HEI, INC.

Victoria, MN

FINANCIAL STATEMENTS

Including Independent Auditors' Report

December 31, 2011 and January 1, 2011

HEI, Inc.
2011 Annual Report

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INDEPENDENT AUDITORS' REPORT

To the Shareholders, Audit Committee and Board of Directors
HEI, Inc.
Victoria, MN

We have audited the accompanying balance sheets of HEI, Inc. as of December 31, 2011 and January 1, 2011 and the related statements of operations, changes in shareholders' equity and cash flows for the fiscal years ended December 31, 2011, January 1, 2011 and January 2, 2010. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of HEI, Inc. as of December 31, 2011 and January 1, 2011 and the results of its operations and cash flows for the fiscal years ended December 31, 2011, January 1, 2011 and January 2, 2010 in conformity with accounting principles generally accepted in the United States of America.

Baker Tilly Virchow Krause, LLP

Minneapolis, Minnesota
February 24, 2012

an independent member of
BAKER TILLY
INTERNATIONAL

HEI, INC.
BALANCE SHEETS

	December 31, 2011	January 1, 2011
	(In thousands, except share and per share data)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ -	$ -
Accounts receivable, net of allowance for doubtful accounts of $35 and $53, respectively	5,489	5,071
Inventories, net	4,680	4,359
Deferred income taxes	447	425
Other current assets	253	227
Total current assets	10,869	10,082
Property and equipment:		
Land	216	216
Building and improvements	4,337	4,337
Fixtures and equipment	26,676	25,334
Accumulated depreciation and amortization	(25,788)	(24,290)
Property and equipment, net	5,441	5,597
Security deposit	230	230
Other long-term assets	328	336
Total assets	$ 16,868	$ 16,245
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 2,151	$ 2,737
Accrued liabilities	701	718
Customer deposit liabilities	11	297
Current maturities of long-term liabilities	927	684
Total current liabilities	3,790	4,436
Long-term liabilities:		
Deferred income taxes	447	425
Other long-term liabilities, less current maturities	2,443	1,953
Long-term debt, less current maturities	5,933	6,431
Total long-term liabilities, less current maturities	8,823	8,809
Total liabilities	12,613	13,245
Commitments and contingencies		
Shareholders' equity:		
Undesignated stock; 5,000,000 shares authorized; none issued	-	-
Convertible preferred stock, $.05 par; 167,000 shares authorized; 32,000 shares issued and outstanding; liquidation preference at $26 per share (total liquidation preference $832)	2	2
Common stock, $.05 par; 20,000,000 shares authorized; 11,155,023 issued and 10,120,023 outstanding shares at December 31, 2011; 10,970,516 issued and 9,870,516 outstanding at January 1, 2011	506	494
Additional paid-in capital	28,433	28,241
Accumulated deficit	(24,686)	(25,737)
Total shareholders' equity	4,255	3,000
Total liabilities and shareholders' equity	$ 16,868	$ 16,245

The accompanying notes are an integral part of these financial statements

HEI, INC.
STATEMENTS OF OPERATIONS

	Fiscal Years Ended		
	December 31, 2011	**January 1, 2011**	**January 2, 2010**
	(In thousands, except share and per share data)		
Net sales	$ 37,415	$ 36,420	$ 31,530
Cost of sales	31,003	31,124	26,116
Gross profit	6,412	5,296	5,414
Operating expenses:			
Selling, general and administrative	4,454	4,934	5,692
Research, development and engineering	583	612	805
Operating income (loss)	1,375	(250)	(1,083)
Interest expense, net	(364)	(286)	(445)
Other income (expense), net	40	167	(30)
Income (loss) before income taxes	1,051	(369)	(1,558)
Income tax expense	-	-	-
Net income (loss)	$ 1,051	$ (369)	$ (1,558)
Income (loss) per common share:			
Basic	$ 0.11	$ (0.04)	$ (0.16)
Diluted	$ 0.10	$ (0.04)	$ (0.16)
Weighted average common shares outstanding:			
Basic	9,979,516	9,766,000	9,699,000
Diluted	10,290,885	9,766,000	9,699,000

The accompanying notes are an integral part of these financial statements

HEI, INC.
STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Convertible Preferred Stock Shares Outstanding	Convertible Preferred Stock	Common Stock Shares Outstanding	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Total Shareholders' Equity
			(In thousands except share data)				
Balance January 3, 2009	32,000	$ 2	9,629,610	$ 482	$ 27,955	$ (23,810)	$ 4,629
Net loss	-	-	-	-	-	(1,558)	(1,558)
Stock-based compensation expense	-	-	-	-	145	-	145
Issuance of common shares under stock benefit plans and option plans	-	-	90,816	4	(4)	-	-
Balance January 2, 2010	32,000	2	9,720,426	486	28,096	(25,368)	3,216
Net loss	-	-	-	-	-	(369)	(369)
Stock-based compensation expense	-	-	-	-	153	-	153
Issuance of common shares under stock benefit plans and option plans	-	-	150,090	8	(8)	-	-
Balance January 1, 2011	32,000	2	9,870,516	494	28,241	(25,737)	3,000
Net income	-	-	-	-	-	1,051	1,051
Stock-based compensation expense	-	-	-	-	204	-	204
Issuance of common shares under stock benefit plans and option plans	-	-	249,507	12	(12)	-	-
Balance December 31, 2011	32,000	$ 2	10,120,023	$ 506	$ 28,433	$ (24,686)	$ 4,255

The accompanying notes are an integral part of these financial statements

HEI, INC.
STATEMENTS OF CASH FLOWS

	Fiscal Years Ended		
	December 31, 2011	**January 1, 2011**	**January 2, 2010**
		(In thousands)	
Cash flow from operating activities:			
Net income (loss)	$ 1,051	$ (369)	$ (1,558)
Adjustments to reconcile net income (loss) to cash flow from operating activities:			
Depreciation and amortization	1,613	1,817	2,005
Change in allowance for doubtful accounts	(18)	(77)	53
(Gain) loss on disposal of property and equipment	(3)	(19)	43
Stock-based compensation expense	204	153	145
Changes in operating assets and liabilities:			
Accounts receivable	(401)	(1,428)	1,067
Inventories	(321)	(1,407)	522
Other current assets	(17)	219	308
Accounts payable	(586)	987	316
Accrued liabilities	(17)	(208)	(382)
Customer deposit liabilities	(286)	69	155
Net cash flow provided by (used in) operating activities	**1,219**	**(263)**	**2,674**
Cash flow from investing activities:			
Additions to property and equipment	(1,194)	(1,614)	(560)
Proceeds from the sale of assets	20	-	5
Additions to patents	(29)	(29)	(38)
Net cash flow used in investing activities	**(1,203)**	**(1,643)**	**(593)**
Cash flow from financing activities:			
Payment of debt issuance costs	-	(23)	(51)
Repayment of long-term debt	(812)	(608)	(1,910)
Proceeds from long-term debt	784	716	2,029
Proceeds (repayments) of long-term debt - revolving line of credit, net	12	1,821	(2,156)
Net cash flow provided by (used in) financing activities	**(16)**	**1,906**	**(2,088)**
Net decrease in cash and cash equivalents	-	-	(7)
Cash and cash equivalents, beginning of year	-	-	7
Cash and cash equivalents, end of year	$ -	$ -	$ -
Supplemental disclosures of cash flow information:			
Interest paid	$ 331	$ 309	$ 446
Taxes paid	-	-	-
Supplemental disclosures of non-cash financing and investing activities:			
Issuance of common stock for vested restricted stock awards	$ 12	$ 8	$ 4
Security deposits utilized towards buy-out of capital leases	-	-	298
Capital lease assets acquired	252	-	63

The accompanying notes are an integral part of these financial statements

Note 1

Business

HEI, Inc. is referred to herein as "HEI," the "Company," "us," "we" or "our," unless the context indicates otherwise. We operate three facilities in North America in support of our globally based customers. We provide contract manufacturing solutions to customers through our flex and rigid-flex substrate and microelectronic assembly capabilities and our medical design and development and box build services. Our primary markets are medical, telecommunications, industrial, military and aerospace. We support our customers' products from initial product development and design through transitional and full-scale serial manufacturing to worldwide distribution and aftermarket support.

Fiscal Years

HEI uses a 4-4-5 week accounting cycle with the Fiscal year ending on the Saturday closest to December 31. As a result, our Fiscal year 2011 ended on December 31, 2011, Fiscal year 2010 ended on January 1, 2011 and Fiscal year 2009 ended on January 2, 2010. All three Fiscal years include 52 weeks.

Summary of Significant Accounting Policies

Financial Statements and Notes. These financial statements include the accounts of the Company with all significant intra-company transactions and balances eliminated. All dollar amounts in these financial statements and notes are presented in thousands, except for share and per share information or unless otherwise noted.

Revenue Recognition. Revenue for manufacturing and assembly is recognized upon shipment to the customer which represents the point at which the risks and rewards of ownership have been transferred to the customer.

Our design and development contracts are typically discrete time and materials projects that may or may not involve separately priced deliverables. Development contract revenue is recognized ratably as development activities occur based on contractual per hour and material reimbursement rates. Development contracts are an interactive process with customers as different design and functionality is contemplated during the design phase. Upon reaching the contractual billing maximums, we defer revenue until contract extensions or purchase orders are received from customers. We occasionally have contractual arrangements in which part or all of the payment or billing is contingent upon achieving milestones or customer acceptance. For those contracts we evaluate whether the contract should be accounted using the completed contract method if the term of the arrangement is short-term or using the percentage of completion method for longer-term contracts.

The Company periodically collects taxes from customers to be remitted to governmental authorities. The Company's policy is to present taxes imposed on revenue-producing transactions on a net basis (excluded from revenues).

Cash and Cash Equivalents. The Company is operating under a revolving line of credit which funds our cash needs on a daily basis. We do not maintain cash balances as part of this arrangement. If the Company were to maintain cash on hand, we would consider investments in highly liquid debt instruments with original maturities of three months or less at the date of purchase to be cash equivalents.

Accounts Receivable. The Company periodically reviews customers' payment and credit history as part of extending unsecured credit and establishes an allowance for doubtful accounts based upon factors surrounding the credit risk of specific customers and other information. Credit risk on accounts receivable is minimized as a result of the diverse nature of the Company's customer base. Invoices are generally due 30 to 90 days after shipment. Accounts receivable that extend past their due date are considered past due. The Company does not accrue interest on past due accounts receivable. Receivables are written off only after all collection attempts have failed and are based on individual credit evaluation and specific circumstances of the customer. Accounts receivable are shown net of an allowance for doubtful accounts of $35 and $53 at December 31, 2011 and January 1, 2011, respectively. The Company decreased the allowance for doubtful accounts by $18 and $77 in Fiscal 2011 and 2010, respectively, and increased it by $53 in Fiscal 2009.

Inventories. Inventories are stated at the lower of cost or market and include materials, labor and overhead costs. Cost is determined using the first-in, first-out method (FIFO). A large portion of the inventory is purchased based upon forecasts and customer purchase orders. If there is a contractual arrangement with the customer the excess or obsolete inventory is the customers' responsibility.

Inventory reserves of $287 and $221 at December 31, 2011 and January 1, 2011, respectively, are established for excess and slow-moving inventory, which are netted against the inventory balances shown in the financial statements.

Inventories consisted of the following:

	December 31, 2011	January 1, 2011
Inventories:		
Purchased parts	$ 3,464	$ 3,379
Work in process	600	672
Finished goods	616	308
Total	$ 4,680	$ 4,359

Property and Equipment. Property and equipment are stated at cost. Depreciation and amortization are provided on the straight-line method over the estimated useful lives of the property and equipment. The approximate useful lives of building and improvements are 10-39 years and fixtures and equipment are 3-10 years. Depreciation expense on property and equipment and amortization expense on equipment under capital leases, was $1.6 million , $1.7 million and $1.8 million for Fiscal 2011, 2010 and 2009, respectively.

Maintenance and repairs are charged to expense as incurred. Major improvements and tooling costs are capitalized and depreciated using the straight-line method over their estimated useful lives. The cost and accumulated depreciation of property and equipment retired or otherwise disposed of is removed from the related accounts, and any resulting gain or loss is credited or charged to operations.

Patents. External costs associated with patents are capitalized and amortized over 84 months or the remaining useful life of the patent, whichever is shorter. Amortization expense related to patents was $27, $26 and $85 for Fiscal 2011, 2010 and 2009, respectively. The book value of the patents (which are classified as other long-term assets) is as follows:

	December 31, 2011	January 1, 2011
Original Cost	$ 764	$ 709
Accumulated amortization	(684)	(657)
Total	$ 80	$ 52

Amortization expense related to patents for the next five years is estimated to be:

Fiscal Years	Amortization Expense
2012	$ 26
2013	16
2014	16
2015	16
2016	6
Total	$ 80

Leases. Assets under capital lease obligations are depreciated in accordance with our normal depreciation policy for owned assets or over the lease term, if shorter, and the related charge to operations is included in depreciation expense.

Certain leases include rent increases during the initial lease term. For these leases, we recognize the related rental expense on a straight-line basis over the term of the lease and record the difference between the expense charged to operations and amounts paid as a deferred rent liability.

Impairment of Long-lived and Intangible Assets. Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Determination of recoverability is based on the Company's judgment and estimates of undiscounted future cash flows resulting from the use of the assets and their eventual disposition. Measurement of an impairment loss for long-lived assets and certain identifiable intangible assets that management expects to hold and use is based on the fair value of the assets. The carrying values of assets determined to be impaired are reduced to their estimated fair values. Fair values of any impaired assets would generally be determined using a market or income approach.

Intangible assets are stated at fair value as of the date acquired less accumulated amortization. Amortization is calculated on a straight-line basis or another method that more fairly represents the utilization of the assets. The future economic benefit of the carrying values of intangible assets that are subject to amortization are tested for recoverability whenever events or changes in circumstances indicate the carrying value of an intangible asset may not be recoverable based on undiscounted cash flows or market factors, and an impairment loss would be recorded in the period so determined. There were no asset impairments in Fiscal 2011, 2010 or 2009.

Research, Development and Engineering. The Company expenses all research, development and engineering costs as incurred.

Shipping and Handling. The Company includes shipping and handling revenue in net sales and shipping and handling costs in cost of sales.

Advertising. Advertising costs are charged to expense as incurred. Advertising costs were $29, $73 and $41 for Fiscal 2011, 2010 and 2009, respectively, and are included in selling, general and administrative expense.

Income Taxes. The income tax expense or benefit is computed on the basis of the various tax jurisdictions' income or loss before income taxes. Deferred income taxes reflect the tax effects of differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The Company uses judgment and assumptions to determine if valuation allowances for deferred income tax assets are required if realization is not likely by considering future market growth, forecasted operations, future taxable income, and the mix of earnings in the tax jurisdictions in which it operates.

The Company considers income taxes in each of the tax jurisdictions in which it operates in order to determine its effective income tax rate. Current income tax exposure is identified and temporary differences resulting from differing treatments of items for tax and financial reporting purposes are assessed. These differences result in deferred tax assets and liabilities, which are included in the Company's balance sheets. We assess the likelihood that our deferred tax assets will be recovered from future taxable income and record a valuation allowance to reduce our deferred tax assets to the amounts we believe to be realizable. Accordingly, the income tax expense in the statements of operations is impacted by changes in the valuation allowance. Significant management estimates and judgment are required in determining any valuation allowance recorded against net deferred tax assets. The Company accounts for uncertain tax positions by recording a liability for unrecognized tax benefits resulting from uncertain tax positions taken, or expected to be taken, in its tax returns.

Stock-Based Compensation. The Company offers share-based compensation programs to its employees and non-employee directors that provide for equity awards which have included restricted stock and stock options. The Company recognizes expense for all stock-based awards with graded vesting on a straight-line basis over the vesting period of the entire award based on the fair value on the date of grant, net of an estimated forfeiture rate. The expected term of stock-based awards and forfeiture rate assumptions are derived from historical data.

The value of restricted stock awards is determined by the market price of the stock on the date of the grant. Stock-based compensation expense related to restricted stock awards was $204, $150 and $136 for Fiscal 2011, 2010 and 2009, respectively. As of December 31, 2011, 1,035,000 shares of restricted stock remain unvested. There were 284,500 and 746,000 restricted stock shares granted in Fiscal 2011 and 2010, respectively, and no restricted stock grants in Fiscal 2009. See Note 7, *Stock Benefit Plans*, for assumptions used to determine the fair value of restricted stock awards.

The Company calculates the fair value of stock-based option awards on the date of the grant using the Black-Scholes option pricing model. The Company did not grant any stock options in Fiscal 2011, 2010 or 2009. As of December 31, 2011, 247,000 stock options are outstanding. Stock-based compensation expense related to option awards were $3 and $9 in Fiscal 2010 and 2009, respectively. As of December 31, 2011 and January 1, 2011, all stock-based compensation expense related to option awards have been fully recognized in the statements of operations.

Stock-based compensation expense for the next five years related to outstanding restricted stock awards as of December 31, 2011 is estimated to be:

Fiscal Years	Stock-based Compensation Expense
2012	$ 215
2013	178
2014	119
2015	80
2016	34
Total	$ 626

Customer Deposits. Customer deposits result from cash received in advance of manufacturing or design and development services being performed.

Income (Loss) Per Common Share. Basic income (loss) per share ("EPS") is computed by dividing net income or loss by the weighted average number of common shares outstanding during each period. Diluted income per share is computed by dividing net income by the weighted average number of common shares outstanding assuming the exercise of convertible preferred stock, restricted stock, dilutive stock options and warrants. The dilutive effect of the stock options, restricted stock and warrants is computed using the average market price of the Company's stock during each period under the treasury stock method. During periods of loss, convertible preferred stock, options, restricted stock and warrants are not dilutive and are thus excluded from the calculation.

Use of Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ significantly from those estimates.

Financial Instruments. The fair value of accounts receivable and accounts payable approximate their carrying value due to the short-term nature of these instruments. The fair market values of the Company's borrowings and other long-term liabilities outstanding approximate their carrying values based upon current market rates of interest.

Recently Adopted Accounting Pronouncements

Multi Deliverable Revenue Arrangements. At the beginning of our 2011 Fiscal year, we adopted the new guidance in ASC Topic 605, "Revenue Recognition", relating to the accounting for revenue arrangements involving multiple deliverables. The updates require companies to allocate revenue in arrangements involving multiple deliverables based on the estimated selling price of each deliverable, even though such deliverables are not sold separately either by the company itself or other vendors. This guidance eliminates the requirement that all undelivered elements must have objective and reliable evidence of fair value before a company can recognize the portion of the overall arrangement fee that is attributable to items that already have been delivered. The adoption of this standard did not materially impact our results of operations or financial condition.

Note 2

Liquidity and Capital Resources

	Fiscal Years Ended		
	December 31, 2011	January 1, 2011	January 2, 2010
Net cash provided by (used in) operating activites	$ 1,219	$ (263)	$ 2,674
Net cash used in investing activites	(1,203)	(1,643)	(593)
Net cash provided by (used in) financing activites	(16)	1,906	(2,088)
Net decrease in cash and cash equivalents	$ -	$ -	$ (7)

The Company's working capital was $7.0 million (current ratio of 2.9 to 1.0) at the end of Fiscal 2011 as compared to $5.6 million (current ratio of 2.3 to 1.0) at the end of Fiscal 2010. This increase in working capital resulted from the use of our cash flows from operations to, in part, pay down current liabilities. The reduction in current liabilities was partially offset by increases in accounts receivable and inventories as our sales volume increased in the last half of the year.

Cash provided by operating activities was $1.2 million for Fiscal 2011 as compared to cash used in operating activities of $0.3 million for Fiscal 2010 and cash provided by operating activities of $2.7 million in Fiscal 2009.

Cash used in investing activities in Fiscal 2011 was $1.2 million as compared to $1.6 million in Fiscal 2010, primarily due to capital expenditures. Capital expenditures in Fiscal 2011 primarily relate to equipment for our Victoria, Minnesota and Tempe, Arizona operations to improve capacity and capabilities. Capital expenditures for the 2011, 2010 and 2009 Fiscal years were $1.2 million, $1.6 million and $0.6 million, respectively. The Company expects capital expenditure payments for Fiscal 2012 to be approximately $1.5 million to $2.5 million, primarily related to investment in new technology, increased capabilities and increased capacity for our Tempe, Arizona operations.

Cash used in financing activities was $16 in Fiscal 2011 as compared to $1.9 million in Fiscal 2010. Financing activities in Fiscal 2011 was primarily comprised of $0.8 million of proceeds from equipment financing, offset by term loan payments.

We generated net income for Fiscal 2011 of $1.1 million compared to a net loss for Fiscal 2010 of $0.4 million and a net loss for Fiscal 2009 of $1.6 million. Throughout the past three Fiscal years, we have adjusted and realigned many of our costs to the extent possible and have begun to realize returns on these efforts. Although sales have grown at a modest rate in the last year, our continued pursuit of new customers and new programs have added new customers at all three of our operating sites and provided strong momentum going into Fiscal 2012.

Cash Requirements

The Company's cash requirements in Fiscal 2012 will be primarily to fund operations, including capital spending and debt service. The Company believes that cash generated from operations and amounts available under its credit facility will be sufficient to meet its cash requirements for the next 12 months. The Company regularly reviews the availability and terms on which it might issue additional equity or debt securities in the public or private markets. However, the Company cannot assure that additional sources of financing would be available to the Company on commercially favorable terms should the Company's capital requirements exceed its cash available from operations and cash available under its credit facility.

Note 3

Warranty Obligations

Sales of our products are subject to limited warranty guarantees that typically extend for a period of between 90 days and 12 months from the date of manufacture. The Company offers extended warranty coverage on certain products it manufactures. If an extended warranty is purchased by a customer the Company recognizes revenue over the life of the warranty period and records the estimated warranty expense over the same period. Warranty terms are included in customer contracts under which we are obligated to repair, replace or refund the purchase price of any components or assemblies our customers deem defective due to workmanship or materials. We do, however, reserve the right to reject warranty claims where we determine that failure is due to normal wear, customer modifications, improper maintenance or misuse. Warranty provisions are based on estimated returns and warranty expenses applied to current period revenue and historical warranty incidence over the preceding 12-month period. Both the return rate and the warranty liability are evaluated on an ongoing basis for adequacy. The following is a roll-forward of the Company’s product warranty accrual for each of the past three Fiscal periods:

Fiscal Years	Balance at Beginning of Year	Provision and Accrual Adjustments	Claims	Balance at End of Year
2011	$ 14	$ 92	$ (78)	$ 28
2010	22	(8)	-	14
2009	31	(9)	-	22

Note 4

Long-Term Debt

Our long-term debt consists of the following:

	December 31, 2011		January 1, 2011	
	Principal Balance	Interest Rate	Principal Balance	Interest Rate
Wells Fargo Business Credit revolving line of credit	$ 3,942	4.58%	$ 3,931	4.30%
Wells Fargo Business Credit equipment term loan	1,589	4.84%	n/a	n/a
Wells Fargo Business Credit mortgage	1,140	5.08%	1,230	4.80%
Wells Fargo Business Credit term loan #1	-	-	96	4.55%
Wells Fargo Business Credit term loan #2	-	-	221	4.55%
Wells Fargo Business Credit term loan #3	-	-	512	4.55%
Wells Fargo Business Credit term loan #4	-	-	464	4.55%
Wells Fargo Business Credit term loan #5	-	-	352	4.55%
Wells Fargo Business Credit term loan #6	-	-	309	4.55%
Total	6,671		7,115	
Current maturities	(738)		(684)	
Total long-term debt	$ 5,933		$ 6,431	

The revolving line of credit facility ("RLOC") was originally entered into by the Company and Wells Fargo Business Credit ("Wells") on May 15, 2007 and, as currrently amended, is comprised of 1) a mortgage loan collateralized by a first mortgage position on the Company's Victoria, Minnesota production facility; 2) an equipment term loan collateralized by certain equipment in our Victoria, Minnesota and Tempe, Arizona production facilities; and 3) a revolving line of credt secured by all of our accounts receivable and inventories plus additional collateral provided by a Director of the Company.

As part of the RLOC, Thomas F. Leahy, a Director of the Company, had originally guaranteed the financing package by providing collateral of $4.0 million. Mr. Leahy's collateral pledge was reduced during Fiscal 2008 to $3.35 million and to $1.3 million in Fiscal 2009. In return for the guarantee and collateral pledge, he is paid a guarantee fee on a monthly basis by the Company in the amount of $2.4 per month.

On December 28, 2011, we amended the RLOC to extend the maturity date of all related indebtedness to May, 2014, increase the maximum line amount to $8.0 million, consolidate the six equipment term loans into one equipment term loan, provide an additional $2.0 million of availability for equipment term loans and provide for a reduction in Mr. Leahy's collateral pledge to $1.0 million if certain financial results were achieved for Fiscal 2011.

The interest on the real estate mortgage is 4.5% over the three-month London Inter Bank Offer Rate ("LIBOR"), the interest rate on the revolving line of credit advances is 4.0% over the three-month LIBOR and the interest rate on the equipment term loan is 4.25% over the three-month LIBOR, except upon an event of default. The credit facilities require a minimum interest charge of $150 per year and there is an unused line fee of 0.25% per year under the revolving credit facility. The three-month LIBOR was 0.58% and 0.30% as of December 31, 2011 and January 1, 2011, respectively.

The RLOC with Wells contains customary affirmative and negative covenants. The financial covenants include a limitation on capital expenditures and a minimum debt service coverage ratio. The creation of indebtedness outside the credit facility, creation of liens, making of certain investments, sale of assets, and incurrence of debt are all either limited or require prior approval from Wells under those covenants. The RLOC also contains customary events of default such as nonpayment and bankruptcy, which if they occur may constitute an event of default. The RLOC was amended on December 31, 2009, May 10, 2010 and October 18, 2010 as a result of violations of debt covenants that occurred during Fiscal 2009 and Fiscal 2010. The Company was in compliance with all of the debt covenants during all of Fiscal 2011.

At December 31, 2011, we have approximately $1.5 million of availability under our revolving credit facility, based on available advance rates on our accounts receivable and inventory balances.

Principal maturities of long-term debt at December 31, 2011, are as follows:

Fiscal Years	Principal Maturities
2012	$ 738
2013	738
2014	5,195
	6,671
Current portion	(738)
Total	$ 5,933

Note 5

Leases

Capital Leases:

During Fiscal 2011, the Company entered into three capital lease agreements to fund the acquisition of machinery and equipment in our Victoria, Minnesota and Tempe, Arizona manufacturing facilities. These leases are secured by the acquired equipment and were all 60 months in length. The weighted average effective interest rate of these leases was 7.9%. There were no capital lease obligations at the end of Fiscal year 2010.

The book value of assets under capital lease obligations are as follows:

	December 31, 2011	January 1, 2011
Original cost	$ 752	$ -
Accumulated depreciation	(51)	-
Total	$ 701	$ -

Operating Leases:

Tempe Facility - We lease an approximate 13,000 square foot production facility in Tempe, Arizona for our high density flexible substrate operations. The lease expired on July 31, 2010, but was extended through July 31, 2015. The Company has the one-time option to cancel the lease on January 31, 2014. Base rent on the lease that expired July 31, 2010 was approximately $103 per year and the rent on the new lease, expiring July, 31, 2015, is approximately $107 per year. During the first half of Fiscal 2010, we leased an additional 4,000 square feet of mixed office and warehouse space in Tempe, Arizona that was used for office and storage space in support of the Tempe operation. This lease had a base rent of approximately $36 per year and expired on July 31, 2010. We left that location and currently lease a similar mixed office and light manufacturing facility with approximately 8,400 square feet, also in Tempe, Arizona. The base rent of this lease is approximately $62 per year and expires on March 31, 2022.

Boulder Facility - We lease an approximate 152,000 square foot mixed office and manufacturing facility in Boulder, Colorado for our medical design and development and box build service operations. Currently, we occupy approximately 70,000 square feet of the facility for our operations, sublease approximately 43,000 square feet and approximately 39,000 square feet are vacant. In April 2005, we entered into a ten year sublease agreement for approximately 24,000 square feet with a high quality tenant. This is a ten year lease which provides for rental payments and reimbursement of operating costs. Aggregate rental and operating cost payments payable of approximately $281 per year commenced in November 2006. We have also subleased approximately 19,000 square feet of warehouse space to three additional tenants with agreements ranging from month-to-month to several years in length, which contribute approximately $106 on an annualized basis. We are continuing to look for sublease tenants for the remaining 39,000 square feet of vacant space. Our base rent payment for the Boulder facility lease was approximately $1.6 million for Fiscal 2011. In addition to the base rent, we pay all operating costs associated with this building.

In October, 2004, the Boulder facility lease was renegotiated into a 15-year operating lease that will expire in September, 2019. At the time of the renegotiated lease, the operating lease was considered to be at above-market terms and therefore, reserves were established for the amount that was above market and for certain obligations that came with the lease. These reserves are amortized over the remaining term of the lease and offset a portion of the related rent expense.

The terms of the October, 2004 lease provide for an annual base rent increase of 3% each year. Rent expense is recognized over the 15 year term of the lease on a straight line basis, and the difference between the expense charged to operations and amounts paid is recorded as an accrued lease expense obligation. Between October, 2004 and December 31, 2011, we have accrued $1.4 million in lease expenses as a long-term liability, which represents the excess of rent expense recorded in our results from operations over the rent payments made. Beginning in September, 2012, the accrued lease liability will begin to decline on a straight-line basis and will be reduced to zero at the end of the lease in September, 2019.

Long-term obligations recorded on our Balance Sheets related to the Boulder lease are as follows:

	December 31, 2011	January 1, 2011
Accrued lease expense	$ 1,387	$ 1,336
Unfavorable operating lease, net	312	353
Remaining sublease lease obligation	304	343
Total	2,003	2,032
Current maturities - operating lease accruals	(79)	(79)
Total long-term lease liabilities	$ 1,924	$ 1,953

Future minimum lease payments (excluding executory costs such as real estate taxes, insurance and maintenance expense) at December 31, 2011, related to all of our capital and operating leases are as follows:

Fiscal Years	Capital Leases	Operating Leases
2012	$ 154	$ 1,897
2013	154	1,943
2014	154	1,969
2015	154	1,982
2016	144	1,974
Thereafter	-	5,953
Total	760	15,718
Amount representing interest	(131)	-
Present value of future minimum lease payments	629	15,718
Current portion	(110)	-
Capital Lease Obligations, net of current portion	$ 519	$ 15,718

Total net rent expense for Fiscal 2011, 2010 and 2009 including common area costs and real estate taxes was $1.4 million, $1.4 million and $1.5 million, respectively.

Note 6

Income Taxes

Income tax expense (benefit) for Fiscal 2011, 2010 and 2009, consisted of the following:

	Fiscal Years Ended		
	December 31, 2011	January 1, 2011	January 2, 2010
Current:			
Federal	$ -	$ -	$ -
State	-	-	-
Deferred	-	-	-
Income tax expense (benefit)	$ -	$ -	$ -

Actual income tax expense (benefit) differs from the expected amount based upon the statutory federal tax rates as follows:

	Fiscal Years Ended		
	December 31, 2011	**January 1, 2011**	**January 2, 2010**
Federal statutory tax rate	(34.0%)	(34.0%)	(34.0%)
State income tax rate (net of federal tax effect)	(4.9%)	(4.9%)	(4.9%)
Change in valuation allowance	30.4%	68.5%	38.5%
Other - principally state tax deferred tax asset true-up and permanent items	8.5%	(29.6%)	0.4%
Effective tax rate	0.0%	0.0%	0.0%

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities at December 31, 2011 and January 1, 2011 are as follows:

	December 31, 2011	**January 1, 2011**
Deferred tax assets (current):		
Receivables	$ 14	$ 21
Inventories	383	328
Accrued liabilities	50	76
Total	447	425
Deferred tax assets (long-term):		
Net operating loss carry-forward	10,848	11,018
Stock-based compensation	75	61
Other	197	197
Gross deferred tax assets (long-term)	11,120	11,276
Less Deferred tax asset valuation allowance	(10,831)	(11,151)
Net deferred tax assets (long-term)	289	125
Deferred tax liabilities (long-term):		
Property and equipment	(736)	(550)
Net deferred tax liabilities (long-term)	(736)	(550)
Net deferred tax asset	$ -	$ -

The Company has federal and state net operating loss carry-forwards at December 31, 2011, of approximately $29.4 million and $11.5 million, respectively, which is available to reduce income taxes payable in future years. If not used, this carry-forward will expire in years 2021 through 2029. Under the Tax Reform Act of 1986, the utilization of this tax loss carry-forward may be limited as a result of significant changes in ownership.

The valuation allowance for deferred tax assets as of December 31, 2011 was $10.8 million and as of January 1, 2011 was $11.2 million. The total change in the valuation allowance for Fiscal 2011, 2010 and 2009 was a decrease of $320, an increase of $253 and an increase of $600, respectively. In assessing the recovery of the deferred tax asset, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income in the periods in which those temporary differences become deductible. Management considers the scheduled reversals of future deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment.

In accounting for uncertainty in income taxes, the Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more likely than not threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement with the relevant tax authority. As a result of the adoption, the Company did not recognize any cumulative changes in its provision for tax expenses.

With few exceptions, the Company is no longer subject to U.S. federal, state or local income tax examinations by tax authorities for the Fiscal years prior to 2008. The Company is not currently under examination by any taxing jurisdiction. In the event of any future tax assessments, the Company has elected to record the income taxes and any related interest and penalties as income tax expense on the Company's statements of operations.

Note 7

Stock Benefit Plans

1998 Plan. Under the Company's 1998 Stock Option Plan (the "1998 Plan"), a maximum of 2,000,000 shares of common stock was issuable pursuant to qualified and nonqualified stock options. Stock options granted become exercisable in varying increments with a portion tied to the closing stock price or up to a maximum of ten years, whichever comes first. The exercise price for options granted is equal to the closing market price of the common stock on the date of the grant. The 1998 Plan expired November 18, 2008. There were 177,000 shares outstanding under the 1998 Plan at December 31, 2011.

Directors' Plan. During Fiscal 1999, the shareholders approved the 1998 Stock Option Plan for Non-employee Directors (the "Director's Plan"). Under the Director's Plan, 425,000 shares were authorized for issuance, with an initial year grant of 55,000 shares and an annual grant thereafter of 10,000 shares to each non-employee director. These grants were effective each year upon adjournment of the annual shareholders' meeting at an exercise price equal to the market price on the date of grant. The options become exercisable at the earlier of seven years after the grant date or on the first day the market value equals or exceeds $25.00. These options expire ten years after the grant date. The Director's Plan expired November 18, 2008. There were 70,000 shares outstanding under the Director's Plan at December 31, 2011.

As of December 31, 2011, 237,000 of the 247,000 outstanding options are fully vested and have expiration dates ranging from January 2012 through June 2015.

Summary of Activity. The following is a summary of all activity involving the above stock option plans:

	Options Outstanding	Weighted Average Exercise Price Per Share	Aggregate Intrinsic Value
Balance, January 3, 2009	**363,700**	**$ 4.66**	
Granted	-	-	
Exercised	-	-	
Cancelled	(37,900)	5.79	
Balance, January 2, 2010	**325,800**	**4.53**	
Granted	-	-	
Exercised	-	-	
Cancelled	(28,800)	8.61	
Balance, January 1, 2011	**297,000**	**4.12**	
Granted	-	-	
Exercised	-	-	
Cancelled	(50,000)	9.93	
Balance, December 31, 2011	**247,000**	**$ 2.95**	**$ -**
Options exercisable	237,000	$ 2.94	$ -

The aggregate intrinsic value in the preceding table represents the total pretax intrinsic value, based on the Company's closing stock price of $0.88 as of December 30, 2011, which theoretically could have been received by the option holders had all option holders exercised their options as of that date. There were no in-the-money options outstanding as of December 31, 2011.

Options that were exercisable as of December 31, 2011, January 1, 2011 and January 2, 2010 were 237,000, 277,000 and 305,800, respectively. The average exercise price of exercisable options at December 31, 2011, January 1, 2010 and January 2, 2010 was $2.94, $4.18 and $4.56, respectively. The weighted average remaining contractual life for options exercisable was 1.8 years at December 31, 2011.

The following table summarizes information about stock options outstanding and exercisable as of December 31, 2011:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	**Number of Options**	**Weighted Average Exercise Price**	**Weighted Average Remaining Contractual Life**	**Number of Options**	**Weighted Average Exercise Price**
$1.68	50,000	$ 1.68	1.2	50,000	$ 1.68
$2.75-3.40	182,000	3.00	2.0	172,000	2.99
$5.95-7.70	15,000	6.53	0.1	15,000	6.53
	247,000	$ 2.95	1.7	237,000	$ 2.94

There were no options granted in Fiscal 2011, 2010 or 2009.

Common Stock Warrants. In May, 2005, the Company issued five-year warrants to purchase 527,152 shares of common stock at an exercise price of $3.05 in connection with a private equity offering and these warrants expired, unexercised, in May 2010. In February 2004, the Company issued five-year warrants to purchase 424,800 share of common stock at an exercise price of $3.72 in connection with a private equity placement and these warrants expired, unexercised, in February 2009. As of December 31, 2011 there were no remaining outstanding warrants.

Restricted Stock Awards. Restricted stock awards are awards of common stock that are subject to restrictions on transfer and to a risk of forfeiture if the awardee leaves the Company before the restrictions lapse. Only upon vesting, does the holder of a restricted stock award have the rights of a shareholder of the Company, including the right to vote the shares and the right to receive dividends on the shares. The value of such stock was established by the market price on the date of the grant. Compensation expense is being recorded over the applicable restricted stock vesting period, utilizing an estimated annual forfeiture rate of 15%. The Company has issued restricted stock to non-employee directors and certain members of the Company's management during the past three Fiscal years with vesting periods that range from six months to five years. A summary of the Company's restricted stock activity is presented in the following table:

	Shares	**Weighted Average Grant Date Fair Value**	**Weighted Average Remaining Contractual Term**
Unvested balance, January 3, 2009	**744,566**	**$ 1.02**	
Granted	-	-	
Vested	(90,816)	1.01	
Forfeited	(100,000)	1.00	
Unvested balance, January 2, 2010	**553,750**	**1.02**	
Granted	746,340	0.41	
Vested	(150,090)	0.47	
Forfeited	(50,000)	1.00	
Unvested balance, January 1, 2011	**1,100,000**	**0.41**	
Granted	284,507	0.84	
Vested	(249,507)	0.91	
Forfeited	(100,000)	0.41	
Unvested balance, December 31, 2011	**1,035,000**	**$ 0.70**	**2.92**

As of December 31, 2011, there was $626 of total unrecognized compensation costs related to the outstanding restricted stock awards which is expected to be recognized over a weighted average period of 2.9 years.

Note 8

Income (Loss) Per Common Share Computation

The components of income (loss) per basic and diluted shares are as follows:

	Fiscal Years Ended		
	December 31, 2011	**January 1, 2011**	**January 2, 2010**
Basic:			
Net income (loss)	$ 1,051	$ (369)	$ (1,558)
Income (loss) per common share	$ 0.11	$ (0.04)	$ (0.16)
Weighted average number of common shares outstanding	9,979,516	9,766,000	9,699,000

	Fiscal Years Ended		
	December 31, 2011	**January 1, 2011**	**January 2, 2010**
Diluted:			
Net income (loss)	$ 1,051	$ (369)	$ (1,558)
Income (loss) per common share	$ 0.10	$ (0.04)	$ (0.16)
Weighted average number of common shares, assuming dilution	10,290,885	9,766,000	9,699,000

Approximately 247,000, 1,397,000 and 1,407,000 shares under stock options, restricted stock and warrants have been excluded from the calculation of diluted net income (loss) per common share as they are antidilutive for our Fiscal 2011, 2010 and 2009, respectively.

Note 9

Equity Offerings

Sale of Convertible Preferred Stock

On May 9, 2005, we completed the sale of 130,538 shares of our Series A convertible preferred stock ("preferred stock") in a private placement to a group of institutional and accredited investors. Gross proceeds to us from the offering were $3.4 million. Each share of preferred stock is convertible into ten shares of our common stock, which in the aggregate would represent an additional 1,305,380 shares of common stock. Through December 31, 2011, 985,380 shares of common stock have been issued in connection with the conversion of 98,538 shares of convertible preferred stock (32,000 shares remaining outstanding at both December 31, 2011 and January 1, 2011).

The purchase price of the preferred stock was $26.00 per share. There are no dividend, coupon or redemption rights associated with our preferred stock; however our preferred stock includes a liquidation preference. The Convertible Preferred Shares have voting rights on an "as if" converted basis.

In the event that the Company liquidates or dissolves, the holders of each outstanding share of preferred stock will be entitled to receive an amount equal to $26.00 per share, plus any declared but unpaid dividends, in preference to the holders of our common stock or any other class of our capital stock ranking junior to our preferred stock. After the full payment of the preference amount to the holders of our preferred stock, and provision or payment of our debts and other liabilities, our remaining assets or property are distributable upon such liquidation and shall be distributed pro rata among the holders of our common stock. At December 31, 2011, there are two unconverted preferred shareholders.

Note 10

Other Financial Statement Data

The following provides additional information concerning selected balance sheet accounts:

	December 31, 2011	January 1, 2011
Accrued liabilities:		
Employee related costs	$ 462	$ 538
Current portion of long-term liabilities	-	79
Warranty reserve	28	14
Other accrued liabilities	211	87
Total accrued liabilities	$ 701	$ 718

Note 11

Guarantee by Related Party

On May 15, 2007, Thomas F. Leahy, a Director of the Company, provided a guarantee for the Wells RLOC financing package not to exceed $4.0 million and provided collateral to secure the guarantee in the same amount. This guarantee was subsequently reduced to $3.35 million in 2008 and further reduced to $1.3 million in 2009. In return for the guarantee and collateral pledge, he is paid a guarantee fee on a monthly basis by the Company. The current guarantee fee is $2.4 per month based on the $1.3 million in collateral and the guarantee fee was $8 per month based on the $3.35 million in collateral. The total guarantee fee paid to Mr. Leahy for Fiscal 2011, 2010 and 2009 was $29, $29 and $73, respectively and the guarantee fee is expected to continue for as long as the guarantee is in place.

On December 28, 2011, we amended the RLOC to extend the maturity date of all related indebtedness to May, 2014, increase the maximum line amount to $8.0 million, consolidate the six equipment term loans into one equipment term loan, provide an additional $2.0 million of availability for equipment term loans and provide for a reduction in Mr. Leahy's collateral pledge to $1.0 million if certain financial results were achieved for Fiscal 2011.

Note 12

Employee Benefit Plans

The Company has a 401(k) plan covering all eligible employees. Employees can make voluntary contributions to the plan of up to 90% of their compensation not to exceed the maximum specified by the Internal Revenue Code. The plan also provides for a matching contribution and a discretionary contribution by the Company. During Fiscal 2011, 2010 and 2009, the Company contributed $243, $247 and $273, respectively to the plan.

Note 13

Major Customers and Concentration of Credit Risk

The table below sets forth the approximate percentage of net sales to major customers that represented over 10% of our revenue:

	Fiscal Years Ended		
	December 31, 2011	**January 1, 2011**	**January 2, 2010**
Customer A	14%	*	12%
Customer B	12%	11%	*
Customer C	11%	*	15%
Customer D	10%	12%	13%
Customer E	*	*	14%
Total	47%	23%	54%

* Less than 10% for period posted

Accounts receivable from these customers represented 49% and 41% of the total trade accounts receivable at December 31, 2011 and January 1, 2011, respectively.

The Company generally sells its products to OEMs in the United States and abroad in accordance with supply contracts or purchase orders specific to certain manufacturer product programs. The Company performs ongoing credit evaluations of its customers' financial conditions and, generally, does not require collateral from its customers. The Company's continued sales to these customers are dependent upon the continuance of the customers' product programs.

Note 14

Reclassification

Certain minor reclassifications have been made to our prior period financial information in order to conform to the current year presentation. The reclassifications did not have an impact on previously reported net loss or shareholders' equity.

Note 15

Subsequent Events

The Company has performed an evaluation of subsequent events through February 24, 2012, which is the date that this annual report is issued.

Under the terms of the amended RLOC agreement with Wells that we signed on December 28, 2011, Mr. Leahy's guarantee, as described in Note 4, *Long-Term Debt* and Note 11, *Guarantee by Related Party*, will be reduced from $1.3 million to $1.0 million within five days of the issuance of this annual report based on our Fiscal 2011 financial results.

No additional disclosures were required based on this review by management.