548	0.5
Amortization of intangible assets	1,234	0.8	375	0.3
Restructuring charges	188	0.1	—	—
Other operating expense, net	(8)	—	(6)	—
Operating income	8,634	5.4	6,331	5.3
Total other income, net	(21)	—	(34)	—
Income before provision for income taxes	8,613	5.4	6,297	5.3
Provision for (benefit from) income taxes	2,843	1.8	(1)	—
Net income	\$ 5,770	3.6 %	\$ 6,298	5.3 %

The following table presents net sales for the six months ended December 31, 2013 and 2012 (in thousands):

SEGMENT	2013		2012		% Change
	Total	% of Total	Total	% of Total	
Medical	\$ 86,324	54.4 %	\$ 62,863	53.2 %	37.3 %
CS	36,569	23.0	26,406	22.4	38.5
DSS	43,971	27.7	37,664	31.9	16.7
Eliminations	(8,104)	(5.1)	(8,878)	(7.5)	(8.7)
Totals	\$ 158,760	100.0 %	\$ 118,055	100.0 %	34.5

The following table presents gross profit and gross profit as a percent of net sales for the six months ended December 31, 2013 and 2012 (in thousands):

SEGMENT	2013		2012	
	Total	GP%	Total	GP%
Medical	\$ 13,802	16.0%	\$ 8,538	13.6%
CS	3,812	10.4	2,524	9.6
DSS	9,557	21.7	9,033	24.0
Totals	\$ 27,171	17.1	\$ 20,095	17.0

The following table presents operating income and operating income as a percent of net sales for the six months ended December 31, 2013 and 2012 (in thousands):

SEGMENT	2013		2012	
	Total	% of Sales	Total	% of Sales
Medical	\$ 7,604	8.8%	\$ 4,425	7.0%
CS	1,904	5.2	1,163	4.4
DSS	4,874	11.1	6,155	16.3
Other unallocated	(5,748)	—	(5,412)	—
Totals	\$ 8,634	5.4	\$ 6,331	5.4

### ***Medical***

Included in the results for the Company's Medical segment for the six months ended December 31, 2013 are net sales of approximately \$26.0 million resulting from the acquisition of Onyx compared to \$6.1 million in net sales from the acquisition of Onyx in the prior year period. Excluding the \$19.9 million incremental sales from the acquisition of Onyx, legacy Medical sales increased approximately \$3.5 million, or 6%, in the six months ended December 31, 2013 as compared with the prior year. Reflected within this increase in legacy sales is \$11.5 million of increased sales to five customers, including this business unit's largest customer, reflecting relative demand for these customers' products. Offsetting these increases were decreased sales to three customers totaling \$8.1 million. Decreased sales to one customer reflects relative demand for this customer's products. Decreased sales to the second customer reflects a supplier issue this customer is having with a subcomponent of their product unrelated to that supplied by the Company. Decreased sales to the third customer reflects this customer's decision to insource one of its programs during fiscal 2013. Medical sales are dependent on a small number of key strategic customers. Fenwal Blood Technologies contributed 19% and 21% of consolidated company net sales during the six months ended December 31, 2013 and 2012, respectively.

The gross profit percentage on Medical sales increased to 16.0% from 13.6% for the six months ended December 31, 2013 and 2012, respectively. This increase in margin percentage on Medical sales primarily reflects certain favorable product mix between the two periods, partially offset by the impact of increased depreciation relating to the write-up in value of the Watertown, South Dakota facility assets in connection with the acquisition accounting for Onyx purchase.

Selling and administrative expenses relating to the Medical segment were \$5.1 million and \$3.7 million for the six months ended December 31, 2013 and 2012, respectively. The current year includes \$1.8 million of direct and allocated incremental expenses related to Onyx operations.

Amortization of intangible assets was \$1.2 million and \$0.4 million for the six months ended December 31, 2013 and 2012, respectively. The increase relates to amortization of customer relationships and non-compete agreements acquired as part of the Onyx transaction.

### ***Complex Systems***

Included in the results for the Company's Complex Systems segment for the six months ended December 31, 2013 are net sales of approximately \$0.8 million resulting from the acquisition of Beckwood Services, Inc. ("Beckwood") and \$4.5 million from the acquisition of Creonix, LLC ("Creonix"). Excluding these sales and a decrease in intercompany sales of \$0.8 million, CS sales to legacy external customers for the six months ended December 31, 2013 increased \$5.7 million, or 32%, as compared with the same period last year, primarily reflecting increased sales to four customers, reflecting relative increased demand for each of these customers' products. CS intercompany sales result primarily from the production of circuit boards that are then utilized in DSS product sales. These intercompany sales are eliminated in consolidation.

The gross profit percentage on CS sales increased to 10.4% for the six months ended December 31, 2013 compared to 9.6% for the six months ended December 31, 2012, primarily reflecting increased capacity utilization, partially offset by unfavorable product mix between the comparative periods.

Selling and administrative expenses relating to the CS segment were \$1.7 million and \$1.4 million for the six months ended December 31, 2013 and 2012, respectively., largely due to the inclusion of operating expenses of Creonix and Beckwood.

Restructuring charges related to the CS segment were \$0.2 million for the six months ended December 31, 2013 and relate to the consolidation of the recently acquired Creonix business into the Company's Brooksville, Florida facility. For a further discussion of this restructuring activity see Note 15, Restructuring Activities, of the "Notes to Unaudited Consolidated Financial Statements" in this Quarterly Report on Form 10-Q.

### ***Defense and Security Systems***

Included in the results for the Company's Defense and Security Systems segment for the six months ended December 31, 2013 are net sales of approximately \$5.2 million resulting from the acquisition of Aydin. Excluding the fiscal year 2014 incremental sales from the acquisition of Aydin, DSS legacy sales increased approximately \$1.1 million, or 3%, in the six months ended December 31, 2013 as compared with the period last year, reflecting increased sonobuoy sales to the U. S. Navy, partially offset by decreased sonobuoy sales to foreign governments and lower U.S. Navy engineering sales. Total sales to the U.S. Navy for the six months ended December 31, 2013 and 2012 was approximately \$26.0 million and \$23.2 million, or 16% and 20%, respectively, of consolidated Company net sales for those periods. Sonobuoy sales to foreign governments were \$11.8 million and \$13.5 million in the six months ended December 31, 2013 and 2012, respectively.

The gross profit percentage on DSS sales decreased to 21.7% for the six months ended December 31, 2013 compared to 24.0% for the six months ended December 31, 2012. Gross profit percentage was negatively affected by unfavorable product mix in the current year.

Selling and administrative expenses relating to the DSS segment were \$3.8 million and \$2.3 million for the six months ended December 31, 2013 and 2012, respectively, reflecting incremental expenses related to Aydin operations and increased business development efforts in the current fiscal quarter.

Internal research and development expenses reflect costs incurred for the internal development of technologies for use in navigation, oil and gas exploration and flat panel display technology. These costs include salaries and related expenses, contract labor and consulting costs, materials and the cost of certain research and development specific equipment. The Company incurred \$0.8 million and \$0.5 million of internally funded research and development expenses for the six months ended December 31, 2013 and 2012, respectively.

### ***Other Unallocated***

Total corporate selling and administrative expenses were \$10.1 million and \$9.1 million for the six months ended December 31, 2013 and 2012, respectively, or 6.4% and 7.7% of consolidated sales, respectively, reflecting relative economies of scale achieved due to the Company's growth between the two comparative quarters. Of these costs, \$4.4 million and \$3.7 million, respectively, were allocated to segment operations in each of these periods. Allocations of corporate selling and administrative expenses are based on the nature of the service provided and can fluctuate from period to period.

Interest expense consists of interest and fees on the Company's outstanding debt and revolving credit facility, including amortization of financing costs. Interest expense was \$0.4 million and \$0.3 million for the six months ended December 31, 2013 and 2012, respectively. The comparative interest expense reflects comparative borrowings under the Company's credit facility between the two periods, partially offset by lower facility fees in the current period as compared to the prior year period. See Note 7, Debt, of the "Notes to Unaudited Condensed Consolidated Financial Statements" in this Quarterly Report on Form 10-Q for a further discussion of debt.

The Company recognized an income tax provisions of approximately \$2.9 million, or approximately 33.0% of income before provision for income taxes, for the six months ended December 31, 2013. During the six months ended December 31, 2012, the Company recognized a \$2.1 million income tax benefit with respect to the Company's investments in a Canadian subsidiary that held the Company's Canadian operations until these operations were ceased during fiscal 2009. Excluding this discrete tax benefit, the Company recognized an income tax provision of approximately \$2.1 million, or approximately 32.9%, of income before provision for income taxes, for the six months ended December 31, 2012. See Note 9, Income Taxes, of the "Notes to Unaudited Condensed Consolidated Financial Statements" in this Quarterly Report on Form 10-Q for a further discussion of income taxes.

Due to the factors described above, the Company reported net income of \$5.8 million (\$0.57 per share, basic and diluted) for the six months ended December 30, 2013, compared to net income of \$6.3 million (\$0.62 per share, basic and diluted) for the corresponding period last year.

## Liquidity and Capital Resources

The Company has a \$65 million credit facility with BMO Harris Bank N.A., consisting of a \$35 million revolving line-of-credit facility (the “Revolving Credit”) to support the Company’s working capital needs and other general corporate purposes, and a \$30 million acquisition loan commitment (the “Acquisition Facility” and together with the Revolving Credit, the “Credit Facility”) to finance permitted acquisitions. The Credit Facility expires on November 15, 2017, is secured by substantially all assets of the Company and provides for up to an additional \$35 million in uncommitted loans available for additional Revolving Credit loans or Acquisition loans. As a condition of the Credit Facility, the Company is subject to certain customary covenants, which it was in compliance with at December 31, 2013. The Company had \$25.0 million of borrowings drawn against the Credit Facility at December 31, 2013. The Company also has approximately \$1.5 million of industrial revenue bonds outstanding at December 31, 2013. See Note 7, Debt, of the “Notes to Unaudited Condensed Consolidated Financial Statements” in this Quarterly Report on Form 10-Q for a further discussion of the Company’s debt.

Certain of the Company’s DSS contracts allow for billings to occur when certain milestones under the applicable program are reached, independent of the amount shipped by Sparton as of such date. These performance based billings reduce the amount of cash that would otherwise be required during the performance of these contracts. As of December 31, 2013 and June 30, 2013, \$19.1 million and \$20.9 million, respectively, of proceeds from billings in excess of costs were received.

The Company currently expects to meet its liquidity needs through a combination of sources including, but not limited to, operations, existing cash balances, its revolving line-of-credit and anticipated continuation of performance based billings on certain DSS contracts. With the above sources providing the expected cash flows, the Company currently believes that it will have sufficient liquidity for its anticipated needs over the next 12 months, but no assurances regarding liquidity can be made.

Operating activities provided \$12.5 million and used \$8.9 million of net cash flows in six months ended December 31, 2013 and 2012, respectively. Excluding changes in working capital, operating activities provided \$10.2 million and \$9.8 million in the first six months of fiscal 2014 and 2013, respectively, reflecting the Company’s relative operating performance during those periods. Working capital provided \$2.3 million and used \$18.7 million of net cash flows in the six months ended December 31, 2013 and 2012, respectively. Working capital related cash flows in the first six months of fiscal 2014 primarily reflect decreased receivables and inventory, partially offset by increased other assets, the funding of production related to U.S. Navy contracts during the year in excess of performance based payments received, and decreased accounts payable and accrued expenses. Working capital related cash flows in the six months of fiscal 2013 primarily reflect increased inventory, reduced accounts payable and accrued expenses and funding of production related to U.S. Navy contracts during the year in excess of advance billings received.

Cash flows used in investing activities in six months ended December 31, 2013 and 2012 totaled \$31.5 million and \$45.4 million, respectively. The six months ended December 31, 2013 reflect the \$15.0 million acquisition of Aydin and the \$15.3 million acquisition of Beckwood. Both acquisitions are subject to certain post-closing adjustments. The Aydin acquisition was funded through borrowings under the Company’s Credit Facility. The Beckwood acquisition was funded through a combination of cash on hand and borrowings under the Company’s Credit Facility. The six months ended December 31, 2012 reflect the \$43.25 million paid through that date in relation to the acquisition of Onyx. The six months ended December 31, 2013 additionally reflects the receipt of \$0.1 million in relation to the settlement of the inventory adjustment to the purchase price of Creonix. Net capital expenditures for the six months ended December 31, 2013 and 2012 were approximately \$1.3 million and \$1.6 million, respectively. The six months ended December 31, 2012 reflects the utilization of \$0.5 million as cash collateral for certain letters of credit outstanding issued by PNC Bank, National Association. These letters of credit were issued under the Company’s Credit Facility during the Company’s third quarter of fiscal 2013, eliminating the need for this cash collateral.

Financing activities provided \$14.0 million and \$13.4 million in the six months ended December 31, 2013 and 2012, respectively. The six months ended December 31, 2013 reflect \$15.0 million of net borrowing under the Company’s Credit Facility, \$0.5 million of tax benefits in excess of recorded stock-based compensation and the repurchase of \$0.9 million of the Company’s common stock under Company’s stock repurchase plan (see below for a further discussion of this program). The six months ended December 31, 2013 and 2012 additionally reflect the use of cash of \$0.7 million and \$0.2 million, respectively, to satisfy income tax withholding requirements in relation to the vesting of executives’ restricted stock in exchange for the surrender of a portion of the vesting shares. Each of the six months ended December 31, 2013 and 2012 also reflect repayments on the Company’s outstanding industrial revenue bonds with the state of Ohio of less than \$0.1 million. The six months ended December 31, 2012 additionally reflects the receipt of \$0.1 million from the exercise of stock options and the payment of \$0.4 million of financing fees.

On May 1, 2013, the Company's Board of Directors approved a repurchase by the Company of up to \$3.0 million of shares of its common stock over a 12-month period. The Company has been authorized to purchase shares from time to time in open market, block transactions and privately negotiated transactions at prices deemed appropriate by management, depending on market conditions, applicable laws and other factors. The stock repurchase program does not require the Company to repurchase any specific number of shares and can be modified, extended or terminated by the Board of Directors at any time.

Pursuant to this stock repurchase program, during the six months ended December 31, 2013, the Company purchased 47,119 shares of its common stock at an average price of \$18.51 per share for approximately \$0.9 million. Previously, during the year ended June 30, 2013, the Company purchased 128,158 shares of its common stock at an average price of \$16.55 per share for approximately \$2.1 million. Total shares purchased pursuant to this stock repurchase program total 175,277 at an average price of \$17.08. Shares purchased under the plan were cancelled upon repurchase. As of December 31, 2013, all authorized funds under the stock repurchase program have been expended.

## **Commitments and Contingencies**

### ***Environmental Remediation***

Sparton has been involved with ongoing environmental remediation since the early 1980's related to one of its former manufacturing facilities, located in Albuquerque, New Mexico ("Coors Road"). Although the Company entered into a long-term lease of the Coors Road property that was accounted for as a sale of property during fiscal 2010, it remains responsible for the remediation obligations related to its past operation of this facility. At December 31, 2013, Sparton had accrued approximately \$2.9 million as its estimate of the remaining minimum future undiscounted financial liability with respect to this matter, of which approximately \$0.4 million is classified as a current liability and included on the balance sheet in other accrued expenses. The Company's minimum cost estimate is based upon existing technology and excludes certain legal costs, which are expensed as incurred. The Company's estimate includes equipment and operating and maintenance costs for onsite and offsite pump and treat containment systems, as well as continued onsite and offsite monitoring. It also includes periodic reporting requirements.

In fiscal 2003, Sparton reached an agreement with the United States Department of Energy ("DOE") and others to recover certain remediation costs. Under the settlement terms, Sparton received cash and obtained some degree of risk protection as the DOE agreed to reimburse Sparton for 37.5% of certain future environmental expenses in excess of \$8.4 million incurred from the date of settlement, if any, of which approximately \$4.9 million has been expended as of December 31, 2013 toward the \$8.4 million threshold. Uncertainties associated with environmental remediation contingencies are pervasive and often result in wide ranges of reasonably possible outcomes. Estimates developed in the early stages of remediation can vary significantly. Normally a finite estimate of cost does not become fixed and determinable at a specific point in time. Rather, the costs associated with environmental remediation become estimable over a continuum of events and activities that help to frame and define a liability. Factors which cause uncertainties for the Company include, but are not limited to, the effectiveness of the current work plans in achieving targeted results and proposals of regulatory agencies for desired methods and outcomes. It is possible that cash flows and results of operations could be materially affected by the impact of changes associated with the ultimate resolution of this contingency. At December 31, 2013, the Company estimates that it is reasonably possible, but not probable, that future environmental remediation costs associated with the Company's past operations at the Coors Road property, in excess of amounts already recorded and net of DOE reimbursement, could be up to \$2.4 million before income taxes over the next seventeen years.

The Company and its subsidiaries are also involved in certain existing compliance issues with the EPA and various state agencies, including being named as a potentially responsible party at several sites. Potentially responsible parties ("PRP"s) can be held jointly and severally liable for the clean-up costs at any specific site. The Company's past experience, however, has indicated that when it has contributed relatively small amounts of materials or waste to a specific site relative to other PRPs, its ultimate share of any clean-up costs has been minor. Based upon available information, the Company believes it has contributed only small amounts to those sites in which it is currently viewed as a PRP and that reasonably possible losses related to these compliance issues are immaterial.

### ***Litigation***

On September 24, 2013, L-3 Communications Corporation, doing business as L-3 Linkabit (“Linkabit”) filed a complaint in the United States District Court for the Middle District of Florida, Orlando Division, alleging, among other things, that the Company failed to follow Linkabit drawings for the manufacture and assembly of certain products and that the Company changed its manufacturing process resulting in shipment of defective products to Linkabit. Linkabit seeks damages for breach of contract, breach of covenants, breach of warranties and negligence. In response to the Company's motion to dismiss on January 10, 2014, Linkabit filed its first amended complaint deleting the alleged negligence claims. The Company believes that its defenses to the claims are very strong and it intends to defend this action vigorously. Given the stage of the litigation and the unresolved remaining questions of fact, the Company cannot estimate any loss, or range of loss, with confidence at this time.

### ***U.S. Government Audits***

Federal government agencies, including the Defense Contract Audit Agency (“DCAA”) and the Defense Contract Management Agency (“DCMA”), routinely audit and evaluate government contracts and government contractors’ administrative processes and systems. These agencies review the Company’s performance on contracts, pricing practices, cost structure, financial capability and compliance with applicable laws, regulations and standards. They also review the adequacy of the Company’s internal control systems and policies, including the Company’s purchasing, accounting, estimating, compensation and management information processes and systems.

The Company implemented a new enterprise resource planning system in November 2012 and currently remains eligible to receive cost reimbursable contracts from the U.S. Government. The Company responded in June 2013 to DCAA review comments received in the fourth quarter of fiscal 2013 regarding corrective actions to improve the reliability for accumulating costs under government contracts. While the Company’s corrective actions remain open for further review, the Company remains confident formal resolution of DCAA cost accounting practices findings will not have a material adverse impact on the Company’s financial results.

### ***Other***

In addition to the foregoing, from time to time, the Company is involved in various legal proceedings relating to claims arising in the ordinary course of business. The Company is not currently a party to any other such legal proceedings, the adverse outcome of which, individually or in the aggregate, is expected to have a material adverse effect on our business, financial condition or results of operations.

### **Contractual Obligations and Off-Balance Sheet Arrangements**

Information regarding the Company’s long-term debt obligations, environmental liability payments, operating lease payments, and other commitments is provided in Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” of the Company’s Annual Report on Form 10-K for the fiscal year ended June 30, 2013. As of June 30, 2013, there were \$13.6 million of debt and a liability related to performance based billings on customer contracts of \$20.9 million. As of December 31, 2013, debt increased to \$26.3 million and the liability related to performance based billings has decreased to \$19.1 million. Other than as noted above, there have been no material changes in the nature or amount of the Company’s contractual obligations since June 30, 2013.

### **Critical Accounting Policies**

Our financial statements are prepared in conformity with GAAP and require us to select appropriate accounting policies. The assumptions and judgments we use in applying our accounting policies have a significant impact on our reported amounts of assets, liabilities, revenue and expenses. While we believe that the assumptions and judgments used in our estimates are reasonable, actual results may differ from these estimates under different assumptions or conditions.

We have identified the most critical accounting policies upon which our financial status depends. The critical policies were determined by considering accounting policies that involve the most complex or subjective decisions or assessments. We also have other policies considered key accounting policies; however, these policies do not meet the definition of critical accounting policies because they do not generally require us to make estimates or judgments that are complex or subjective. Our critical accounting policies include the following:

- Business combinations
- Goodwill and intangible assets

- Government contract cost estimates
- Environmental contingencies
- Income taxes
- Commercial inventory valuation
- Allowance for probable losses on receivables
- Valuation of property, plant and equipment
- Stock-based compensation
- Pension obligations

There have been no significant changes to our critical accounting policies that are described in Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” section of our Annual Report on Form 10-K for the year ended June 30, 2013.

#### **New Accounting Pronouncements**

See Note 17, New Accounting Standards, of the “Notes to Unaudited Condensed Consolidated Financial Statements” in this Quarterly Report on Form 10-Q for a discussion of new accounting pronouncements.

#### **Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

The Company manufactures its products in the United States and Vietnam. Sales of the Company’s products are in the U.S. and foreign markets. The Company is subject to foreign currency exchange rate risk relating to intercompany activity and balances and to receipts from customers and payments to suppliers in foreign currencies. Adjustments related to the remeasurement of the Company’s Vietnamese financial statements into U.S. dollars are included in current earnings. As a result, the Company’s financial results could be affected by factors such as changes in foreign currency exchange rates or economic conditions in the domestic and foreign markets in which the Company operates. However, minimal third party receivables and payables are denominated in foreign currency and the related market risk exposure is considered to be immaterial.

The Company’s revolving credit line, when drawn upon, is subject to future interest rate fluctuations which could potentially have a negative impact on cash flows of the Company. The Company had \$25.0 million outstanding under its Credit Facility at December 31, 2013. A prospective increase of 100 basis points in the interest rate applicable to the Company’s outstanding borrowings under its Credit Facility would result in an increase of approximately \$0.3 million in our annual interest expense. The Company is not party to any currency exchange or interest rate protection agreements as of December 31, 2013.

#### **Item 4. Controls and Procedures.**

Each of our Chief Executive Officer and Chief Financial Officer has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934) as of the end of the period covered by this quarterly report. Based on such evaluation, such officers have concluded that, as of the end of the period covered by this quarterly report, our disclosure controls and procedures are effective.

There have been no changes in our internal controls over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended December 31, 2013 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

## **PART II. OTHER INFORMATION**

#### **Item 1. Legal Proceedings.**

See “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Commitments and Contingencies” of this report.

In addition to the above, from time to time, we are involved in various legal proceedings relating to claims arising in the ordinary course of business. We are not currently a party to any such legal proceedings, the outcome of which, individually or in the aggregate, is expected to have a material adverse effect on our business, financial condition or results of operations.



**Item 1A. Risk Factors.**

You should carefully consider the risks and uncertainties described in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended June 30, 2013 and the other information in our subsequent filings with the SEC, including this Quarterly Report on Form 10-Q. Our business, financial condition, results of operations and stock price could be materially adversely affected by any of these risks. The risks described in our Annual Report on Form 10-K are not the only ones we face. Additional risks and uncertainties that are currently unknown to us or that we currently consider to be immaterial may also impair our business or adversely affect our financial condition, results of operations and stock price.

**Item 5. Other Information**

On January 29, 2014, the Company adopted a form of indemnification agreement to be entered into with each of its directors and officers. Under the terms of the agreement, consistent with the provisions of the Company's Code of Regulations and applicable law, the Company agrees to indemnify each director and officer, to the fullest extent permitted by Ohio law, from claims and losses arising from their service as an officer or director, as applicable. Subject to certain procedures outlined in the agreement, the Company is required to advance expenses incurred as a result of any such proceeding as to which an officer or director could be indemnified. The agreement provides for procedures for the determination of a person's right to receive indemnification consistent with Ohio law. The Company anticipates it will enter into substantially similar agreements with any new directors and officers. The form of indemnification agreement is attached hereto as Exhibit 10.\_\_\_\_ and incorporated by reference herein. The foregoing summary of the indemnification agreement is qualified in its entirety by the text of the Exhibit.

**Item 6. Exhibits.**

Exhibit Number	Description
3.1	Second Amended Articles of Incorporation of the Registrant, incorporated herein by reference from the Registrant's Proxy Statement on Form DEF 14A filed with the SEC on September 21, 2010.
3.2	Amended and Restated Code of Regulations of the Registrant, incorporated herein by reference from the Registrant's Proxy Statement on Form DEF 14A filed with the SEC on September 21, 2010.
3.3	Amendment to Amended and Restated Code of Regulations of the Registrant, incorporated herein by reference from exhibit 99.1 to the Registrant's Current Report on Form 8-K filed with the SEC on May 9, 2011.
3.4	Amendment to Amended and Restated Code of Regulations of the Registrant, incorporated herein by reference from exhibit 99.1 to the Registrant's Current Report on Form 8-K filed with the SEC on May 7, 2012.
3.5	Amendment to Amended and Restated Code of Regulations of the Registrant, incorporated herein by reference from exhibit 99.1 to the Registrant's Current Report on Form 8-K filed with the SEC on October 26, 2012.
10.1*	Form of Director and Officer Indemnification Agreement.
18.1	Preferability Letter from Independent Registered Public Accounting Firm Regarding Change in Accounting Principle, incorporated herein by reference from the Registrant's Quarterly Report on Form 10-Q filed with the SEC on November 5, 2013.
31.1*	Chief Executive Officer certification under Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Chief Financial Officer certification under Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Chief Executive Officer and Chief Financial Officer certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document

\* Filed herewith.

**SIGNATURES**

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

Sparton Corporation

Date: February 3, 2014

By: /s/ CARY B. WOOD

Cary B. Wood  
President and Chief Executive Officer  
(Principal Executive Officer)

Date: February 3, 2014

By: /s/ MARK SCHLEI

Mark Schlei  
Senior Vice President and Chief Financial Officer  
(Principal Financial Officer)

## DIRECTOR AND OFFICER INDEMNIFICATION AGREEMENT

This Director and Officer Indemnification Agreement, dated as of \_\_\_\_\_, 2014 (this "**Agreement**"), is made by and between Sparton Corporation, an Ohio corporation (the "Company") and (the "**Indemnitee**"), a director and/or officer of the Company.

### RECITALS

A. The Indemnitee has agreed to serve or is currently serving as a director and/or officer of the Company, and the Company desires that the Indemnitee continue serving in such capacity. The Indemnitee is willing, subject to certain conditions, including the execution and performance of this Agreement by the Company, to continue serving in such capacity.

B. In addition to the indemnification to which the Indemnitee is entitled under the Code of Regulations of the Company, as may be amended (the "**Regulations**"), the Company has obtained, at its sole expense, insurance protecting the Company and its officers and directors, including the Indemnitee, against certain losses arising out of any threatened, pending or completed action, suit, or proceeding to which such persons may be made or are threatened to be made parties.

NOW, THEREFORE, in order to induce the Indemnitee to serve or continue to serve in his current capacity, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Company and the Indemnitee agree as follows:

1. CONTINUED SERVICE

The Indemnitee shall serve or continue to serve as a director and/or officer of the Company so long as he is duly elected or appointed in accordance with the Regulations or until he resigns in writing or is removed from office in accordance with applicable law.

2. INITIAL INDEMNITY

(a) The Company shall indemnify the Indemnitee if or when he is a party or is threatened to be made a party to any threatened, pending or completed action, suit, proceeding or claim, whether civil, criminal, administrative or investigative (other than an action by or in the right of the Company), by reason of the fact that he is or was a director and/or officer of the Company or is or was serving at the request of the Company as a director, trustee, officer, employee, member, manager or agent of another corporation, domestic or foreign, nonprofit or for profit, a limited liability company, or a partnership, joint venture, trust or other enterprise, or by reason of any action alleged to have been taken or omitted in any such capacity, against any and all costs, charges, expenses (including fees and expenses of attorneys or others; all such costs, charges and expenses being herein jointly referred to as "**Expenses**"), judgments, fines and amounts paid in settlement actually incurred by the Indemnitee in connection therewith, including any appeal of or from any judgment or decision, (i) in the case of an Indemnitee who is a director of the Company, unless it is proved by clear and convincing evidence in a court of competent jurisdiction that the Indemnitee's action or failure to act involved an act or omission undertaken with deliberate intent to cause injury to the Company or undertaken with reckless disregard for the best interests of the Company and (ii) in the case of an Indemnitee who is an officer of the Company but not a director of the Company, if the Indemnitee acted in good faith and in a manner which he reasonably believed to be in or not opposed to the best interests of the Company. In addition,

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with respect to any criminal action or proceeding, indemnification hereunder shall be made only if the Indemnitee had no reasonable cause to believe his conduct was unlawful. The termination of any action, suit, proceeding or claim by judgment, order, settlement or conviction, or upon a plea of nolo contendere or its equivalent, shall not, of itself, create a presumption that the Indemnitee did not satisfy the foregoing applicable standard of conduct.

(b) The Company shall indemnify the Indemnitee if or when he is a party or is threatened to be made a party, to any threatened, pending or completed action, suit, proceeding or claim by or in the right of the Company to procure a judgment in its favor, by reason of the fact that the Indemnitee is or was a director and/or officer of the Company or is or was serving at the request of the Company as a director, trustee, officer, employee, member, manager or agent of another corporation, domestic or foreign, nonprofit or for profit, a limited liability company, or a partnership, joint venture, trust or other enterprise, or by reason of any action alleged to have been taken or omitted in any such capacity, against any and all Expenses, judgments, fines and amounts paid in settlement actually incurred by the Indemnitee in connection therewith, including any appeal of or from any judgment or decision, (i) in the case of an Indemnitee who is a director of the Company, unless it is proved by clear and convincing evidence in a court of competent jurisdiction that the Indemnitee's action or failure to act involved an act or omission undertaken with deliberate intent to cause injury to the Company or undertaken with reckless disregard for the best interests of the Company and (ii) in the case of an Indemnitee who is an officer of the Company but not a director of the Company, if the Indemnitee acted in good faith and in a manner which he reasonably believed to be in or not opposed to the best interests of the Company. Notwithstanding the foregoing provisions of this Section 2(b), no indemnification pursuant to this Section 2(b) shall be made (A) in the case of an Indemnitee who is an officer but not a director of the Company, in respect of any claim, issue or matter as to which the Indemnitee is adjudged to be liable for negligence or misconduct in the performance of his duty to the Company unless, and only to the extent that, the court of common pleas or other court in which such action, suit, proceeding or claim was brought determines, notwithstanding any adjudication of liability, that in view of all the circumstances of the case the Indemnitee is fairly and reasonably entitled to indemnity for such Expenses, judgments, fines and amounts paid in settlement as such court of common pleas or other court shall deem proper, or (B) in the case of an Indemnitee who is a director of the Company, in respect of any action, suit, proceeding or claim in which the only liability asserted against the Indemnitee is pursuant to Section 1701.95 of the Ohio Revised Code (the "**ORC**").

(c) Any indemnification under Section 2(a) or 2(b) hereof (unless ordered by a court) shall be made by the Company only upon a determination relating to a specific case that indemnification of the Indemnitee is proper in the circumstances because he has met the applicable standard of conduct set forth in Section 2(a) or 2(b) hereof. Such determination shall be made (i) by the Board of Directors of the Company (the "**Board**") by a majority vote or consent of a quorum consisting of Directors who were not and are not parties to or threatened with such action, suit, proceeding or claim, or (ii) if such a quorum of disinterested Directors is not available or if a majority of such quorum so directs, in a written opinion by independent legal counsel (designated for such purpose by the Board) who shall not be an attorney, or a firm having associated with it an attorney, who has been retained by or who has performed services for the Company, or any person to be indemnified, within the five years preceding such determination, or (iii) by the shareholders of the Company (the "**Shareholders**"), or (iv) by the court of common pleas or other court in which such action, suit, proceeding or claim was brought. Any determination made by the disinterested directors or by independent legal counsel under this Section 2(c) shall be promptly communicated to the person who threatened or brought the action or suit by or in the right of the corporation under Section 2(b) hereof, and, within ten days after receipt of that notification, the person shall have the right to petition the court of common pleas or the court in which the action or suit was brought to review the reasonableness of that determination.

(d) To the extent that the Indemnitee has been successful on the merits or otherwise, including the dismissal of an action without prejudice, in defense of any action, suit, proceeding or claim referred to

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in Section 2(a) or 2(b) hereof, or in defense of any claim, issue or matter therein, he shall be indemnified against Expenses actually incurred by him in connection therewith.

(e) Expenses actually incurred by the Indemnitee in defending any action, suit, proceeding or claim referred to in Section 2(a) or 2(b) hereof, or in defense of any claim, issue or matter therein, shall be paid by the Company as they are incurred in advance of the final disposition of such action, suit, proceeding or claim under the procedure set forth in Section 6(b) hereof.

(f) For purposes of this Agreement, references to "**other enterprises**" shall include employee benefit plans; references to "**fin**es" shall include any excise taxes assessed on the Indemnitee with respect to any employee benefit plan; references to "**serv**ing at the request of the Company" shall include any service as a director, officer, employee, member, manager or agent of the Company which imposes duties on, or involves services by, the Indemnitee with respect to an employee benefit plan, its participants or beneficiaries; references to the masculine shall include the feminine; references to the singular shall include the plural and vice versa; and the word including is used by way of illustration only and not by way of limitation.

(g) No amendment to the Second Amended Articles of Incorporation of the Company (the "**Articles**") may deny, diminish or encumber the Indemnitee's rights to indemnity pursuant to the Regulations, the ORC or any other applicable law as applied to any act or failure to act occurring in whole or in part prior to the date (the "**Effective Date**") upon which the amendment was approved by the shareholders of the Company. In the event that the Company shall purport to adopt any amendment to its Articles or Regulations or take any other action the effect of which is to deny, diminish or encumber the Indemnitee's rights to indemnity pursuant to the Articles, the Regulations, the ORC or any such other law, such amendment shall apply only to acts or failures to act occurring entirely after the Effective Date thereof.

### 3. ADDITIONAL INDEMNIFICATION

(a) Pursuant to Section 1701.13(E)(6) of the ORC, without limiting any right which the Indemnitee may have pursuant to Section 2 hereof or any other provision of this Agreement or the Articles, the Regulations, the ORC, any policy of insurance or otherwise, but subject to any limitation on the maximum permissible indemnity which may exist under applicable law at the time of any request for indemnity hereunder and subject to the following provisions of this Section 3, the Company shall indemnify the Indemnitee against any amount which he is or becomes obligated to pay relating to or arising out of any claim made against him because of any act, failure to act or neglect or breach of duty, including any actual or alleged error, misstatement or misleading statement, that he commits, suffers, permits or acquiesces in while acting in his capacity as a director of the Company. The payments which the Company is obligated to make pursuant to this Section 3 shall include any and all Expenses, judgments, fines and amounts paid in settlement, actually incurred by the Indemnitee in connection therewith including any appeal of or from any judgment or decision; provided, however, that the Company shall not be obligated under this Section 3 to make any payment in connection with any claim against the Indemnitee:

- (i) to the extent of any fine or similar governmental imposition which the Company is prohibited by applicable law from paying (as determined by final order of a court of competent jurisdiction); or
- (ii) to the extent based upon or attributable to the Indemnitee having actually realized a personal profit to which he was not legally entitled, including profit (A) from the purchase and sale by the Indemnitee of equity securities of the Company which are recoverable by the Company pursuant to Section 16(b) of the Securities Exchange Act of 1934 or (B) arising from transactions in publicly traded securities of the Company which were effected by the Indemnitee in violation of Section 10(b) of the Securities Exchange Act of 1934 or Rule 10b-5 promulgated thereunder.

(b) A determination as to whether the Indemnitee shall be entitled to indemnification under this Section 3 shall be made in accordance with Section 6(a) hereof. Expenses incurred by the Indemnitee in defending any claim to which this Section 3 applies shall be paid by the Company as they are actually and

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reasonably incurred in advance of the final disposition of such claim under the procedure set forth in Section 6(b) hereof.

4. ADDITIONAL RIGHTS

The rights to indemnification provided by this Agreement shall not be exclusive of any other rights of indemnification to which the Indemnitee may be entitled under the Articles, the Regulations, the ORC or any other statute, any insurance policy, other agreement or vote of shareholders or directors or otherwise, as to any actions or failures to act by the Indemnitee, and shall continue after he has ceased to be a director, officer, employee or agent of the Company or other entity for which his service gives rise to a right hereunder, and shall inure to the benefit of his heirs, executors and administrators. For the avoidance of doubt, limitations on indemnification under any such other agreement or right will not affect the parties' relative rights hereunder.

5. PARTIAL INDEMNITY

If Indemnitee is entitled under any provision of this Agreement to indemnification by the Company for some or a portion of the Expenses actually or reasonably incurred by him in the investigation, defense, appeal or settlement of any proceeding, but not for all of the total amount thereof, the Company shall nevertheless indemnify the Indemnitee for the portion thereof to which Indemnitee is entitled.

6. CERTAIN PROCEDURES RELATING TO INDEMNIFICATION

(a) For purposes of pursuing his rights to indemnification under Section 3 hereof, the Indemnitee shall (i) submit to the Board a sworn statement of request for indemnification substantially in the form of Exhibit 1 attached hereto and made a part hereof (the "Indemnification Statement") averring that he is entitled to indemnification hereunder and (ii) present to the Company evidence in reasonable detail of all amounts for which indemnification is requested. Submission of an Indemnification Statement to the Board shall create a presumption that the Indemnitee is entitled to indemnification hereunder, and the Company shall, within 30 calendar days after submission of the Indemnification Statement, make the payments requested in the Indemnification Statement to or for the benefit of the Indemnitee, unless (A) within such 30-calendar-day period by the vote or consent of a majority of the Directors, even if less than a quorum, shall determine that the Indemnitee is not entitled to indemnification under Section 3 hereof, (B) such vote shall be based upon clear and convincing evidence sufficient to rebut the foregoing presumption, and (C) the Company shall notify the Indemnitee within such period of such vote, which notice shall disclose with particularity the evidence upon which the vote is based. The foregoing notice shall be sworn to by all persons who participated in the vote and voted to deny indemnification. The provisions of this Section 6(a) are intended to be procedural only and shall not affect the right of Indemnitee to indemnification under Section 3 hereof so long as Indemnitee follows the prescribed procedure, and any determination by a majority of the Directors that the Indemnitee is not entitled to indemnification and any failure to make the payments requested in the Indemnification Statement shall be subject to *de novo* judicial review by any court of competent jurisdiction.

(b) For purposes of obtaining payments of Expenses in advance of final disposition pursuant to Section 2(e) hereof or the last sentence of Section 3(b) hereof, the Indemnitee shall submit to the Company a sworn request for advancement of Expenses substantially in the form of Exhibit 2 attached hereto and made a part hereof (the "**Undertaking**"), averring that he has incurred or in good faith expects to incur actual Expenses in defending an action, suit, proceeding or claim referred to in Section 2(a) or 2(b) hereof or any claim referred to in Section 3 hereof, or pursuant to Section 11 hereof. Unless determined in a final order of a court of competent jurisdiction to be prohibited from payment at the time of the Indemnitee's act or omission at issue, or unless the only liability asserted against the Indemnitee in the subject action, suit, proceeding or claim is pursuant to ORC Section 1701.95, the Indemnitee shall be eligible to execute Part A of the Undertaking by which he undertakes to: (i) (A) in the case of an Indemnitee who is a director of the Company, repay such

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amount if it is proved by clear and convincing evidence in a court of competent jurisdiction that the Indemnitee's action or failure to act involved an act or omission undertaken with deliberate intent to cause injury to the Company or undertaken with reckless disregard for the best interests of the Company and (B) in the case of an Indemnitee who is an officer of the Company but not a director of the Company, repay such amount if (x) with respect to any action, suit, proceeding or claim (other than an action by or in the right of the Company) brought against the Indemnitee by reason of the fact that the Indemnitee is or was an officer of the Company for which the Indemnitee has received advancement of Expenses, it is determined that the Indemnitee did not act in good faith and in a manner which he reasonably believed to be in or not opposed to the best interests of the Company or (y) with respect to any action, suit, proceeding or claim brought against the Indemnitee by or in the right of the Company for which the Indemnitee has received advancement of Expenses, the Indemnitee is adjudged to be liable for negligence or for misconduct in the performance of his duty to the Company and the court has not determined that Indemnitee is entitled to indemnification and (ii) reasonably cooperate, at the Company's sole cost and expense, with the Company concerning the action, suit, proceeding or claim. In all cases, the Indemnitee shall be eligible to execute Part B of the Undertaking by which he undertakes to repay such amount if it ultimately is determined by a final order of a court of competent jurisdiction that he is not entitled to be indemnified by the Company under this Agreement or otherwise. In the event that the Indemnitee is eligible to and does execute both Part A and Part B of the Undertaking, the Expenses which are paid by the Company pursuant thereto shall be required to be repaid by the Indemnitee only if he is required to do so under the terms of both Part A and Part B of the Undertaking. Upon receipt of the Undertaking, the Company shall thereafter promptly pay such Expenses of the Indemnitee as are noticed to the Company in reasonable detail arising out of the matter described in the Undertaking. No security shall be required in connection with any Undertaking.

7. LIMITATION ON INDEMNITY

Notwithstanding anything contained herein to the contrary, the Company shall not be required hereby to indemnify the Indemnitee with respect to any action, suit, proceeding or claim that was initiated by the Indemnitee unless (i) such action, suit, proceeding or claim was initiated by the Indemnitee to enforce any rights to indemnification arising hereunder and such person shall have been formally adjudged to be entitled to indemnity by reason hereof, (ii) authorized by another agreement to which the Company is a party whether heretofore or hereafter entered, or (iii) otherwise ordered by the court in which the suit was brought.

8. SUBROGATION; DUPLICATION OF PAYMENTS

(a) In the event of payment under this Agreement, the Company shall be subrogated to the extent of such payment to all of the rights of recovery of Indemnitee, who shall execute all papers required and shall do everything that may be necessary to secure such rights, including the execution of such documents necessary to enable the Company effectively to bring suit to enforce such rights; provided, however, that such subrogation shall be subject to the Company executing an instrument in writing satisfactory to the Indemnitee in his discretion under which the Company agrees to fully indemnify, defend and hold harmless the Indemnitee from any Expense or other liability that may arise therein or therefrom.

(b) The Company shall not be liable under this Agreement to make any payment in connection with any claim made against Indemnitee to the extent Indemnitee has actually received payment (under any insurance policy, the Regulations or otherwise) of the amounts otherwise payable hereunder without any reservation of rights or other claim for potential disgorgement thereof, as determined by the Indemnitee in good faith.

9. DEFENSE OF CLAIMS; NOTICE

(a) The Company shall be entitled to participate in the defense of any threatened or pending action, suit, proceeding or claim in respect of which the Indemnitee requests indemnification hereunder or to assume the defense thereof, with counsel reasonably satisfactory to the Indemnitee; provided that if the Indemnitee believes, after consultation with counsel selected by the Indemnitee, that (i) the use of counsel

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chosen by the Company to represent the Indemnitee would present such counsel with an actual or potential conflict, (ii) the named parties in any such action, suit, proceeding or claim (including any impleaded parties) include both the Company and the Indemnitee and the Indemnitee shall conclude that there may be one or more legal defenses available to him that are different from or in addition to those available to the Company, (iii) any such representation by such counsel would be precluded under the applicable standards of professional conduct then prevailing or (iv) any such representation could be reasonably expected to increase Indemnitee's risk of liability, then the Indemnitee shall be entitled to retain separate counsel (but not more than one law firm plus, if applicable, local counsel in respect of any particular action, suit, proceeding or claim) at the Company's expense. The Company shall not, without the prior written consent of the Indemnitee, effect any settlement of any threatened or pending action, suit, proceeding or claim to which the Indemnitee is, or could have been, a party unless such settlement solely involves the payment of money and includes a complete and unconditional release of the Indemnitee from all liability on any claims that are the subject matter of such action, suit, proceeding or claim. The Indemnitee shall not unreasonably withhold its consent to any proposed settlement; provided that the Indemnitee may withhold consent to any settlement that does not provide a complete and unconditional release of the Indemnitee. Indemnitee shall not make any admission or effect any settlement without the Company's written consent unless Indemnitee shall have determined to undertake his/her own defense in such matter and has waived the benefits of this Agreement.

(b) Indemnitee shall provide to the Company prompt written notice of any proceeding brought, threatened, asserted or commenced against Indemnitee with respect to which Indemnitee may assert a right to indemnification hereunder; provided that failure to provide such notice shall not, in any way, limit Indemnitee's rights under this Agreement

10. LIABILITY INSURANCE

For the duration of the Indemnitee's service as a director and/or officer of the Company, and thereafter for so long as the Indemnitee shall be subject to any pending or possible action, suit, proceeding or claim of the type described in Section 2 hereof or any pending or possible claim of the type described in Section 3 hereof, the Company shall cause to be maintained in effect policies of directors' and officers' liability insurance providing coverage for directors and/or officers of the Company that is at least substantially comparable in scope and amount to that provided by the Company's current policies of directors' and officers' liability insurance. The Company shall provide, upon request, the Indemnitee with a copy of all directors' and officers' liability insurance applications, binders, policies, declarations, endorsements and other related materials, and shall provide the Indemnitee with a reasonable opportunity to review and comment on the same. In all policies of directors' and officers' liability insurance obtained by the Company, the Indemnitee shall be named as an insured in such a manner as to provide the Indemnitee the same rights and benefits, subject to the same limitations, as are accorded to the Company's directors and officers most favorably insured by such policy.

11. FEES AND EXPENSES OF ENFORCEMENT

It is the intent of the Company that the Indemnitee not be required to incur the expenses associated with the enforcement of his rights under this Agreement by litigation or other legal action because the cost and expense thereof would substantially detract from the benefits intended to be extended to the Indemnitee hereunder. Accordingly, if it should appear to the Indemnitee that the Company has failed to comply with any of its obligations under this Agreement or in the event that the Company or any other person initiates any litigation or other legal action to declare this Agreement void or unenforceable or to deny to, or to recover from, the Indemnitee the benefits intended to be provided to the Indemnitee hereunder, the Company irrevocably authorizes the Indemnitee from time to time to retain counsel of his choice, at the expense of the Company as hereafter provided, to represent the Indemnitee in connection with the initiation and prosecution by the Indemnitee of any litigation or other legal action to enforce his rights under this Agreement or in connection with the defense by the Indemnitee of any litigation or other legal action initiated by the Company

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or any other person to declare this Agreement void or unenforceable or to deny to, or to recover from, the Indemnitee the benefits intended to be provided to the Indemnitee hereunder. Regardless of the outcome thereof, the Company shall pay and be solely responsible for any and all costs, charges, and expenses, including fees and expenses of attorneys and others, reasonably incurred by the Indemnitee in connection with any litigation or other legal action referred to in the immediately preceding sentence of this Section 11. In addition, the Company shall pay and be solely responsible for the fees and expenses of any Independent Counsel.

12. MERGER OR CONSOLIDATION

In the event that the Company shall be a constituent corporation in a consolidation, merger, or other reorganization, the Company, if it shall not be the surviving, resulting, or acquiring corporation therein, shall require as a condition thereto that the surviving, resulting, or acquiring corporation agree to assume all of the obligations of the Company hereunder and to indemnify the Indemnitee to the full extent provided herein. Whether or not the Company is the resulting, surviving, or acquiring corporation in any such transaction, the Indemnitee shall stand in the same position under this Agreement with respect to the resulting, surviving, or acquiring corporation as he would have with respect to the Company if its separate existence had continued.

13. SEVERABILITY

If any provision of this Agreement or the application of any provision hereof to any person or circumstances is held invalid, unenforceable or otherwise illegal, the remainder of this Agreement and the application of such provision to other persons or circumstances shall not be affected, and the provision so held to be invalid, unenforceable or otherwise illegal shall be reformed to the extent (and only to the extent) necessary to make it enforceable, valid and legal.

14. NON-TRANSFERRABILITY; SUCCESSORS

Except as provided in Section 4 hereof, the rights to indemnification provided by this Agreement are personal to Indemnitee and are non-transferable by Indemnitee, and no party other than the Indemnitee is entitled to indemnification under this Agreement.

15. SECURITY

To ensure that the Company's obligations pursuant to this Agreement can be enforced by Indemnitee, the Company may, at its option, establish a trust pursuant to which the Company's obligations pursuant to this Agreement and other similar agreements can be funded.

16. NOTICES

All notices and other communications hereunder shall be in writing and shall be personally delivered or sent by recognized overnight courier service (a) if to the Company, to the then-current principal executive offices of the Company (Attention: General Counsel) or (b) if to the Indemnitee, to the last known address of Indemnitee as reflected in the Company's records. Either party may change its address for the delivery of notices or other communications hereunder by providing notice to the other party as provided in this Section 16. All notices shall be effective upon actual delivery by the methods specified in this Section 16.

17. GOVERNING LAW

This Agreement shall be governed by and construed in accordance with the laws of the State of Ohio, without giving effect to the principles of conflict of laws thereof.

18. MODIFICATION

This Agreement and the rights and duties of the Indemnitee and the Company hereunder may be modified only by an instrument in writing signed by both parties hereto.

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19. COUNTERPARTS

This Agreement may be executed in any number of counterparts and each of such counterparts will for all purposes be deemed to be an original, and all counterparts together will constitute but one and the same instrument.

[Signature Page Follows]

IN WITNESS WHEREOF, the parties hereto have duly executed this Agreement as of the date first above written.

**SPARTON CORPORATION**

By:  
Name:  
Title:

[Signature of Indemnitee]

Exhibit 1

INDEMNIFICATION STATEMENT

STATE OF \_\_\_\_\_ )  
 ) ss  
COUNTY OF \_\_\_\_\_ )

I, \_\_\_\_\_, being first duly sworn, do depose and say as follows:

20. This Indemnification Statement is submitted pursuant to the Indemnification Agreement, dated \_\_\_\_\_, 20\_\_ , between Sparton Corporation, an Ohio corporation (the "**Company**"), and the undersigned.

21. I am requesting indemnification against costs, charges, expenses (which may include fees and expenses of attorneys and/or others), judgments, fines and amounts paid in settlement (collectively, "**Liabilities**"), which have been actually and reasonably incurred by me in connection with a claim referred to in Section 3 of the aforesaid Indemnification Agreement.

22. With respect to all matters related to any such claim, I am entitled to be indemnified as herein contemplated pursuant to the aforesaid Indemnification Agreement.

23. Without limiting any other rights which I have or may have, I am requesting indemnification against Liabilities which have or may arise out of

[Signature of Indemnitee]



Subscribed and sworn to before me, a Notary Public in and for said County and State, this \_\_\_\_ day of \_\_\_\_\_, 20\_\_.

[Seal]

My commission expires the \_\_\_\_ day of \_\_\_\_\_, 20\_\_.

13

Exhibit 2

UNDERTAKING

STATE OF \_\_\_\_\_ )  
 ) ss  
COUNTY OF \_\_\_\_\_ )

I, \_\_\_\_\_, being first duly sworn, do depose and say as follows:

24. This Undertaking is submitted pursuant to the Indemnification Agreement, dated \_\_\_\_\_, 20\_\_, between Sparton Corporation an Ohio corporation (the **“Company”**) and the undersigned.

25. I am requesting payment of costs, charges and expenses which I have reasonably incurred or will reasonably incur in defending an action, suit, proceeding or claim, referred to in Section 2(a) or 2(b) or any claim referred to in Section 3, or pursuant to Section 11, of the aforesaid Indemnification Agreement.

26. The costs, charges, and expenses for which payment is requested are, in general, all expenses related to

27. **Part A** The Indemnitee shall not be eligible to execute Part A of this Undertaking if, at the time of the Indemnitee’s act or omission at issue, the Articles of Incorporation, as may be amended, or the Code of Regulations, as may be amended, of the Company prohibit such advances by specific reference to the Ohio Revised Code (the **“ORC”**) Section 1701.13(E)(5)(a), or if the only liability asserted against the Indemnitee is in an action, suit, proceeding or claim on the Company’s behalf pursuant to ORC Section 1701.95. In the event that the Indemnitee is eligible to and does execute both Part A and Part B hereof, the costs, charges and expenses which are paid by the Company pursuant hereto shall be required to be repaid by the Indemnitee only if he is required to do so under the terms of both Part A and Part B hereof.

**If the Indemnitee is going to be both a director and officer, then use both of the following paragraphs.**

**[Use only this paragraph if the Indemnitee is only a director of the Company]** With respect to any claim for indemnification related to my position as a Director for which I received an advancement of

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Expenses, I hereby undertake to (a) repay all amounts paid pursuant hereto if it is proved by clear and convincing evidence in a court of competent jurisdiction that my action or failure to act which is the subject of the matter described herein involved an act or omission undertaken with deliberate intent to cause injury to the Company or undertaken with reckless disregard for the best interests of the Company and (b) reasonably cooperate, at the Company's sole cost and expense, with the Company concerning the action, suit, proceeding or claim.

**[Use only this paragraph if the Indemnitee is only an officer of the Company but not a director of the Company]**

With respect to any claim for indemnification related to my position as an officer for which I received an advancement of Expenses, I hereby undertake to (a) repay all amounts paid pursuant hereto (i) with respect to any action, suit, proceeding (other than an action by or in the right of the Company) brought against me by reason of the fact that I am or was an officer of the Company for which I received advancement of Expenses, it is determined that I did not act in good faith and in a manner which I reasonably believed to be in or not opposed to the best interests of the Company or (ii) with respect to any action, suit, proceeding or claim brought against me by or in the right of the Company for which I received advancement of Expenses, I am adjudged to be liable for negligence or for misconduct in the performance of my duty to the Company and the court has not determined that I am entitled to indemnification and (b) reasonably cooperate, at the Company's sole cost and expense, with the Company concerning the action, suit, proceeding or claim.

[Signature of Indemnitee]

4. Part B

I hereby undertake to repay all amounts paid pursuant hereto if it ultimately is determined that I am not entitled to be indemnified by the Company under the aforesaid Indemnification Agreement or otherwise.

[Signature of Indemnitee]

Subscribed and sworn to before me, a Notary Public in and for said County and State, this \_\_\_\_ day of \_\_\_\_\_, 20\_\_.

[Seal]

My commission expires the \_\_\_\_ day of \_\_\_\_\_, 20\_\_.

**CERTIFICATION UNDER SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Cary B. Wood, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Sparton Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 3, 2014

/s/ CARY B. WOOD

Cary B. Wood, President and Chief Executive Officer

**CERTIFICATION UNDER SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Mark Schlei, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Sparton Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 3, 2014

/s/ MARK SCHLEI

Mark Schlei, Senior Vice President and Chief Financial Officer

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Sparton Corporation (the "Company") on Form 10-Q for the period ended December 31, 2013, as filed with the Securities and Exchange Commission on the date hereof (the "Periodic Report"), we, Cary B. Wood, President and Chief Executive Officer of the Company, and Mark Schlei, Senior Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- 1 The Periodic Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- 2 The information contained in the Periodic Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: February 3, 2014

/s/ CARY B. WOOD

Cary B. Wood, President and Chief Executive  
Officer

Date: February 3, 2014

/s/ MARK SCHLEI

Mark Schlei, Senior Vice President and Chief  
Financial Officer



