

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)

Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2016

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 0-20852

ULTRALIFE CORPORATION

(Exact name of registrant as specified in its charter)

Delaware 16-1387013
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

2000 Technology Parkway, Newark, New York 14513
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (315) 332-7100

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

| Title of each class | Name of each exchange on which registered |
|--|---|
| Common Stock, par value \$0.10 per share | NASDAQ Global Market |

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

Indicate by check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes.... No..X...

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

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]

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.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company ..X...

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

On June 26, 2016, the aggregate market value of the common stock held by non-affiliates as defined in Rule 405 under the Securities Act of 1933) of the registrant was approximately \$46,435,667 (in whole dollars) based upon the closing price for such common stock as reported on the NASDAQ Global Market on June 24, 2016.

As of February 8, 2017, the registrant had 15,363,658 shares of common stock outstanding, net of 4,015,752 treasury shares.

DOCUMENTS INCORPORATED BY REFERENCE

Certain portions of the registrant's definitive proxy statement relating to the Annual Meeting of Shareholders to be held on July 18, 2017 are specifically incorporated by reference in Part III, Items 10, 11, 12, 13 and 14 of this Annual Report on Form 10-K, except for the equity plan information required by Item 12 as set forth herein.

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PART I

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements. This report contains certain forward-looking statements and information that are based on the beliefs of management as well as assumptions made by and information currently available to management. The statements contained in this report relating to matters that are not historical facts are forward-looking statements that involve risks and uncertainties, including, but not limited to, our reliance on certain key customers; potential costs because of the warranties we supply with our products and services; our efforts to develop new commercial applications for our products; possible future declines in demand for the products that use our batteries or communications systems; the unique risks associated with our China operations; reduced U.S. and foreign military spending including the uncertainty associated with government budget approvals; our inability to comply with changes to the regulations for the shipment of our products; variability in our quarterly and annual results and the price of our common stock; possible impairments of our goodwill and other intangible assets; possible breaches in security and other disruptions; safety risks, including the risk of fire; negative publicity of Lithium-ion batteries; our resources being overwhelmed by our growth prospects; our ability to retain top management and key personnel; potential disruptions in our supply of raw materials and components; our exposure to foreign currency fluctuations; our customers' demand falling short of volume expectations in our supply agreements; the risk that we are unable to protect our proprietary and intellectual property; rules and procedures regarding contracting with the U.S. and foreign governments; exposure to possible violations of the U.S. Foreign Corrupt Practices Act, the U.K. Bribery Act or other anti-corruption laws; our ability to utilize our net operating loss carry-forwards; our ability to comply with government regulations regarding the use of "conflict minerals"; possible audits of our contracts by the U.S. and foreign governments and their respective defense agencies; known and unknown environmental matters; technological innovations in the non-rechargeable and rechargeable battery industries; and other risks and uncertainties, certain of which are beyond our control.

Although we base these forward-looking statements on assumptions that we believe are reasonable when made, we caution you that forward-looking statements are not guarantees of future performance and that our actual results of operations, financial condition and liquidity and the development of the industries in which we operate may differ materially from those made in or suggested by the forward-looking statements contained herein. In addition, even if our results of operations, financial condition and liquidity and the development of the industries in which we operate are consistent with the forward-looking statements contained in this document, those results or developments may not be indicative of results or developments in subsequent periods. Given these risks and uncertainties, you are cautioned not to place undue reliance on these forward-looking statements. Any forward-looking statements that we make herein speak only as of the date of those statements, and we undertake no obligation to update those statements or to publicly announce the results of any revisions to any of those statements to reflect future events or developments. Comparisons of results for current and any prior periods are not intended to express any future trends or indications of future performance, unless expressed as such, and should only be viewed as historical data. When used in this report, the words "anticipate", "believe", "estimate" or "expect" or words of similar import are intended to identify forward-looking statements. For further discussion of certain of the matters described above and other risks and uncertainties, see "Risk Factors" in Item 1A of this Annual Report on Form 10-K.

As used in this annual report, unless otherwise indicated, the terms "the Company", "we", "our" and "us" refer to Ultralife Corporation ("Ultralife") and includes our wholly-owned subsidiaries, ABLE New Energy Co., Limited and its wholly-owned subsidiary ABLE New Energy Co., Ltd; Ultralife UK LTD and its wholly-owned subsidiary, Accutronics Ltd; Ultralife Batteries (UK) Ltd.; and our majority-owned joint venture Ultralife Batteries India Private Limited.

Dollar amounts throughout this Form 10-K Annual Report are presented in thousands of dollars, except for per share amounts.

ITEM 1. BUSINESS

General

We offer products and services ranging from power solutions to communications and electronics systems to customers across the globe in the government, defense and commercial sectors. With an emphasis on strong engineering and a collaborative approach to problem solving, we design and manufacture power and communications systems including: rechargeable and non-rechargeable batteries, charging systems, communications and electronics systems and accessories, and custom engineered systems. We continually evaluate ways to grow, including the design, development and sale of new products, expansion of our sales force to penetrate new markets and geographies, as well as seeking opportunities to expand through acquisitions.

We sell our products worldwide through a variety of trade channels, including original equipment manufacturers (“OEMs”), industrial and defense supply distributors, and directly to U.S. and international defense departments. We enjoy strong name recognition in our markets under our Ultralife® Batteries, Lithium Power®, McDowell Research®, AMTI™, ABLE™, ACCUTRONICS™, ACCUPRO™, and ENTELLION™ brands. We have sales, operations and product development facilities in North America, Europe and Asia.

We report our results in two operating segments: Battery & Energy Products and Communications Systems. The Battery & Energy Products segment includes: Lithium 9-volt, cylindrical, thin cell and other non-rechargeable batteries, in addition to rechargeable batteries, uninterruptable power supplies, charging systems and accessories. The Communications Systems segment includes: RF amplifiers, power supplies, cable and connector assemblies, amplified speakers, equipment mounts, case equipment, man-portable systems, integrated communication systems for fixed or vehicle applications and communications and electronics systems design. We believe that reporting performance at the gross profit level is the best indicator of segment performance. As such, we report segment performance at the gross profit level and operating expenses as Corporate charges. (See Note 11 in the Notes to Consolidated Financial Statements.)

Our website address is www.ultralifecorporation.com. We make available free of charge via a hyperlink on our website (see Investor Relations link on the website) our annual report on Form 10-K, proxy statements, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports and statements as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission (“SEC”). We will provide copies of these reports upon written request to the attention of Philip A. Fain, CFO, Treasurer and Secretary, Ultralife Corporation, 2000 Technology Parkway, Newark, New York, 14513. Our filings with the SEC are also available through the SEC website at www.sec.gov or at the SEC Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549 or by calling 1-800-SEC-0330.

Battery & Energy Products

We manufacture and/or market a family of Lithium Manganese Dioxide (Li-MnO₂), Lithium Manganese Dioxide Carbon Monofluoride (Li-CFx/MnO₂) hybrid and Lithium Thionyl Chloride (Li-SOCl₂) non-rechargeable batteries including 9-volt, HiRate® cylindrical, ThinCell®, and other form factors. Applications for our 9-volt batteries include: smoke alarms, wireless security systems and intensive care monitors, among many other devices. Our HiRate® and ThinCell® Lithium non-rechargeable batteries are sold primarily to the military and to OEMs in industrial markets for use in a variety of applications including radios, emergency radio beacons, search and rescue transponders, pipeline inspection gauges, portable medical devices and other specialty instruments and applications. Military applications for our non-rechargeable HiRate® batteries include: man-pack and survival radios, night vision devices, targeting devices, chemical agent monitors and thermal imaging equipment. Our Lithium Thionyl Chloride batteries, sold under our ABLE and Ultralife brands as well as a private label brand, are used in a variety of applications including utility meters, wireless security devices, electronic meters, automotive electronics and geothermal devices. We believe that the chemistry of Lithium batteries provides significant advantages over other currently available non-rechargeable battery technologies. These advantages include: higher energy density, lighter weight, longer operating time, longer shelf life and a wider operating temperature range. Our non-rechargeable batteries also have relatively flat voltage profiles, which provide stable power. Conventional non-rechargeable batteries, such as alkaline batteries, have sloping voltage profiles that result in decreasing power output during discharge. While the price of our Lithium batteries is generally higher than alkaline batteries, the increased energy per unit of weight and volume of our Lithium batteries allow for longer operating times and less frequent battery replacements for our targeted applications.

We believe that our ability to design and produce lightweight, high-energy Lithium ion and Nickel Metal Hydride (NiMH) rechargeable batteries and charging systems in a variety of custom sizes, shapes, and thicknesses offers substantial benefits to our customers. We market Lithium ion and NiMH rechargeable batteries comprising cells manufactured by qualified cell manufacturers. Our rechargeable products can be used in a wide variety of applications including communications, medical and other portable electronic devices.

Within this segment, we also seek to fund the development of new products that we hope will advance our technologies through contracts with both government agencies and private sector third parties.

We continue to obtain development contracts for intellectual property that we believe will enhance our efforts to commercialize new products that we develop. Revenues in this segment that pertain to development or license contracts may vary widely each year, depending upon the quantity and size of contracts obtained.

Revenues for this segment for the year ended December 31, 2016 were \$64,753 and segment contribution (gross profit) was \$19,580.

Under our McDowell Research and AMTI brands, we design and manufacture a line of communications systems and accessories to support military communications requirements, including RF amplifiers, power supplies, power cables, connector assemblies, amplified speakers, equipment mounts, case equipment, man-portable systems and integrated communication systems for fixed or vehicle applications such as vehicle adapters, Vehicle Installed Power Enhanced Rifleman Appliqué (“VIPER”) systems and SATCOM systems. All systems are packaged to meet specific customer needs in rugged enclosures to allow for their use in extreme environments. We market these products to all branches of the U.S. military and approved foreign defense organizations, as well as, U.S. and international prime defense contractors.

Revenues for this segment for the year ended December 31, 2016 were \$17,707 and segment contribution (gross profit) was \$5,528.

Corporate

We allocate revenues and cost of sales between the above operating segments. The balance of income and expense, including but not limited to research and development expenses, and selling, general and administrative expenses, are reported as Corporate expenses.

There were no revenues for this category for the year ended December 31, 2016 and our corporate operating expenses were \$21,345.

See Management’s Discussion and Analysis of Financial Condition and Results of Operations and the 2016 Consolidated Financial Statements and Notes thereto contained in this Annual Report on Form 10-K for additional information on the expenses referred to above. For information relating to total assets by segment, revenues for the last two years by segment, and contribution by segment for the last two years, see Note 11 in the Notes to Consolidated Financial Statements.

History

Ultralife was formed as a Delaware corporation in December 1990. In March 1991, we acquired certain technology and assets from Eastman Kodak Company (“Kodak”) relating to its 9-volt Lithium Manganese Dioxide non-rechargeable battery. In December 1992, we completed our initial public offering and became listed on NASDAQ.

In May 2006, we acquired ABLE New Energy Co., Ltd. (“ABLE”), an established manufacturer of Lithium batteries located in Shenzhen, China, which broadened our product offering, including a wide range of Lithium Thionyl Chloride and Lithium Manganese batteries, and provided additional exposure to new consumer markets.

In July 2006, we finalized the acquisition of substantially all the assets of McDowell Research, Ltd. (“McDowell”), a manufacturer of military communications accessories located originally in Waco, Texas. We relocated its operations to our Newark, New York facility during the second half of 2007, which enhanced our channels into the military communications area and strengthened our presence in global defense markets. In January 2012, we relocated these operations to our Virginia Beach, Virginia facility in order to gain operational efficiencies.

In March 2008, we formed a joint venture, named Ultralife Batteries India Private Limited (“India JV”), with our distributor partner in India. The India JV assembles Ultralife power solution products and manages local sales and marketing activities, serving commercial, government and defense customers throughout India. We have invested cash into the India JV, as consideration for our 51% ownership stake in the India JV.

In March 2009, we acquired the tactical communications products business of Science Applications International Corporation. The tactical communications products business (“AMTI”) designs, develops and manufactures tactical communications products including: amplifiers, man-portable systems, cables, power solutions and ancillary communications equipment, which are sold by Ultralife under the brand name AMTI. The acquisition strengthened our communications systems business and provided us with direct entry into the handheld radio/amplifier market, complementing Ultralife’s communications systems offerings.

In January 2016, we acquired Accutronics Limited (“Accutronics”), a U.K. corporation based in Newcastle-under-Lyme, U.K., a leading independent designer and manufacturer of smart batteries and charger systems for high-performance, feature-laden portable and handheld electronic devices. With a portfolio encompassing custom battery design, development and manufacturing for OEM’s; standard smart batteries, chargers and accessories; and pre-engineered batteries and power solutions for specific applications, Accutronics primarily serves the portable medical device market throughout Europe. Medical applications include digital imaging, ventilators, anesthesia, endoscopy, patient monitoring, cardio pulmonary care, oxygen concentration and aspiration. We acquired Accutronics to advance our strategy of commercial revenue diversification, to expand our geographical penetration, and to achieve revenue growth from new product development. We expect substantial sales synergies between Accutronics and our existing commercial battery business as we cross-sell our existing products and acquired Accutronics’ products to our respective customer bases.

Products, Services and Technology

Battery & Energy Products

A non-rechargeable battery is used until discharged and then replaced. The principal competing non-rechargeable battery technologies are Carbon zinc, alkaline and Lithium. We manufacture a range of non-rechargeable battery products based on Lithium Manganese Dioxide, Lithium Manganese Carbon Monofluoride hybrid, and Lithium Thionyl Chloride technologies.

We believe that the chemistry of Lithium batteries provides significant advantages over currently available non-rechargeable battery technologies, which include: lighter weight, longer operating time, longer shelf life, and a wider operating temperature range. Our non-rechargeable batteries also have relatively flat voltage profiles, which provide stable power. Conventional non-rechargeable batteries, such as alkaline batteries, have sloping voltage profiles that result in decreasing power during discharge. While the prices for our Lithium batteries are generally higher than commercially available alkaline batteries produced by others, we believe that the increased energy per unit of weight and volume of our batteries will allow longer operating time and less frequent battery replacements for our targeted applications. As a result, we believe that our non-rechargeable batteries are priced competitively with other battery technologies on a price per unit of energy or volume basis.

Our non-rechargeable products include the following product configurations:

9-Volt Lithium Battery. Our 9-volt Lithium battery delivers a unique combination of the highest available energy density and stable voltage, which results in a longer operating life for the battery and, accordingly, fewer battery replacements. While our 9-volt battery price is generally higher than conventional 9-volt Carbon zinc and alkaline batteries, we believe the enhanced operating performance and decreased costs associated with battery replacement make our 9-volt battery more cost effective than conventional batteries on a cost per unit of energy or volume basis when used in a variety of applications.

We market our 9-volt Lithium batteries to OEM, distributor and retail markets including industrial electronics, safety and security, and medical. Typical applications include: smoke alarms, wireless alarm systems, bone growth stimulators, telemetry devices, blood analyzers, ambulatory infusion pumps and parking meters. A significant portion of the sales of our 9-volt battery is to major smoke alarm OEMs for use in their long-life smoke alarms. We also manufacture our 9-volt Lithium battery under private labels for a variety of companies. Additionally, we sell our 9-volt battery to the broader consumer market through national and regional retail chains and Internet retailers.

Our current 9-volt battery manufacturing capacity is adequate to meet forecasted customer demand over the next three years.

Cylindrical Batteries. Featuring high energy, wide temperature range, long shelf life and operating life, our cylindrical cells and batteries, based on Lithium Manganese Dioxide, Lithium Manganese Dioxide Carbon Monofluoride hybrid and Lithium Thionyl Chloride technologies, represent some of the most advanced Lithium power sources currently available. We market a wide range of cylindrical non-rechargeable Lithium cells and batteries in various sizes under both the Ultralife HiRate and ABLE brands. These include: D, C, 5/4 C, 1/2 AA, 2/3 A and other sizes, which are sold individually as well as packaged into multi-cell battery packs, including our leading BA-5390 military battery, an alternative to the competing Li-SO₂ BA-5590 battery, and one of the most widely used battery types in the U.S. armed forces for portable applications. Our BA-5390 battery provides 50% to 100% more energy (mission time) than the BA-5590, and it is used in approximately 60 military applications. With the introduction of our Lithium Carbon Monofluoride hybrid chemistry, we now offer a D-cell that has 100% more energy than the competing Li-SO₂ D-cell.

We market our line of Lithium cells and batteries to the OEM market for commercial, defense, medical, asset tracking and search and rescue applications, among others. Significant commercial applications include pipeline inspection equipment, automatic re-closers and oceanographic devices. Asset tracking applications include RFID (Radio Frequency Identification) systems. Among the defense uses are manpack radios, night vision goggles, chemical agent monitors and thermal imaging equipment. Medical applications include: AED's (Automated External Defibrillators), infusion pumps and telemetry systems. Search and rescue applications include: ELT's (Emergency Locator Transmitters) for aircraft and EPIRB's (Emergency Position Indicating Radio Beacons) for ships.

Thin Cell Batteries. We manufacture a range of thin Lithium Manganese Dioxide batteries under the Thin Cell® brand. Thin Cell batteries are flat, lightweight batteries providing a unique combination of high energy, long shelf life, wide operating temperature range and very low profile. We are currently marketing these batteries to OEMs for applications such as displays, wearable medical devices, toll passes, theft detection systems, and RFID devices.

In contrast to non-rechargeable batteries, after a rechargeable battery is discharged, it can be recharged and reused many times. Generally, discharge and recharge cycles can be repeated hundreds or thousands of times in rechargeable batteries, but the achievable number of cycles (cycle life) varies among technologies and is an important competitive factor. All rechargeable batteries experience a small, but measurable, loss in energy with each cycle. The industry commonly reports cycle life in the number of cycles a battery can achieve until 80% of the battery's initial energy capacity remains. In the rechargeable battery market, the principal competing technologies are Nickel Cadmium, Nickel Metal Hydride and Lithium ion (including Lithium polymer) batteries. Rechargeable batteries are used in many applications, such as military radios, laptop computers, mobile telephones, portable medical devices, wearable devices and many other commercial, defense and consumer products.

Three important performance characteristics of a rechargeable battery are design flexibility, energy density and cycle life. Design flexibility refers to the ability of rechargeable batteries to be designed to fit a variety of shapes and sizes of battery compartments. Thin profile batteries with prismatic geometry provide the design flexibility to fit the battery compartments of today's electronic devices. Energy density refers to the total amount of electrical energy stored in a battery divided by the battery's weight and volume as measured in watt-hours per kilogram and watt-hours per liter, respectively. High energy density batteries generally are longer lasting power sources providing longer operating time and necessitating fewer battery recharges. High energy density and long achievable cycle life are important characteristics for comparing rechargeable battery technologies. Greater energy density will permit the use of batteries of a given weight or volume for a longer time period. Accordingly, greater energy density will enable the use of smaller and lighter batteries with energy comparable to those currently marketed. Lithium ion batteries, by the nature of their electrochemical properties, are capable of providing higher energy density than comparably sized batteries that utilize other chemistries and, therefore, tend to consume less volume and weight for a given energy content. Long achievable cycle life, particularly in combination with high energy density, is suitable for applications requiring frequent battery recharges, such as cellular telephones and laptop computers, and allows the user to charge and recharge many times before noticing a difference in performance. We believe that our lithium ion batteries generally have some of the highest energy density and longest cycle life available.

Lithium Ion Cells and Batteries. We market a variety of Lithium ion cells and rechargeable batteries comprising cells manufactured by qualified cell manufacturers. These products are used in a wide variety of applications including communications, medical and other portable electronic devices.

Battery Charging Systems and Accessories. To provide our customers with complete power system solutions, we offer a wide range of rugged military and commercial battery charging systems and accessories including smart chargers, multi-bay charging systems and a variety of cables.

Multi-Kilowatt Module. Our Multi-Kilowatt Module lithium ion battery system is a large format battery utilizable for energy storage, battery back-up, and remote power applications. This product is a direct replacement of 2.5 kWh and greater lead acid batteries in 24V or 48V applications. It can be connected in multiples to obtain higher-voltages and is capable of over 3,000 cycles while maintaining 80% of its capacity.

Technology Contracts. Our technology contract activities involve the development of new products or the enhancement of existing products through contracts with both government agencies and other private sector third parties.

Communications Systems

Under our McDowell Research and AMTI brands, we design and manufacture a line of communications systems and accessories to support military communications systems, including RF amplifiers, power supplies, power cables, connector assemblies, amplified speakers, equipment mounts, case equipment, man-portable systems and integrated communication systems for fixed or vehicle applications such as vehicle adapters and SATCOM systems. We package all systems to meet specific customer needs in rugged enclosures to allow their use in extreme environments.

We offer a wide range of military communications systems and accessories designed to enhance and extend the operation of communications equipment such as vehicle-mounted, manpack and handheld transceivers. Our communications products include the following product configurations:

RF Amplifiers. Our RF amplifiers include: 20, 50 and 75-watt amplifiers and 20-watt accessories and kits. These amplifiers are used to extend the range of manpack and handheld tactical transceivers and can be used on mobile or fixed site applications.

Integrated Systems. Our integrated systems include: vehicle mounted systems; SATCOM systems; rugged, deployable case systems; multiband transceiver kits; enroute communications cases; and radio cases. These systems give communications operators everything that is needed to provide reliable links to support C4ISR (Command, Control, Communications, Computers and Information, Surveillance and Reconnaissance).

Power Systems. Our power systems include: universal AC/DC power supplies with battery backup for tactical manpack and handheld transceivers; ROVER™ power supplies; interoperable power adapters and chargers; portable power systems; tactical combat and AC to DC power supplies, among many others. We can provide power supplies for virtually all tactical communications devices.

Communications and Electronics. Our communications and electronics services include the design, integration, and fielding of portable, mobile and fixed-site communications systems.

Sales and Marketing

We employ a staff of sales and marketing personnel in North America, Europe and Asia. We sell our products and services directly to commercial customers, including OEM's, as well as government and defense agencies in the U.S. and abroad and have contractual arrangements with sales agents who market our products on a commission basis in defined territories. Every effort is made to adjust future prices accordingly, but the ability to adjust prices is generally based on market conditions.

We also distribute some of our products through domestic and international distributors and retailers. Our sales are generated primarily from customer purchase orders. We have several long-term contracts with the U.S. government and other customers. These contracts do not commit the customers to specific purchase volumes, nor to specific timing of purchase order releases, and they include fixed price agreements over various periods of time. In general we do not believe our sales are seasonal, although we may sometimes experience seasonality for some of our military products based on the timing of government fiscal budget expenditures.

A significant portion of our business comes from sales of products and services to the U.S. and foreign governments through various contracts. These contracts are subject to procurement laws and regulations that specify policies and procedures for acquiring goods and services. The regulations also contain guidelines for managing contracts after they are awarded, including conditions under which contracts may be terminated, in whole or in part, at the government's convenience or for default. Failure to comply with the procurement laws or regulations can result in civil, criminal or administrative proceedings involving fines, penalties, suspension of payments, or suspension or debarment from government contracting or subcontracting for a period of time.

During the year ended December 31, 2016 we had two major customers, both large defense primary contractors, which individually comprised 13% and 12% of our revenues, respectively, in 2016 and 2% and 23% of our revenues, respectively, in 2015. There were no other customers that comprised greater than 10% of our total revenues during these years.

In 2016, sales to U.S. and non-U.S. customers were approximately \$45,094 and \$37,366, respectively. In 2015, sales to U.S. and non-U.S. customers were approximately \$46,741 and \$29,686, respectively. For more information relating to revenues by country for the last two fiscal years and long-lived assets for the last two fiscal years by country of origin, see Note 11 in the Notes to the Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K.

Battery & Energy Products

We target sales of our non-rechargeable products to manufacturers of security and safety equipment, medical devices, search and rescue equipment, specialty instruments, point of sale equipment and metering applications, as well as users of military equipment. Our strategy is to develop sales and marketing alliances with OEM's and governmental agencies that utilize our batteries in their products, commit to cooperative research and development or marketing programs, and recommend our products for design-in or replacement use in their products. We are addressing these markets through direct contact by our sales and technical personnel, use of sales agents and stocking distributors, manufacturing under private label, and promotional activities.

We seek to capture a significant market share for our products within our targeted OEM markets, which we believe, if successful will result in increased product awareness and sales at the end-user or consumer level. We are also selling our 9-volt battery to the consumer market through retail distribution through a number of national retailers. Most military procurements are done directly by the specific government organizations requiring products, based on a competitive bidding process. Additionally, we are typically required to successfully meet contractual specifications and to pass various qualifications testing for the products under contract by the military. An inability by us to pass these tests for our new products in a timely fashion could have a material adverse effect on future growth prospects. When a government contract is awarded, there is a government procedure that allows for unsuccessful companies to formally protest the award if they believe they were unjustly treated in the government's bid evaluation process. A prolonged delay in the resolution of a protest, or a reversal of an award resulting from such a protest, could have a material adverse effect on our business, financial condition and results of operations.

We market our products to defense organizations in the U.S. and other countries. These efforts have resulted in our winning significant contracts. In September 2010, we were awarded a production contract by the Defense Logistics Agency for up to five years, with a maximum total potential of \$42,100, to provide our BA-5390 non-rechargeable Lithium Manganese Dioxide batteries to the U.S. military. Production deliveries began in the first quarter of 2011. Through the completion of the contract in September 2015, we shipped BA-5390 batteries totaling \$10,000. Subsequent to the completion of the contract, we continued to receive orders for BA-5390 batteries from the Defense Logistics Agency that we shipped in 2015 and 2016, and that are included in our 2017 backlog. A subsequent contract has not been awarded by the Defense Logistics Agency for BA -5390 batteries at this time.

We target sales of our Lithium ion rechargeable batteries and charging systems to OEM customers, as well as distributors and resellers focused on our target markets. We respond to RFPs to design products for OEMs, and believe that our design capabilities, product characteristics and solution integration will drive OEMs to incorporate our batteries into their product offerings, resulting in revenue growth opportunities for us.

We continue to expand our marketing activities as part of our strategic plan to increase sales of our rechargeable products for commercial, standby, defense and communications applications, as well as hand-held devices, wearable devices and other electronic portable equipment. A key part of this expansion includes increasing our design and assembly capabilities as well as building our network of distributors and value added distributors throughout the world.

At December 31, 2016 and 2015, our backlog related to Battery & Energy Products was approximately \$23,100 and \$18,500, respectively. The increase in our backlog related to Battery & Energy Products is primarily due to our acquisition of Accutronics, and higher demand for batteries from a large U.S.-based global defense contractor, government and defense suppliers and a global medical products OEM. The 2016 backlog is related to orders that are expected to ship throughout 2017.

Communications Systems

We target sales of our communications systems, which include power solutions and accessories to support communications systems such as RF amplifiers, power supplies, power cables, connector assemblies, amplified speakers, equipment mounts, case equipment and integrated communication systems, to military OEMs and U.S. and allied foreign militaries. We sell our products directly and through authorized distributors to OEMs and to defense organizations in the U.S. and internationally. We market our products to defense organizations and OEMs in the U.S. and internationally.

At December 31, 2016 and 2015, our backlog related to Communications Systems orders was approximately \$3,000 and \$8,400, respectively. The 2016 backlog related to Communications Systems reflects orders from a large U.S.-based global defense contractor. The 2015 backlog represents the award of an \$8,200 order through an OEM for the U.S. Army for our McDowell Research Corporation ("MRC") product – Vehicle Installed Power Enhanced Rifleman Appliqué ("VIPER"), as well as integrated systems supporting OEM's. The 2015 backlog was shipped in 2016, and the 2016 backlog is expected to ship in 2017.

Patents, Trade Secrets and Trademarks

We rely on licenses of technology as well as our patented and unpatented proprietary information, know-how and trade secrets to maintain and develop our competitive position. Despite our efforts to protect our proprietary information, there can be no assurance that others will neither develop the same or similar information independently nor obtain access to our proprietary information, know how and trade secrets. In addition, there can be no assurance that we would prevail if we asserted our intellectual property rights against third parties, or that third parties will not successfully assert infringement claims against us in the future. We believe, however, that our success depends more on the knowledge, ability, experience and technological expertise of our employees, than on the legal protection that our patents and other proprietary rights may or will afford.

We hold ten patents issued in the U.S., two patents issued in Mexico and one patent issued in the European Union, and have three patents pending in the U.S. and Europe. We believe our patents protect technology that makes automated production more cost-effective and protects important competitive features of our products. However, we do not consider our business to be dependent on patent protection.

As part of our employment commencement process, our employees are required to enter into agreements providing for confidentiality of certain information and the assignment of rights to inventions made by them while employed by us. These agreements also contain certain noncompetition and non-solicitation provisions effective during the employment term and for varying periods thereafter depending on position and location. There can be no assurance that we will be able to enforce these agreements. All of our employees agree to abide by the terms of a Code of Ethics policy that provides for the confidentiality of certain information received during the course of their employment. Nevertheless, the enforceability of such agreements is subject to public policy limitations that vary from state to state so we cannot assure that they will be enforceable in accordance with their terms, if at all.

Trademarks are an important aspect of our business. We sell our products under a number of trademarks, which we own or use under license. The following are registered trademarks of ours: Ultralife®, Ultralife Thin Cell®, Ultralife HiRate®, LithiumPower®, LithiumPower & Design®, SmartCircuit®, We Are Power®, AMTI®, ABLE™ ACCUTRONICS®, ACCUPRO®, ENTELLION®, Intelligent Power Vault®, McDowell Research® and RPS®.

Manufacturing and Raw Materials

We manufacture our products from raw materials and component parts that we purchase. Our manufacturing facilities in Newark, New York are ISO 9001:2008, ISO 14001, and ISO 13485 certified. Our manufacturing facilities in Shenzhen, China are ISO 9001:2008, ISO 14001 and ISO 13485 certified. Our manufacturing facilities in Virginia Beach, Virginia are ISO 9001:2008 certified. Our manufacturing facilities in the United Kingdom are ISO 9001 and ISO 13485 certified.

We expect our future raw material purchases to fluctuate based on our knowledge regarding the timing of customer orders, the related need to build inventory in anticipation of orders and actual shipment dates.

Battery & Energy Products

Our Newark, New York and Shenzhen, China facilities have the capacity to produce cylindrical cells, 9-volt batteries, and thin cells. Capacity, however, is also affected by demand for particular products, and product mix changes can produce bottlenecks in an individual operation, constraining overall capacity. We have acquired new machinery and equipment in areas where production bottlenecks have resulted in the past and we believe that we have sufficient capacity in these areas. We continually evaluate our requirements for additional capital equipment, and we believe that the planned increases will be adequate to meet foreseeable customer demand.

Certain materials used in our products are available only from a single source or a limited number of sources. Additionally, we may elect to develop relationships with a single or limited number of sources for materials that are otherwise generally available. Although we believe that alternative sources are available to supply materials that could replace materials we use and that, if necessary, we would be able to redesign our products to make use of an alternative material, any interruption in our supply from any supplier that serves currently as our sole source could delay product shipments and adversely affect our financial performance and relationships with our customers. Although we have experienced interruptions of product deliveries by sole source suppliers, which have not had a material adverse effect on us, we cannot assure that they would not have an adverse effect on us in the future. All other raw materials utilized by us are readily available from many sources.

We believe that the raw materials and components utilized for our rechargeable batteries are readily available from many sources. Although we believe that alternative sources are available to supply materials and components that could replace materials or components we use, any interruption in our supply from any supplier that serves currently as our sole source could delay product shipments and adversely affect our financial performance and relationships with our customers.

Our Newark, New York facility has the capacity to produce significant volumes of rechargeable batteries, as this operation generally assembles battery packs and chargers and is limited only by physical space and is not constrained by manufacturing equipment capacity which can accommodate significant additional volumes of product. Similarly, our China and United Kingdom facilities also have capacity to produce significant quantities beyond current volumes and are not constrained by manufacturing equipment capacity.

The total carrying value of our Battery & Energy Products inventory, including raw materials, work in process and finished goods, amounted to approximately \$13,639 and \$12,534 as of December 31, 2016 and 2015, respectively. The year-over-year increase reflects the acquisition of Accutronics in January 2016.

Communications Systems

In general, we believe that the raw materials and components utilized by us for our communications accessories and systems, including RF amplifiers, power supplies, cables, repeaters and integration kits, are available from many sources. Although we believe that alternative sources are available to supply materials and components that could replace materials or components we use, any interruption in our supply from any supplier that serves currently as our sole source could delay product shipments and adversely affect our financial performance and relationships with our customers.

Our Virginia Beach, Virginia facility has the capacity to produce communications products and systems. This operation generally assembles products and is limited only by physical space and is not constrained by manufacturing equipment capacity.

The total carrying value of our Communications Systems inventory, including raw materials, work in process and finished goods, amounted to approximately \$9,817 and \$11,280 as of December 31, 2016 and 2015, respectively. The year-over-year decrease resulted from the fulfillment of the large VIPER award and improved inventory management in 2016.

Research and Development

We concentrate significant resources on research and development activities to improve our technological capabilities and to design new products for customers' applications. We conduct our research and development in Newark, New York; Virginia Beach, Virginia; Tallahassee, Florida; Newcastle-under-Lyme, United Kingdom and Shenzhen, China. During 2016 and 2015, we expended \$6,155 and \$6,112, respectively, on research and development, including \$209 and \$509, respectively, on customer sponsored research and development activities, which are included in cost of goods sold. We expect that research and development expenditures in the future will be fairly consistent with those in 2016, as we anticipate that new product development initiatives will drive our growth. As in the past, we will continue to make funding decisions for our research and development efforts based upon strategic demand for customer applications.

Battery & Energy Products

We continue to internally develop non-rechargeable cells and batteries with the goal of broadening our product offering to our customers.

We continue to internally develop our rechargeable product portfolio, including batteries, battery management systems, cables and charging systems, as our customers' needs for portable power continue to grow and new technologies become available.

The U.S. government sponsors research and development programs designed to improve the performance and safety of existing battery systems and to develop new battery systems.

We continue to internally develop a variety of communications accessories and systems for the global defense market to meet the ever-changing demands of our customers.

Safety; Regulatory Matters; Environmental Considerations

Certain of the materials utilized in our batteries may pose safety problems if improperly used, stored, or handled. We have designed our batteries to minimize safety hazards both in manufacturing and use.

The transportation of non-rechargeable and rechargeable Lithium batteries is regulated in the U.S. by the Department of Transportation's Pipeline and Hazardous Materials Safety Administration ("PHMSA"), and internationally by the International Civil Aviation Organization ("ICAO") and corresponding International Air Transport Association ("IATA") Dangerous Goods Regulations and the International Maritime Dangerous Goods Code ("IMDG"), and other country specific regulations. These regulations are based on the United Nations Recommendations on the Transport of Dangerous Goods Model Regulations and the United Nations Manual of Tests and Criteria. We currently ship our products pursuant to PHMSA, ICAO, IATA, IMDG and other country specific hazardous goods regulations. The regulations require companies to meet certain testing, packaging, labeling, marking and shipping paper specifications for safety reasons. We have not incurred, and do not expect to incur, any significant costs in order to comply with these regulations. We believe we comply with all current U.S. and international regulations for the shipment of our products, and we intend and expect to comply with any new regulations that are imposed. We have established our own testing facilities to ensure that we comply with these regulations. However, if we are unable to comply with any such new regulations, or if regulations are introduced that limit our or our customers' ability to transport our products in a cost-effective manner, this could have a material adverse effect on our business, financial condition and results of operations.

The European Union's Restriction of Hazardous Substances Directive ("the EU RoHS Directive") places restrictions on the use of certain hazardous substances in electrical and electronic equipment. All applicable products sold in the European Union market must pass RoHS compliance. While this directive does not apply to batteries and does not currently affect our defense products, should any changes occur in the directive that would affect our products, we intend and expect to comply with any new regulations that are imposed. However, we cannot assure that the cost of complying with such new regulations would not have a material adverse effect on us. Our commercial chargers are substantially in compliance with the EU RoHS Directive.

The European Union's Battery Directive "on batteries and accumulators and waste batteries and accumulators" (the "EU Battery Directive") is intended to cover all types of batteries regardless of their shape, volume, weight, material composition or use. It is aimed at reducing mercury, cadmium, lead and other metals in the environment by minimizing the use of these substances in batteries and by treating and re-using old batteries. The EU Battery Directive applies to all types of batteries except those used to protect European Member States' security, for military purposes, or sent into space. To achieve these objectives, the EU Battery Directive prohibits the marketing of some batteries containing hazardous substances. It establishes schemes aimed at high level of collection and recycling of batteries with quantified collection and recycling targets. The EU Battery Directive sets out minimum rules for producer responsibility and provisions with regard to labeling of batteries and their removability from equipment. The EU Battery Directive requires product markings for batteries and accumulators to provide information on capacity and to facilitate reuse and safe disposal. We currently ship our products pursuant to the requirements of the EU Battery Directive.

This EU Battery Directive requires that producers or importers of particular classes of electrical goods are financially responsible for specified collection, recycling, treatment and disposal of past and future covered products. This directive assigns levels of responsibility to companies doing business in European Union markets based on their relative market share. This directive calls on each European Union member state to enact enabling legislation to implement the directive. As additional European Union member states pass enabling legislation our compliance system should be sufficient to meet such requirements. Our current estimated costs associated with our compliance with these directives based on our current market share are not significant. However, we continue to evaluate the impact of these directives as European Union member states implement guidance, and actual costs could differ from our current estimates.

China's "Management Methods for Restricted Use of Hazardous Substances in Electrical and Electronic Products" ("China RoHS 2") provides a regulatory framework including hazardous substance restrictions similar to those imposed by the EU RoHS Directive. China RoHS 2 applies to methods for the control and reduction of pollution and other public hazards to the environment caused during the production, sale, and import of electrical and electronic products ("EEP") in China. The regulatory framework of China RoHS 2, also now references the updated marking and labeling requirements under Standard SJ/T 11364-2014 ("Marking Standard"). The methods under China RoHS 2 only apply to EEP placed in the marketplace in China. We believe our compliance system is sufficient to meet our requirements under China RoHS 2. Our current estimated costs associated with our compliance with this regulation based on our current market share are not significant. However, we continue to evaluate the impact of this regulation, and actual costs could differ from our current estimates.

National, state and local laws impose various environmental controls on the manufacture, transportation, storage, use and disposal of batteries and of certain chemicals used in the manufacture of batteries. Although we believe that our operations are in material compliance with current environmental regulations, there can be no assurance that changes in such laws and regulations will not impose costly compliance requirements on us or otherwise subject us to future liabilities, costs and expenses. There can be no assurance that additional or modified regulations relating to the manufacture, transportation, storage, use and disposal of materials used to manufacture our batteries or restricting disposal of batteries will not be imposed or that such regulations will not have a material adverse effect on our business, financial condition and results of operations. In 2016 and 2015, we spent approximately \$117 and \$155, respectively, on environmental compliance, including costs to properly dispose of potentially hazardous waste.

Since non-rechargeable and rechargeable Lithium battery chemistries react adversely with water and water vapor, certain of our manufacturing processes must be performed in a controlled environment with low relative humidity. Our Newark, New York and Shenzhen, China facilities contain dry rooms or glove box equipment, as well as specialized air-drying equipment.

In addition to the environmental regulations previously described, our products are subject to U.S. and international laws and regulations governing international trade and exports including but not limited to the International Traffic in Arms Regulations (“ITAR”), the Export Administration Regulations (“EAR”) and trade sanctions against embargoed countries.

The ITAR is a set of United States government regulations that control the export and import of defense-related articles and services on the United States Munitions List. These regulations implement the provisions of the Arms Export Control Act, and are described in the Code of Federal Regulations. The Department of State Directorate of Defense Trade Controls interprets and enforces ITAR. Its goal is to safeguard U.S. national security and further U.S. foreign policy objectives.

The related EAR are enforced and interpreted by the Bureau of Industry and Security in the Commerce Department. The Department of Defense is also involved in the review and approval process. Inspections in support of import and export laws are performed at border crossings by Customs and Border Protection, an agency of the Department of Homeland Security.

Products and services developed and manufactured in our foreign locations are subject to the export and import controls of the nation in which the foreign location operates.

We believe we are in material compliance with these domestic and international export regulations. However, failure of compliance could have a material adverse effect on our business through possible fines, denial of export privileges, or loss of customers. Further, while we are not aware of any proposed changes to these regulations, any change in the scope or enforcement of export or import regulations or related legislation could have a material adverse effect on our business through increased costs of compliance or reduction in the international growth prospects available to us.

Our future estimated costs associated with our compliance with ITAR, EAR, and the foreign export and import controls we are subject to based on our current sales volumes are not significant. However, we continue to evaluate the impact of these regulations, and actual costs could differ from our current estimates.

Battery & Energy Products

Our non-rechargeable battery products incorporate Lithium metal, which reacts with water and may cause fires if not handled properly. In the past, we have experienced fires that have temporarily interrupted certain manufacturing operations. We believe that we have adequate fire suppression systems and insurance, including business interruption insurance, to protect against the occurrence of fires and fire losses in our facilities.

Our 9-volt battery, among other sizes, is designed to conform to the dimensional and electrical standards of the American National Standards Institute. Authorized certification bodies such as Underwriters Laboratories, Intertek and SGS recognize several of our products.

We are not currently aware of any regulatory requirements regarding the disposal of communications products.

Corporate

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 Section 1502 (the “Dodd-Frank Act”) requires public companies to disclose whether tantalum, tin, gold and tungsten, commonly known as “conflict minerals,” are necessary to the functionality or production of a product manufactured by a public company and if those elements originated from armed groups in the Democratic Republic of Congo or adjoining countries. To comply with the Dodd-Frank Act, as implemented by SEC rules, we are required to perform due diligence inquiries of our suppliers to determine whether or not our products contain such minerals and from which countries and source (smelter) the minerals were obtained. Our annual report on Form SD was filed by the statutory due date of June 1, 2016 for the 2015 calendar year and we continue to implement appropriate measures with our suppliers in order to better ascertain the origin of the conflict minerals in our products.

Competition

Competition in both the battery and communications systems markets is, and is expected to remain, intense. The competition ranges from development stage companies to major domestic and international companies, many of which have financial, technical, marketing, sales, manufacturing, distribution and other resources significantly greater than ours. We compete against companies producing batteries as well as companies producing communications systems. We compete on the basis of design flexibility, performance, price, reliability and customer support. There can be no assurance that our technologies and products will not be rendered obsolete by developments in competing technologies or services that are currently under development or that may be developed in the future or that our competitors will not market competing products and services that obtain market acceptance more rapidly than ours.

Historically, although other entities may attempt to take advantage of the growth of the battery market, the Lithium battery cell industry has certain technological and economic barriers to entry. The development of technology, equipment and manufacturing techniques and the operation of a facility for the automated production of Lithium battery cells require large capital expenditures, which may deter new entrants from commencing production. Through our experience in battery cell manufacturing, we have also developed significant expertise in the non-rechargeable battery market, which we believe would be difficult to reproduce without substantial time and expense.

Employees

As of December 31, 2016, we employed a total of 552 permanent and temporary employees: 35 in research and development, 447 in production and 70 in sales and administration. None of our employees are represented by a labor union.

ITEM 1A. RISK FACTORS

Our business faces many risks. As such, prospective investors and shareholders should carefully consider and evaluate all of the risk factors described below as well as other factors discussed in this Annual Report on Form 10-K and in our other filings with the SEC. Any of these factors could adversely affect our business, financial condition and results of operations. Additional risks and uncertainties that are not currently known to us or that are not currently believed by us to be material may also harm our business operations and financial results. These risk factors may change from time to time and may be amended, supplemented, or superseded by updates to the risk factors contained in periodic reports on Form 10-Q and Form 10-K that we file with the SEC in the future.

A significant portion of our revenues is derived from certain key customers.

During the years ended December 31, 2016 and 2015, we had two major customers, both large defense primary contractors, which together comprised 25% of our revenues in each year. Last year, one of those customers comprised 23% of our sales. There were no other customers that comprised greater than 10% of our total revenues during these years. While we consider our relationship with this prime contractor to be good, the reduction, delay or cancellation of orders from this customer or this customer’s insolvency / inability to pay, for any reason, would reduce our revenue and operating income and could materially and adversely affect our business, operating results and financial condition in other ways.

We may incur significant costs because of the warranties we supply with our products and services.

With respect to our battery products, we typically offer warranties against any defects in manufacture or workmanship for a period up to one year from the date of purchase. With respect to our communications systems products, we now offer up to a three-year warranty. We provide for a reserve for these potential warranty expenses, which is based on an analysis of historical warranty issues. There is no assurance that future warranty claims will be consistent with past history, and in the event we experience a significant increase in warranty claims, there is no assurance that our reserves will be sufficient. This could have a material adverse effect on our business, financial condition and results of operations.

Our efforts to develop new products or new commercial applications for our products could be prolonged or could fail.

Although we develop certain products for new commercial applications, we cannot assure that our products will be accepted due to the highly competitive nature of the industry. There are many new product and technology entrants into the marketplace, and we must continually reassess the market segments in which our products can be successful and seek to engage customers in those segments that will adopt our products for use in their products. In addition, these companies must be successful with their products in their markets for us to gain increased business. Increased competition, failure to gain customer acceptance of products, the introduction of competitive technologies or failure of our customers in their markets could have a further adverse effect on our business and reduce our revenue and operating income.

A decline in demand for products using our batteries or communications systems could reduce demand for our products and/or our products could become obsolete.

A substantial portion of our business depends on the continued demand for products using our batteries and communications systems sold by our customers, including original equipment manufacturers. Our success depends significantly upon the success of those customers' products in the marketplace. We are subject to many risks beyond our control that influence the success or failure of a particular product or service offered by a customer, including:

- competition faced by the customer in its particular industry,
- market acceptance of the customer's product or service,
- the engineering, sales, marketing and management capabilities of the customer,
- technical challenges unrelated to our technology or products faced by the customer in developing its products or services, and
- the financial and other resources of the customer.

The market for our products is characterized by changing technology and evolving industry standards, often resulting in product obsolescence or short product lifecycles. Although we believe that our products utilize state-of-the-art technology, there can be no assurance that competitors will not develop technologies or products that would render our technologies and products obsolete or less marketable. Many of the companies with which we compete have substantially greater resources than we do, and some have the capacity and volume of business to be able to produce their products more efficiently than we can. In addition, these companies are developing or have developed products using a variety of technologies that are expected to compete with our technologies. If these companies successfully market their products in a manner that renders our technologies obsolete, this would reduce our revenue and operating income and could have other material adverse effects on our business, financial condition and results of operations.

Our operations in China are subject to unique risks and uncertainties.

Our operating facility in China presents risks including, but not limited to, changes in local regulatory requirements, changes in labor laws, local wage laws, environmental regulations, taxes and operating licenses, compliance with U.S. regulatory requirements, including the Foreign Corrupt Practices Act, uncertainties as to application and interpretation of local laws and enforcement of contract and intellectual property rights, currency restrictions, currency exchange controls, fluctuations of currency, and currency revaluations, eminent domain claims, civil unrest, power outages, water shortages, labor shortages, labor disputes, increase in labor costs, rapid changes in government, economic and political policies, political or civil unrest, acts of terrorism, or the threat of boycotts, and other civil disturbances that are outside of our control. Any such disruptions could depress our earnings and have other material adverse effects on our business, financial condition and results of operations.

For example, during 2014 the landlord for our China facility informed us that the local village government in Shenzhen was exercising its right of eminent domain and that the lease for our facility would not be extended past its expiration in October 2014 due to zoning changes. Accordingly, we developed and executed a plan which we completed in 2015. Under the plan we found a replacement facility, entered into a five-year lease, negotiated compensation from the local government for our forfeited leasehold improvements and moving expenses, refurbished the replacement facility to meet our operational needs and relocated all of our operations and employees to the new facility. While this situation was handled on time, on plan and with no known disruption to our business, there can be no assurances that other situations posing such risks to the business will be successfully remediated to the same extent.

Reductions or delays in U.S. and foreign military spending could continue to have a material adverse effect on our business, financial condition and results of operations.

A significant portion of our revenues is derived from contracts with the U.S. and foreign militaries or OEMs that supply the U.S. and foreign militaries. In the years ended December 31, 2016 and 2015, approximately \$41,600 or 50% and \$42,700 or 56%, respectively, of our revenues were comprised of sales made directly or indirectly to the U.S. and foreign militaries.

While significant gains have been made in commercial markets with our Battery & Energy Products business, we are still highly dependent on sales to U.S. Government customers. The amounts and percentages of our net revenue that was derived from sales to U.S. Government customers, including the Department of Defense, whether directly or through prime contractors, was approximately \$33,600 or 41% in 2016 and \$36,700 or 48% in 2015. Therefore, any significant disruption or deterioration of our relationship with the U.S. Government or any prime defense contractor could still significantly reduce our revenue. Our competitors continuously engage in efforts to expand their business relationships with the U.S. Government and will continue these efforts in the future, and the U.S. Government may choose to use other contractors or suppliers.

Budget and appropriations decisions made by the U.S. Government, including possible future sequestration periods or other similar formulaic reductions in federal expenditures, are outside of our control and have long-term consequences for our business. A continued decline in U.S. military expenditures could result in a reduction in the military's demand for our products, which could have a material adverse effect on our business, financial condition and results of operations.

Any inability to comply with changes to the regulations for the shipment of our products could limit our ability to transport our products to customers in a cost-effective manner and reduce our operating income and margins.

The transportation of Lithium batteries is regulated by the International Civil Aviation Organization ("ICAO") and corresponding International Air Transport Association ("IATA") Dangerous Goods Regulations and the International Maritime Dangerous Goods Code ("IMDG") and in the U.S. by the Department of Transportation's Pipeline and Hazardous Materials Safety Administration ("PHMSA"). These regulations are based on the United Nations Recommendations on the Transport of Dangerous Goods Model Regulations and the United Nations Manual of Tests and Criteria. We currently ship our products pursuant to ICAO, IATA and PHMSA hazardous goods regulations. These regulations require companies to meet certain testing, packaging, labeling and shipping specifications for safety reasons. We have not incurred, and do not expect to incur, any significant costs in order to comply with these regulations. We believe we comply with all current U.S. and international regulations for the shipment of our products, and we intend and expect to comply with any new regulations that are imposed. We have established our own testing facilities to ensure that we comply with these regulations. If we are unable to comply with the new regulations, however, or if regulations are introduced that limit our ability to transport our products to customers in a cost-effective manner, this could reduce our operating income and margins, and have other material adverse effects on our business, financial condition and results of operations.

Our quarterly and annual results and the price of our common stock could fluctuate significantly.

Our future operating results may vary significantly from quarter-to-quarter and from year-to-year depending on factors such as the timing and shipment of significant orders, new product introductions, major project wins, U.S. and foreign government demand, delays in customer releases of purchase orders, delays in receiving raw materials from vendors, the mix of distribution channels through which we sell our products and services and general economic conditions. Frequently, a substantial portion of our revenue in each quarter is generated from orders booked and fulfilled during that quarter. As a result, revenue levels are difficult to predict for each quarter. If revenue results are below expectations, operating results will be adversely affected as we have a sizeable base of fixed overhead costs that do not fluctuate much with changes in revenue. Due to such variances in operating results, we have sometimes failed to meet, and in the future may not meet, market expectations regarding our future operating results.

In addition to the uncertainties of quarterly and annual operating results, future announcements concerning us or our competitors, including technological innovations or commercial products, litigation or public concerns as to the safety or commercial value of one or more of our products may cause the market price of our common stock to fluctuate substantially for reasons which may be unrelated to our operating results.

Any impairment of goodwill and indefinite-lived intangible assets, and other intangible assets, could negatively impact our results of operations.

Our goodwill and indefinite-lived intangible assets are subject to an impairment test on an annual basis and are also tested whenever events and circumstances indicate that goodwill and/or indefinite-lived intangible assets may be impaired. Any excess goodwill and/or indefinite-lived intangible assets value resulting from the impairment test must be written off in the period of determination. Intangible assets (other than goodwill and indefinite-lived intangible assets) are generally amortized over the useful life of such assets. In addition, from time to time, we may acquire or make an investment in a business which will require us to record goodwill based on the purchase price and the value of the acquired tangible and intangible assets. We may subsequently experience unforeseen issues with such business which adversely affect the anticipated results of the business or value of the intangible assets and trigger an evaluation of the recoverability of the recorded goodwill and intangible assets for such business. There is a possibility that our goodwill and other intangible assets, particularly in our Communications Systems business, could be impaired should there be a significant change in our internal forecasts and other assumptions we use in our impairment analysis. Future determinations of significant write-offs of goodwill or intangible assets as a result of an impairment test or any accelerated amortization of other intangible assets could have a negative impact, although not affecting cash, on our results of operations and financial condition.

We have completed our annual impairment analysis for goodwill and indefinite-lived intangible assets, in accordance with the applicable accounting guidance, and have concluded that we do not have any impairment of goodwill or intangible assets for the year ended December 31, 2016. Our impairment analysis was primarily focused on the goodwill and intangible assets pertaining to our Communications Systems business with particular emphasis on our McDowell Research Corporation trademark which was partially impaired in 2015 and passed by a relatively narrow margin in 2016. For the year ended December 31, 2015, we recorded a non-cash impairment amounting to \$150 of our McDowell Research Corporation trademark in our Communications Systems business. The non-cash impairment charge was caused by time delays in the awarding by government and defense customers in recent years of certain large projects in our pipeline. The aggregate goodwill and net book value of intangible assets amounted to \$27,159 and \$20,229 at December 31, 2016 and 2015, respectively. The year-over-year increase resulted from our acquisition of Accutronics in January 2016, which comprised \$7,259 of the year-end balance (goodwill of \$3,824 and intangible assets of \$3,435). For both years, our testing took into account our large opportunity pipeline for Communications Systems products as well as the maturity of the opportunities, and assumed the future award and estimated timing of certain major projects based on our knowledge of the status of these projects and the probability of award at the current time. Until an award is actually consummated and resulting purchase orders are issued, there are no guarantees that the underlying projects will contribute to revenues and operating income to justify the level of goodwill and intangible assets on our balance sheet. Accordingly, we will continue our practice of updating our analysis as warranted on an ongoing basis.

Breaches in security and other disruptions, could diminish our ability to generate revenues or contain costs and negatively impact our business in other ways.

We face certain security threats, including threats to our information technology infrastructure, attempts to gain access to our proprietary or classified information, and threats to physical and cyber security. Our information technology networks and related systems are critical to the operation of our business and essential to our ability to successfully perform day-to-day operations. The risks of a security breach, cyber attack, cyber intrusion, or disruption, particularly through actions taken by computer hackers, foreign governments and cyber terrorists, have increased as the number, intensity and sophistication of attempted attacks and intrusions from around the world have increased. Although we have acquired and developed systems and processes designed to protect our proprietary or classified information, they may not be sufficient and the failure to prevent these types of events could disrupt our operations, require significant management attention and resources, and could negatively impact our reputation among our customers and the public, which could have a negative impact on our financial condition, and weaken our results of operations and liquidity.

We are subject to certain safety risks, including the risk of fire, inherent in the manufacture, use and transportation of Lithium batteries.

Due to the high energy inherent in Lithium batteries, our Lithium batteries can pose certain safety risks, including the risk of fire. We incorporate procedures in research, development, product design, manufacturing processes and the transportation of Lithium batteries that are intended to minimize safety risks, but we cannot assure that accidents will not occur or that our products will not be subject to recall for safety concerns. Although we currently carry insurance policies which cover loss of the plant and machinery, leasehold improvements, inventory and business interruption, any accident, whether at the manufacturing facilities or from the use of the products, may result in significant production delays or claims for damages resulting from injuries or death. While we maintain what we believe to be sufficient casualty liability coverage to protect against such occurrences, these types of losses could reduce our operating income and have other material adverse effects on our business, financial condition and results of operation.

Negative publicity of Lithium ion batteries may negatively impact the industries or markets we operate in.

We are unable to predict the impact, severity or duration of negative publicity related to fire / mishandling of Lithium ion batteries or the environmental impact of their disposal, and how it may impact the industries or markets we serve. Ongoing negative attention being given to Lithium ion batteries that are used in certain cellular phones or are integrated into the power systems of new commercial aircraft and electric motor vehicles may have an impact on the Lithium ion battery industry as a whole, regardless of the design or usage of those batteries. The residual effects of such events could have an adverse effect on our business, financial condition, and results of operations.

Our growth and expansion strategy could strain or overwhelm our resources.

Rapid growth of our business could significantly strain management, operations and technical resources. If we are successful in obtaining rapid market growth of our products, we will likely be required to deliver large volumes of quality products to customers on a timely basis at a reasonable cost. For example, demand for our new or existing products combined with our ability to penetrate new markets and geographies or secure a major project award, could strain the current capacity of our manufacturing facilities and require additional capital resources, equipment and time to meet the required demand. We cannot assure, however, that our business will grow rapidly or that our efforts to expand manufacturing and quality control activities will be successful or that we will be able to satisfy commercial scale production requirements on a timely and cost-effective basis.

We also may be required to continue to improve our operations, management and financial systems and controls in order to remain competitive. The failure to manage growth and expansion effectively could have an adverse effect on our business, financial condition, and results of operations.

The loss of top management and key personnel could significantly harm our business, and our ability to put in place a succession plan and recruit experienced, competent management is critical to the success of the business.

The loss of top management and key personnel could significantly harm our business, and our ability to put in place a succession plan and recruit experienced, competent management is critical to the success of our business. The continuity of our officers and executive team is vital to the successful implementation of our business model and growth strategy designed to deliver sustainable, consistent profitability. A top management priority has been the development and implementation of a formal written succession plan to mitigate the risks associated with the loss of senior executives. There is no guarantee that we will be successful in our efforts to effectively implement our succession plan.

Because of the specialized, technical nature of our business, we are highly dependent on certain members of our management, sales, engineering and technical staffs. The loss of these employees could have a material adverse effect on our business, financial condition and results of operations. Our ability to effectively pursue our business strategy will depend upon, among other factors, the successful retention of our key personnel, recruitment of additional highly skilled and experienced managerial, sales, engineering and technical personnel, and the integration of such personnel obtained through business acquisitions. We cannot assure that we will be able to retain or recruit this type of personnel. An inability to hire sufficient numbers of people or to find people with the desired skills could result in greater demands being placed on limited management resources which could delay or impede the execution of our business plans and have other material adverse effects on our business, financial condition and results of operations.

Our supply of raw materials and components could be disrupted.

Certain materials and components used in our products are available only from a single or a limited number of suppliers. As such, some materials and components could become in short supply resulting in limited availability and/or increased costs. Additionally, we may elect to develop relationships with a single or limited number of suppliers for materials and components that are otherwise generally available. Due to our involvement with supplying defense products to the U.S. government, we could receive a government preference to continue to obtain critical supplies to meet military production needs. However, if the government did not provide us with a government preference in such circumstances, the difficulty in obtaining supplies could have a material adverse effect on our business, financial condition and results of operations. We believe that alternative suppliers are available to supply materials and components that could replace materials and components currently used and that, if necessary, we would be able to redesign our products to make use of such alternatives. However, any interruption in the supply from any supplier that serves as a sole source could delay product shipments and have a material adverse effect on our business, financial condition and results of operations. We have experienced interruptions of product deliveries by sole source suppliers in the past, and we cannot guarantee that we will not experience a material interruption of deliveries from sole source suppliers in the future. Of particular note is the increased demand for Lithium-based cells from the electric vehicle manufacturers. While this has resulted in increased supply of such cells, we continue to monitor our supply chain closely to ensure that any potential supply interruptions are minimized. Additionally, we could face increasing pricing pressure from our suppliers dependent upon volume due to rising costs by these suppliers that could be passed on to us in higher prices for our raw materials, which could increase our cost of business, lower our margins and have other materially adverse effects on our business, financial condition and results of operations.

We are subject to foreign currency fluctuations.

We maintain manufacturing operations in North America, Europe and China, and we export products to various countries. We purchase materials and sell our products in foreign currencies, and therefore currency fluctuations may impact our pricing of products sold and materials purchased. While the percentage of our business with customers outside of the U.S. slightly declined in 2015, sales to such customers still make up a significant percentage of our total revenues. For example, in 2016, 45% our sales were to customers outside of the U.S. as compared to 39% in 2015. The recent strengthening of the U.S. Dollar relative to our customers' currencies could make our products relatively more expensive to them, and may adversely affect our sales levels and reduce profitability. In addition, our United Kingdom and China subsidiaries maintain their books in local currency and the translation of the subsidiary financial statements into U.S. dollars for our consolidated financial statements could have an adverse effect on our consolidated financial results due to changes in local currency value relative to the U.S. dollar. Accordingly, currency fluctuations could have a material adverse effect on our business, financial condition and results of operations by increasing our expenses and reducing our income. Finally, we maintain certain domestic U.S. cash balances denominated in foreign currencies, and the U.S. dollar equivalent of these balances fluctuates with changes in the foreign exchange rates between these currencies and the U.S. dollar.

Our customers may not meet the volume expectations in our supply agreements.

We sell most of our products and services through supply agreements and contracts. While supply agreements and contracts contain volume-based pricing based on expected volumes, we cannot assure that adjustments to reflect volume shortfalls will be made under current industry practices because pricing is rarely adjusted retroactively when contract volumes are not achieved. Every effort is made to adjust future prices accordingly, but our ability to adjust prices is generally based on market conditions and we may not be able to adjust prices in various circumstances.

A finding that our proprietary and intellectual property rights are not enforceable or invalid could allow our competitors and others to produce competing products based on our proprietary and intellectual property or limit our ability to continue to manufacture and market our products.

We believe our success depends more on the knowledge, ability, experience and technological expertise of our employees than on the legal protection of patents and other proprietary rights. However, we claim proprietary rights in various unpatented technologies, know-how, trade secrets and trademarks relating to products and manufacturing processes. We cannot guarantee the degree of protection these various claims may or will afford, or that competitors will not independently develop or patent technologies that are substantially equivalent or superior to our technology. We protect our proprietary rights in our products and operations through contractual obligations, including nondisclosure agreements with certain employees, customers, consultants and strategic partners. There can be no assurance as to the degree of protection these contractual measures may or will afford. We have had patents issued and have patent applications pending in the U.S. and elsewhere. We cannot assure (1) that patents will be issued from any of these pending applications, or that the claims allowed under any issued patents will be sufficiently broad to protect our technology, (2) that any patents issued to us will not be challenged, invalidated or circumvented, or (3) as to the degree or adequacy of protection any patents or patent applications may or will afford. Further, if we are found to be infringing third party patents, we cannot assure that we will not be subjected to significant damages or will be able to obtain licenses with respect to such patents on acceptable terms, if at all. The failure to obtain necessary licenses could delay product shipments or the introduction of new products, and costly attempts to design around such patents could foreclose the development, manufacture or sale of products.

We are subject to the contract rules and procedures of the U.S. and foreign governments. These rules and procedures create significant risks and uncertainties for us that are not usually present in contracts with private parties.

We continue to develop battery products and communications systems to meet the needs of the U.S. and foreign governments. We compete in solicitations for awards of contracts. The receipt of an award, however, does not always result in the immediate release of an order and does not guarantee in any way any given volume of orders. Any delay of solicitations or anticipated purchase orders by, or future failure of, the U.S. or foreign governments to purchase products manufactured by us could have a material adverse effect on our business, financial condition and results of operations. In these scenarios we are also typically required to successfully meet contractual specifications and to pass various qualification-testing for the products under contract. Our inability to pass these tests in a timely fashion, as well as meet delivery schedules for orders released under contract, could have a material adverse effect on our business, financial condition and results of operations.

Additionally, when a U.S. government contract is awarded, there is a government procedure that permits unsuccessful companies to formally protest such award if they believe they were unjustly treated in the evaluation process. As a result of these protests, the government is precluded from proceeding under these contracts until the protests are resolved. A prolonged delay in the resolution of a protest, or a reversal of an award resulting from such a protest could have material adverse effects on our business, financial condition and results of operations.

We could be adversely affected by violations of the US Foreign Corrupt Practices Act (“FCPA”), the U.K. Bribery Act or other anti-corruption laws.

The FCPA, U.K. Bribery Act and other anti-corruption laws generally prohibit companies and their intermediaries from making improper payments (to foreign officials and otherwise) and require companies to keep accurate books and records and maintain appropriate internal controls. Our training program and policies mandate compliance with such laws. We operate in some parts of the world that have experienced governmental corruption to some degree, and, in certain circumstances, strict compliance with anti-bribery laws may conflict with local customs and practices. If we are found to be liable for violations of anti-corruption laws (either due to our own acts or our inadvertence, or due to the acts or inadvertence of others, including employees of our third party partners or agents), we could suffer from civil and criminal penalties or other sanctions, incur significant internal investigation costs and suffer reputational harm.

Our ability to use our net operating loss carry-forwards in the future may be limited, which could increase our tax liabilities and reduce our net income.

At December 31, 2016, we had approximately \$72 million of U.S. and \$13 million of U.K. net operating loss carry-forwards (“NOLs”) and \$2 million of U.S. tax credit carry-forwards available to offset future taxable income. We continually assess the carrying value of this asset based on the relevant accounting standards. As of December 31, 2016, we reflected a full valuation allowance against our deferred tax asset to the extent we are not able to be offset the asset by future reversing temporary differences. As we continue to assess the realizability of our deferred tax assets, the amount of the valuation allowance could be reduced. In addition, certain of our NOL carryforwards are subject to U.S. alternative minimum tax such that carryforwards can offset only 90% of alternative minimum taxable income. Achieving our business plan targets, particularly those relating to revenue and profitability, is integral to our assessment regarding the recoverability of our net deferred tax asset.

Compliance with government regulations regarding the use of "conflict minerals" may result in increased costs and risks to the company.

As part of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Act"), the SEC has promulgated disclosure requirements regarding the use of certain minerals, which are mined from the Democratic Republic of Congo and adjoining countries, known as conflict minerals. The disclosure rules were effective in May 2014. We are required to perform due diligence inquiries of our supply chain and publicly disclose whether we manufacture (as defined in the Act) any products that contain conflict minerals and could incur significant costs related to implementing a process that will meet the mandates of the Act. Additionally, customers typically rely on us to provide critical data regarding the parts they purchase, including conflict mineral information. Our material sourcing is broad-based and multi-tiered, and we may not be able to easily verify the origins for conflict minerals used in the products we sell. We have many suppliers and each provides conflict mineral information in a different manner, if at all. Accordingly, because the supply chain is complex, we may face reputational challenges if we are unable to sufficiently verify the origins of conflict minerals used in our products. Additionally, customers may demand that the products they purchase be free of conflict minerals. This may limit the number of suppliers that can provide products in sufficient quantities to meet customer demand or at competitive prices.

The U.S. and foreign governments can audit our contracts with their respective defense and government agencies and, under certain circumstances, can adjust the economic terms of those contracts.

A portion of our business comes from sales of products and services to the U.S. and foreign governments through various contracts. These contracts are subject to procurement laws and regulations that lay out policies and procedures for acquiring goods and services. The regulations also contain guidelines for managing contracts after they are awarded, including conditions under which contracts may be terminated, in whole or in part, at the government's convenience or for default. Failure to comply with the procurement laws or regulations can result in civil, criminal or administrative proceedings involving fines, penalties, suspension of payments, or suspension or disbarment from government contracting or subcontracting for a period of time.

We may incur significant costs because of known and unknown environmental matters.

National, state and local laws impose various environmental controls on the manufacture, transportation, storage, use and disposal of batteries and of certain chemicals used in the manufacture of batteries. We use and generate a variety of chemicals and other hazardous by-products in our manufacturing operations. These environmental laws govern, among other things, air emissions, wastewater discharges and the handling, storage and release of wastes and hazardous substances. Such laws and regulations can be complex and are subject to change. Although we believe that our operations are in substantial compliance with current environmental regulations and that, except as noted below, there are no environmental conditions that will require material expenditures for clean up at our present or former facilities or at facilities to which we have sent waste for disposal, there can be no assurance that changes in such laws and regulations will not impose costly compliance requirements on us or otherwise subject us to future liabilities. There can be no assurance that additional or modified regulations relating to the manufacture, transportation, storage, use and disposal of materials used to manufacture our batteries or restricting disposal of batteries will not be imposed, or as to how these regulations will affect our customers or us. Such changes in regulations could reduce our operating income and margins and have other material adverse effects on our business, financial condition and results of operations. We could incur substantial costs as a result of violations of environmental laws, including clean up costs, fines and sanctions and third-party property damage or personal injury claims. Failure to comply with environmental requirements could also result in enforcement actions that materially limit or otherwise affect the operations of the facilities involved. Under certain environmental laws, a current or previous owner or operator of an environmentally contaminated site may be held liable for the entire cost of investigation, removal or remediation of hazardous materials at such property. This liability could result whether or not the owner or operator knew of, or was responsible for, the presence of any hazardous materials.

The EU RoHS Directive places restrictions on the use of certain hazardous substances in electrical and electronic equipment. All applicable products sold in the European Union market after July 1, 2006 must comply with EU RoHS Directive. While this directive does not apply to batteries and does not currently affect our defense products, should any changes occur in the directive that would affect our products, we intend and expect to comply with any new regulations that are imposed. Our commercial chargers are in compliance with this directive. Additional European Union directives, entitled the Waste Electrical and Electronic Equipment ("WEEE") Directive and the Directive "on batteries and accumulators and waste batteries and accumulators", impose regulations affecting our non-defense products. These directives require that producers or importers of particular classes of electrical goods are financially responsible for specified collection, recycling, treatment and disposal of past and future covered products. These directives assign levels of responsibility to companies doing business in European Union markets based on their relative market share. These directives call on each European Union member state to enact enabling legislation to implement the directive. As additional European Union member states pass enabling legislation our compliance system should be sufficient to meet such requirements. Our current estimated costs associated with our compliance with these directives based on our current market share are not significant. However, we continue to evaluate the impact of these directives as European Union member states implement guidance, and actual costs could differ from our current estimates.

The EU Battery Directive is intended to cover all types of batteries regardless of their shape, volume, weight, material composition or use. It is aimed at reducing mercury, cadmium, lead and other metals in the environment by minimizing the use of these substances in batteries and by treating and re-using old batteries. This directive applies to all types of batteries except those used to protect European Member States' security, for military purposes, or sent into space. To achieve these objectives, the EU Battery Directive prohibits the marketing of some batteries containing hazardous substances. It establishes processes aimed at high levels of collection and recycling of batteries with quantified collection and recycling targets. The directive sets out minimum rules for producer responsibility and provisions with regard to labeling of batteries and their removability from equipment. Product markings are required for batteries and accumulators to provide information on capacity and to facilitate reuse and safe disposal. We currently ship our products pursuant to the requirements of the directive. Our current estimated costs associated with our compliance with these directives based on our current market share are not significant. However, we continue to evaluate the impact of these directives as European Union member states implement guidance, and actual costs could differ from our current estimates.

The China RoHS 2 directive provides a regulatory framework, including similar hazardous substance restrictions as are imposed by the EU RoHS Directive, and applies to methods for the control and reduction of pollution and other public hazards to the environment caused during the production, sale, and import of EEP in China affecting a broad range of electronic products and parts. The regulatory framework of China RoHS 2, also now references the updated marking and labeling requirements under Standard SJ/T 11364-2014 ("Marking Standard"). The methods under China RoHS 2 only apply to EEP placed in the marketplace in China. We believe *our compliance system is sufficient to meet our requirements under China RoHS 2. Our current estimated costs associated with our compliance with this regulation based on our current market share are not significant. However, we continue to evaluate the impact of this regulation, and actual costs could differ from our current estimates.*

A number of domestic and international communities are prohibiting the landfill disposal of batteries and requiring companies to make provisions for product recycling. Of particular note are the EU Batteries Directive and the New York State Rechargeable Battery Recycling Law. We are committed to responsible product stewardship and ongoing compliance with these and future statutes and regulations. The compliance costs associated with current recycling statutes and regulations are not expected to be significant at this time. However, we continue to evaluate the impact of these regulations, and actual costs could differ from our current estimates and additional laws could be enacted by these and other states which entail greater costs of compliance.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

As of December 31, 2016, we own two buildings in Newark, New York comprising approximately 250,000 square feet, which serve operations primarily in the Battery & Energy Products operating segment. Our corporate headquarters are located in our Newark, New York facility. We also lease approximately 97,000 square feet in two buildings on one campus in Shenzhen, China and approximately 25,000 square feet in six buildings in a contiguous area in Newcastle-under-Lyme, United Kingdom, which serve operations in the Battery & Energy Products operating segment. The Shenzhen, China campus location includes a dormitory facility. We lease approximately 32,500 square feet in a facility in Virginia Beach, Virginia, which serves operations in the Communications Systems operating segment. We also lease sales and administrative offices, as well as manufacturing and production facilities, in India, which serve operations in the Battery & Energy Products operating segment. Our research and development efforts for our Battery & Energy Products are conducted at our Newark, New York, Newcastle-under-Lyme, United Kingdom and Shenzhen, China facilities, while our research and development efforts for our Communications Systems products are conducted in Tallahassee, Florida and at our facility in Virginia Beach, Virginia. We believe that our facilities are adequate and suitable for our current needs. However, we may require additional manufacturing and administrative space if demand for our products and services grows.

ITEM 3. LEGAL PROCEEDINGS

We are subject to legal proceedings and claims that arise in the normal course of business. We believe that the final disposition of such matters will not have a material adverse effect on our financial position, results of operations or cash flows.

Dreamliner Litigation

In July 2013, an unoccupied Boeing 787 Dreamliner aircraft operated by Ethiopian Airlines (“EA”) was damaged by a fire while parked at London Heathrow Airport. We participated in and provided technical assistance in support of an investigation of this incident conducted by U.K. and U.S. regulatory authorities as well as by the manufacturer of the aircraft, as we are one of many downstream suppliers to that manufacturer. A final report was issued by the Air Accidents Investigative Branch - - UK Civil Aviation regulatory authority, with findings indicating that the fire was primarily caused by circumstances related to the plane’s emergency locator transmitter (“ELT”) manufactured and installed by another company.

A component of the ELT is a battery pack which incorporates Ultralife’s industry-standard Lithium Manganese Dioxide non-rechargeable D-cell. Ultralife has had this cell in production since 2001, with millions of units produced. The cell is widely-used for global defense and commercial applications. This battery product has gone through rigorous safety and qualification testing, including United Nations Transport of Dangerous Goods, Manual of Tests and Criteria, and is authorized for use in aerospace applications under Technical Standard Order C142.

On May 4, 2015, we were notified of a lawsuit in which we were named, along with other suppliers to the aircraft manufacturer, concerning that 2013 fire. The suit was filed by EA in the Commercial Court, Queen’s Bench Division of the High Court of Justice, London and seeks as damages \$42,000 plus other unspecified amounts, including those for loss of use and diminution in value of the aircraft. We maintain liability and products liability insurance through reputable providers, and in accordance with our corporate practices, immediately advised and referred this matter to our insurers. We are working with those insurers and their counsel to actively defend against this action, which is ongoing.

At this time, we believe that there is not a reasonable possibility that this incident will result in a material financial exposure to the Company.

Arista Power Litigation

Since September 2011, we have been pursuing legal action against Arista Power, Inc. (“Arista”) and our former employee, David Modeen, for, among other things, alleged breach of certain agreements, duties and obligations, including misappropriation of our confidential information and trade secrets, tortious interference, and breach of contract. On January 12, 2016, Arista filed for liquidation under Chapter 7 of the bankruptcy laws of the United States, without accurately identifying our ongoing lawsuit against them. Although we have not withdrawn our lawsuit, nor has it been dismissed, the Company did not submit a Proof of Claim in connection with Arista’s bankruptcy filing, nor does it intend to actively pursue its claims against Arista at this time.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

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

Market Information

Ultralife's common stock is listed on the NASDAQ Global Market under the symbol "ULBI."

The following table sets forth the quarterly high and low closing sales prices of our common stock during 2015 and 2016:

| | Closing Sales Prices | |
|----------------------------------|----------------------|---------|
| | High | Low |
| 2015: | | |
| Quarter ended March 29, 2015 | \$ 3.99 | \$ 3.00 |
| Quarter ended June 28, 2015 | \$ 4.40 | \$ 3.56 |
| Quarter ended September 27, 2015 | \$ 5.45 | \$ 3.90 |
| Quarter ended December 31, 2015 | \$ 7.49 | \$ 5.28 |
| 2016: | | |
| Quarter ended March 27, 2016 | \$ 6.51 | \$ 4.95 |
| Quarter ended June 26, 2016 | \$ 5.85 | \$ 3.76 |
| Quarter ended September 25, 2016 | \$ 5.05 | \$ 3.95 |
| Quarter ended December 31, 2016 | \$ 5.05 | \$ 3.92 |

Holdings

As of February 9, 2017, there were approximately 3,000 registered holders of record of our common stock.

Purchases of Equity Securities by the Issuer

On April 28, 2014, the Company's Board of Directors approved a share repurchase program (the "Share Repurchase Program") which became effective on May 1, 2014 and under which the Company was authorized to repurchase up to 1.8 million shares of its outstanding common stock over a period not to exceed twelve months. The Share Repurchase Program was extended through June 2, 2016, and the maximum number of shares authorized to be repurchased under the program was increased to 3.4 million shares.

Share repurchases under this program were made in accordance with SEC Rule 10b-18 using a variety of methods, which included open market purchases and block trades in compliance with applicable insider trading and other securities laws and regulations. With the exception of repurchases made during stock trading black-out periods under 10b5-1 Plans, the timing, manner, price and amount of any repurchases were determined at the Company's discretion. The Share Repurchase Program expired on June 2, 2016 and did not obligate the Company to repurchase any specific number of shares.

In 2016, we repurchased a total of 156,092 shares of our common stock for an aggregate consideration of \$630, of which 149,904 shares were repurchased under the Share Repurchase Program for an aggregate amount (excluding fees and commissions) of \$603. In 2015, we repurchased a total of 2,258,929 shares of our common stock for an aggregate consideration of \$9,388, of which 2,225,437 shares were repurchased under the Share Repurchase Program for an aggregate amount (excluding fees and commissions) of \$9,162.

From the inception of the Share Repurchase Program on May 1, 2014 through its expiration on June 2, 2016, the Company repurchased 2,592,095 shares for an aggregate cost (excluding fees and commissions) of \$10,480.

The following table sets forth information regarding 2016 purchases of our common stock under this program:

| | Total Number of Shares Purchased | Average Price Paid Per Share | Total Number of Shares Purchased As Part of Publicly Announced Program | Maximum Number of Shares That May Yet Be Purchased Under the Program |
|----------------|---|---|---|---|
| Total for 2016 | 149,904 | \$ 4.02 | 2,592,095 | - |

Dividends

We have never declared or paid any cash dividends on our capital stock. Pursuant to our current credit facility, we are precluded from paying any dividends. We intend to retain earnings, if any, to finance future operations and expansion and, therefore, do not anticipate paying any cash dividends in the foreseeable future. Any future payment of dividends will depend upon our financial condition, capital requirements and earnings, as well as upon other factors that our Board of Directors may deem relevant.

ITEM 6. SELECTED FINANCIAL DATA

As a smaller reporting company, we are not required to provide this information.

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

7.

The following discussion and analysis should be read in conjunction with the accompanying Consolidated Financial Statements and Notes thereto appearing elsewhere in this Form 10-K.

The financial information in this Management's Discussion and Analysis of Financial Condition and Results of Operations is presented in thousands of dollars, except for share and per share amounts. All figures presented below represent results from continuing operations, unless otherwise specified.

General

We offer products and services ranging from power solutions to communications and electronics systems to customers across the globe in the government, defense and commercial sectors. With an emphasis on strong engineering and a collaborative approach to problem solving, we design, manufacture, install and maintain power and communications systems including rechargeable and non-rechargeable batteries, communications and electronics systems and accessories and custom engineered systems. We sell our products worldwide through a variety of trade channels, including original equipment manufacturers ("OEMs"), industrial and defense supply distributors and directly to U.S. and international defense departments.

We report our results in two operating segments: Battery & Energy Products and Communications Systems. The Battery & Energy Products segment includes Lithium 9-volt, cylindrical, thin cell and various other non-rechargeable batteries, in addition to rechargeable batteries, uninterruptable power supplies, charging systems and accessories, such as cables. The Communications Systems segment includes RF amplifiers, power supplies, cable and connector assemblies, amplified speakers, equipment mounts, case equipment, integrated communication system kits and communications and electronics systems design. We believe that reporting performance at the gross profit level is the best indicator of segment performance. As such, we report segment performance at the gross profit level and operating expenses as Corporate charges.

We continually evaluate ways to grow, including opportunities to expand through mergers, acquisitions and joint ventures, which can broaden the scope of our products and services, expand operating and market opportunities and provide the ability to enter new lines of business synergistic with our portfolio of offerings.

During 2014, we elected to terminate our lease for our U.K. service office and repair facility that was to have expired in May 2018. The termination of this lease was effective as of January 31, 2015.

In January 2016, we acquired Accutronics Limited ("Accutronics"), a U.K. corporation based in Newcastle-under-Lyme, U.K., a leading independent designer and manufacturer of smart batteries and charger systems for high-performance, feature-laden portable and handheld electronic devices.

Currently, we do not experience significant seasonal sales trends in any of our operating segments, although sales to the U.S. Defense Department and other international defense organizations can be sporadic based on the needs of those particular customers.

Consolidated revenues increased by \$6,033 or 7.9% to \$82,460 for the year ended December 31, 2016 compared to \$76,427 for the year ended December 31, 2015. During 2016, we experienced revenue growth of 58.7% for our Communications Systems business and a revenue decline of 0.8% for our Battery & Energy Products business. This 2016 performance reflected a \$7,519 or 22.5% increase in sales to our commercial customers and a \$1,486 or 3.5% decrease in sales to our government and defense customers. The increase in commercial sales reflects our acquisition of Accutronics in January 2016, which partially offset the year earlier sales demand for our 9-Volt batteries from large global smoke detector OEM's to comply with legislation and trends in a certain European Union country for products lasting ten years and large shipments of batteries to service the metering and toll pass industries in China. Sales to medical customers in the 2016 period increased by 47.4% over 2015 when excluding Accutronics and almost doubled when including Accutronics. Medical sales comprised 26.5% of total sales in 2016 compared to 10.2% for 2015. The decrease in government and defense sales primarily reflected lower demand from a large, global defense prime contractor for our batteries and chargers and lower battery sales to the U.S. Defense of Defense partially offset by higher revenues from our Communications Systems business driven by shipments of Vehicle Installed Power Enhanced Rifleman Appliqué ("VIPER") systems to fulfill contracts awarded in 2015 and 2016.

Gross margin decreased to 30.4% for the year ended December 31, 2016, as compared to 30.5% for the year ended December 31, 2015. The 10 basis point decline was due primarily to product mix in our Communications Systems business segment and a one-time adjustment to increase the opening inventory of Accutronics to fair market value in accordance with purchase accounting.

Operating expenses increased by \$1,359 or 6.8% to \$21,345 during the year ended December 31, 2016, compared to \$19,986 during the year ended December 31, 2015. This increase was fully attributable to the acquisition of Accutronics on January 13, 2016, which contributed operating expenses of \$2,882 in 2016, including \$203 of one-time direct acquisition costs and \$323 of intangible asset amortization. Excluding Accutronics results, operating expenses decreased \$1,523 or 7.6% due primarily to strict control over discretionary spending, while focusing on the development of new products and revenue growth. Operating expenses as a percentage of revenues decreased from 26.2% in 2015 to 25.9% in 2016 due to the combination of higher revenues and lower expenses in 2016.

Net income attributable to Ultralife was \$3,509, or \$0.23 per basic share (\$0.23 per diluted share) for the year ended December 31, 2016, compared to \$2,869 or \$0.18 per basic share (\$0.17 per diluted share) for the year ended December 31, 2015.

Adjusted EBITDA, defined as net income (loss) attributable to Ultralife before net interest expense, provision (benefit) for income taxes, depreciation and amortization, plus/minus expenses/income that we do not consider reflective of our continuing operations, amounted to \$7,502 for the year ended December 31, 2016 compared to \$6,966 for the prior period. See the section "Adjusted EBITDA" beginning on page 30 for a reconciliation of Adjusted EBITDA to net income attributable to Ultralife.

As a result of careful working capital management and cash generated from operations, our liquidity remains solid with total cash of \$10,706, a decrease of \$3,827 from the cash position of \$14,533 as of December 31, 2015. The decrease reflects the January 2016 acquisition of Accutronics utilizing cash of \$11,161 and the completion of our Share Repurchase Program with the repurchase of 149,904 shares for \$603, partially offset by our operating performance and inventory reduction. We had no debt as of December 31, 2016 or December 31, 2015.

For the year, we achieved our stated goal of generating profitable growth, posting 13% operating income growth on an 8% revenue increase. As we look ahead to 2017, an improving backlog and disciplined execution of our business model while continuing to invest in market and sales reach expansion and new product development, positions us well to further diversify beyond our core U.S. government/defense business and achieve another year of profitable growth.

Results of Operations

Year Ended December 31, 2016 Compared With the Year Ended December 31, 2015:

| | Year Ended December 31, | | Increase/ (Decrease) |
|--|-------------------------|------------|-------------------------|
| | 2016 | 2015 | |
| Revenues: | | | |
| Battery & Energy Products | \$ 64,753 | \$ 65,272 | \$ (519) |
| Communications Systems | 17,707 | 11,155 | 6,552 |
| Total | 82,460 | 76,427 | 6,033 |
| Cost of Products Sold: | | | |
| Battery & Energy Products | 45,173 | 46,574 | (1,401) |
| Communications Systems | 12,179 | 6,537 | 5,642 |
| Total | 57,352 | 53,111 | 4,241 |
| Gross Profit: | | | |
| Battery & Energy Products | 19,580 | 18,698 | 882 |
| Communications Systems | 5,528 | 4,618 | 910 |
| Total | 25,108 | 23,316 | 1,792 |
| Operating Expenses | 21,345 | 19,986 | 1,359 |
| Operating Income | 3,763 | 3,330 | 433 |
| Other Expense, Net | (183) | (180) | 3 |
| Income Before Taxes | 3,580 | 3,150 | 430 |
| Income Tax Provision | 98 | 310 | (212) |
| Net Income | 3,482 | 2,840 | 642 |
| Net Loss Attributable to Non-Controlling Interest | 27 | 29 | (2) |
| Net Income Attributable to Ultralife | \$ 3,509 | \$ 2,869 | \$ 640 |
| Net Income Attributable to Ultralife Common Shares – Basic | \$ 0.23 | \$ 0.18 | \$ 0.05 |
| Net Income Attributable to Ultralife Common Shares – Diluted | \$ 0.23 | \$ 0.17 | \$ 0.06 |
| Weighted Average Shares Outstanding – Basic | | | |
| | 15,261,000 | 16,182,000 | (921,000) |
| Weighted Average Shares Outstanding – Diluted | | | |
| | 15,405,000 | 16,458,000 | (1,053,000) |

Revenues. Total revenues for the year ended December 31, 2016 amounted to \$82,460, an increase of \$6,033, or 7.9% from the \$76,427 reported for the year ended December 31, 2015.

Battery & Energy Products revenues decreased \$519, or 0.8%, for the year ended December 31, 2016. Commercial revenues of this business increased \$7,519, or 22.5%, over 2015 and now comprise 62.6% of total segment sales versus 51.1% last year. The year-over-year increase resulted from the inclusion of Accutronics sales in the amount of \$10,362 and an increase in core medical sales, which offset the year-earlier demand for our 9-Volt batteries from large global smoke detector OEM's to comply with legislation and trends in a certain European Union country for products lasting ten years and large shipments of batteries to service the metering and toll pass industries in China. Government and defense sales of this business decreased \$8,038, or 25.2%, from 2015 and now comprise 36.6% of total segment sales versus 48.9% last year. The year-over-year decline was due primarily to the lower battery and charger shipments to a large international prime defense supplier and lower shipments of primary batteries to the U.S. Department of Defense in 2016.

Communications Systems revenues increased \$6,552, or 58.7%, for the year ended December 31, 2016. The increase resulted from fulfillment of orders through an OEM to the U.S. Army of the Vehicle Installed Power Enhanced Rifleman Appliqué (“VIPER”) following our September 2015 award of an \$8.2 million contract and an October 2016 follow-up award for \$2.2 million. The shipments of VIPER systems more than offset a decrease in core product sales due to closing and funding delays associated with some orders which are expected to ship in 2017.

Our order backlog at December 31, 2016 was approximately \$26,200, a decrease of approximately \$700 from the backlog at December 31, 2015, which was \$26,900. The decrease is primarily due to the award of an \$8,200 order through an OEM for the U.S. Army for our new MRC product – Vehicle Installed Power Enhanced Rifleman Appliqué (“VIPER”) in 2015 that was shipped in 2016, which offset backorders associated with our acquisition of Accutronics, and higher demand for batteries and power supplies from large U.S.-based global defense contractors and a global medical products OEM. Our backlog at December 31, 2016 is expected to ship throughout 2017.

Cost of Products Sold and Gross Profit. Cost of products sold for the year ended December 31, 2016 increased \$4,241, or 8.0%, from the year ended December 31, 2015. Consolidated cost of products sold as a percentage of total revenue increased from 69.5% for the year ended December 31, 2015 to 69.6% for the year ended December 31, 2016. Correspondingly, consolidated gross margin was 30.4% for the year ended December 31, 2016, compared with 30.5% for the year ended December 31, 2015. The 10 basis point decline in gross margin is due primarily to product mix impacting the Communications Systems segment and a one-time adjustment to increase the opening inventory of Accutronics to fair market value in accordance with purchase accounting.

For our Battery & Energy Products segment, the cost of products sold decreased \$1,401 or 3.0%, from the year ended December 31, 2015. Battery & Energy Products’ gross profit for 2016 was \$19,580 or 30.2% of revenues, an increase of \$882 or 4.7% from gross profit of \$18,698, or 28.6% of revenues, for 2015. As a result, Battery & Energy Products’ gross margin as a percentage of revenues increased for the year ended December 31, 2016 by 160 basis points over the prior year, reflecting favorable product mix including the higher overall gross margins recognized for Accutronics high value proposition products.

For our Communications Systems segment, the cost of products sold increased by \$5,642 or 86.3% from the year ended December 31, 2015. Communications Systems’ gross profit for the year ended December 31, 2016 was \$5,528 or 31.2% of revenues, an increase of \$910 or 19.7% from gross profit of \$4,618 or 41.4% of revenues, for the year ended December 31, 2015. The 1,020 basis points decrease in gross margin as a percentage of revenue during 2016 is due to sales product mix primarily related to the high volume initial VIPER award.

Operating Expenses. Total operating expenses for the year ended December 31, 2016 increased \$1,359 or 6.8% from the year ended December 31, 2015. This increase was primarily attributable to the acquisition of Accutronics on January 13, 2016, which contributed operating expenses of \$2,882 in 2016, including \$203 of one-time direct acquisition costs and \$323 of intangible asset amortization. Excluding Accutronics results, operating expenses decreased \$1,523 or 7.6% due primarily to strict control over non-revenue related discretionary spending, while focusing on the development of new products and revenue growth.

Overall, operating expenses as a percentage of revenues were 25.9% for the year ended December 31, 2016 compared to 26.2% for the comparable 2015 period. Amortization expense associated with intangible assets related to our acquisitions increased to \$503, including \$323 for Accutronics, for the year ended December 31, 2016 (\$303 in selling, general and administrative expenses and \$200 in research and development costs), compared with \$235 for the year ended December 31, 2015 (\$105 in selling, general, and administrative expenses and \$130 in research and development costs). Research and development costs were \$5,946 in 2016, an increase of \$343, or 6.1%, from \$5,603 reported in 2015. The increase is comprised of \$534 of research and development costs (including intangible asset amortization of \$106) incurred by Accutronics, partially offset by a decrease of \$191 primarily representing discretionary spending reductions. Selling, general, and administrative expenses increased \$1,166 or 8.2%, from \$14,233 for the year ended December 31, 2015 to \$15,399 for the year ended December 31, 2016. The increase is fully attributable to the inclusion of Accutronics results and the one-time direct acquisition costs which contributed \$2,348 (including intangible asset amortization of \$217) of selling, general and administrative expenses for the 2016 period, partially offset by continued actions in the core businesses to reduce discretionary expenses. For 2015, we recorded a non-cash impairment charge of \$150 to reduce the book value of our McDowell Research Corporation trademark. The 2015 trademark impairment charge was based on compliance with U.S. Generally Accepted Accounting Principles (“U.S. GAAP”), and resulted from taking into account timing delays in the awarding by government/defense customers in recent years of certain large projects in our Communications Systems pipeline.

Other Income (Expense). Other (expense) totaled (\$183) for the year ended December 31, 2016 compared to (\$180) for the year ended December 31, 2015. Interest and financing expense, net of interest income, increased \$18 to \$263 for 2016 from \$245 for 2015, as a result of one-time costs of \$48 associated with the acquisition of Accutronics. Miscellaneous income amounted to \$80 for 2016 compared with \$65 for 2015, primarily due to transactions impacted by foreign currency fluctuation between the U. S. Dollar, Pound Sterling and the Euro.

Income Taxes. We recorded a tax provision of \$98 for the year ended December 31, 2016 compared with a tax provision of \$310 for the year ended December 31, 2015. The December 31, 2016 provision is primarily due to the income reported for our United Kingdom operations including Accutronics, state taxes and the recognition of deferred tax liabilities generated from the amortization of goodwill and certain intangible assets for tax purposes that cannot be predicted to reverse for book purposes during our loss carryforward periods. The December 31, 2015 provision is primarily due to the income reported for our China and United Kingdom operations during the periods, the estimated provision for U.S. federal alternative minimum tax liability, state taxes, and the recognition of deferred tax liabilities generated from the amortization of goodwill and certain intangible assets for tax purposes that cannot be predicted to reverse for book purposes during our loss carry-forward periods. The year-over-year decrease is primarily attributable to the amounts and geographic mix of earnings and an excess accrual of income taxes from prior years. In 2015, the tax provision was reduced by a deferred tax benefit amounting to \$51 relating to our \$150 impairment of a trademark. The effective consolidated tax rates for the years ended December 31, 2016 and 2015 were as follows:

| | Years Ended December 31, | |
|--------------------------------|---------------------------------|-------------|
| | 2016 | 2015 |
| Income Before Income Taxes (a) | \$ 3,580 | \$ 3,150 |
| Income Tax Provision (b) | 98 | 310 |
| Effective Rate (b) / (a) | 2.7% | 9.8% |

In 2016 and 2015, in the U.S. and certain operations in the U.K., we continue to report a valuation allowance for our deferred tax assets we believe cannot be offset by reversing temporary differences because based on past history, it is more likely than not that we would not utilize our U.S. and U.K. net operating losses (“NOLs”) that had accumulated over time before their expiration. The recognition of a valuation allowance on our deferred tax assets resulted from our evaluation of all available evidence, both positive and negative. The assessment of the realizability of the NOLs was based on a number of factors including, our history of operating losses, the volatility of our earnings, our historical operating volatility, our historical inability to accurately forecast earnings for future periods and the continued uncertainty of the general business climate. We concluded that these historical factors represent sufficient negative evidence and have concluded that we should continue to have a full valuation allowance against our net deferred tax assets. (See Notes 1 and 9 in the Notes to Consolidated Financial Statements for additional information.)

In addition, certain of our NOL carry-forwards are subject to U.S. alternative minimum tax such that carry-forwards can offset only 90% of alternative minimum taxable income. The use of our U.K. NOL carryforwards may be limited due to the change in the U.K. operation during 2008 from a manufacturing and assembly center to primarily a distribution and service center.

Net Income Attributable to Ultralife. Net income attributable to Ultralife and income attributable to Ultralife common shareholders per diluted share was \$3,509 and \$0.23, respectively, for the year ended December 31, 2016, compared to \$2,869 and \$0.17, respectively, for the year ended December 31, 2015 as a result of the reasons described above. The 2016 period was impacted by the purchase accounting adjustments and non-recurring costs totaling \$343 related to the acquisition of Accutronics, equivalent to \$0.02 per share. Average common shares outstanding used to compute diluted earnings per share decreased from 16,458,000 in the 2015 period to 15,405,000 in the 2016 period, mainly due to the repurchase of shares under the Company’s Share Repurchase Program (see Note 3 to our Consolidated Financial Statements) partially offset by stock option exercises.

Adjusted EBITDA

In evaluating our business, we consider and use Adjusted EBITDA, a non-GAAP financial measure, as a supplemental measure of our operating performance. We define Adjusted EBITDA as net income (loss) attributable to Ultralife before net interest expense, provision (benefit) for income taxes, depreciation and amortization, plus/minus expenses/income that we do not consider reflective of our ongoing operations. We use Adjusted EBITDA as a supplemental measure to review and assess our operating performance and to enhance comparability between periods. We also believe the use of Adjusted EBITDA facilitates investors’ use of operating performance comparisons from period to period and company to company by backing out potential differences caused by variations in such items as capital structures (affecting relative interest expense and stock-based compensation expense), the book amortization of intangible assets (affecting relative amortization expense), the age and book value of facilities and equipment (affecting relative depreciation expense) and other significant non-operating expenses or income. We also present Adjusted EBITDA because we believe securities analysts, investors and other interested parties frequently use it as a measure of financial performance. We reconcile Adjusted EBITDA to net income (loss) attributable to Ultralife, the most comparable financial measure under U.S. GAAP.

We use Adjusted EBITDA in our decision-making processes relating to the operation of our business together with U.S. GAAP financial measures such as income (loss) from operations. We believe that Adjusted EBITDA permits a comparative assessment of our operating performance, relative to our performance based on our U.S. GAAP results, while isolating the effects of depreciation and amortization, which may vary from period to period without any correlation to underlying operating performance, and of non-cash stock-based compensation, which is a non-cash expense that varies widely among companies. We believe that by presenting Adjusted EBITDA, we assist investors in gaining a better understanding of our business on a going forward basis. We provide information relating to our Adjusted EBITDA so that securities analysts, investors and other interested parties have the same data that we employ in assessing our overall operations. We believe that trends in our Adjusted EBITDA are a valuable indicator of our operating performance on a consolidated basis and of our ability to produce operating cash flows to fund working capital needs, to service debt obligations and to fund capital expenditures.

The term Adjusted EBITDA is not defined under U.S. GAAP, and is not a measure of operating income, operating performance or liquidity presented in accordance with U.S. GAAP. Our Adjusted EBITDA has limitations as an analytical tool, and when assessing our operating performance, Adjusted EBITDA should not be considered in isolation or as a substitute for net income (loss) attributable to Ultralife or other consolidated statement of operations data prepared in accordance with U.S. GAAP. Some of these limitations include, but are not limited to, the following:

- a. Adjusted EBITDA does not reflect (1) our cash expenditures or future requirements for capital expenditures or contractual commitments; (2) changes in, or cash requirements for, our working capital needs; (3) the interest expense, or the cash requirements necessary to service interest or principal payments, on our debt; (4) income taxes or the cash requirements for any tax payments; and (5) all of the costs associated with operating our business;
- b. although depreciation and amortization are non-cash charges, the assets being depreciated and amortized often will have to be replaced in the future, and Adjusted EBITDA does not reflect any cash requirements for such replacements;
- c. while stock-based compensation is a component of cost of products sold and operating expenses, the impact on our consolidated financial statements compared to other companies can vary significantly due to such factors as assumed life of the stock-based awards and assumed volatility of our common stock; and
- d. other companies may calculate Adjusted EBITDA differently than we do, limiting its usefulness as a comparative measure.

We compensate for these limitations by relying primarily on our U.S. GAAP results and using Adjusted EBITDA only on a supplemental basis. Adjusted EBITDA is calculated as follows for the periods presented:

| | Years ended December 31, | |
|---|---------------------------------|-----------------|
| | 2016 | 2015 |
| Net Income Attributable to Ultralife | \$ 3,509 | \$ 2,869 |
| Add: | | |
| Interest Expense, Net | 263 | 245 |
| Income Tax Provision | 98 | 310 |
| Depreciation and Amortization of Financing Fees | 2,294 | 2,472 |
| Amortization of Intangible Assets | 503 | 235 |
| MRC Trademark Impairment | - | 150 |
| Stock-Based Compensation Expense | 710 | 571 |
| Non-Cash Purchase Accounting Adjustment | 96 | - |
| Loss on Asset Disposal and Other | 29 | 114 |
| Adjusted EBITDA | \$ 7,502 | \$ 6,966 |

Liquidity and Capital Resources

Cash Flows and General Business Matters

As of December 31, 2016, cash totaled \$10,706 (including restricted cash of \$77), a decrease of \$3,827 from the beginning of the year primarily attributable to the Company's acquisition of Accutronics. During the year ended December 31, 2016, we generated \$7,653 of cash from operating activities as compared to \$8,551 of cash for the year ended December 31, 2015, a decrease of \$898. In 2016, the cash generated from operating activities was a result of our net income of \$3,482 plus an add-back of \$3,536 for non-cash expenses of depreciation, amortization, and stock-based compensation. Working capital changes accounted for \$635 of the operating cash generation, due mainly to a decrease in inventory, offset by an increase in accounts receivable and a decline in our accounts payable and other liabilities. In 2015, the cash generated from operating activities resulted from our net income of \$2,840 plus an add-back of \$3,542 for non-cash expenses of depreciation, amortization, loss on disposal of equipment and improvements, and stock-based compensation. Working capital changes accounted for \$2,169 of the operating cash generation, due mainly to a decrease in inventory.

We used \$11,011 in cash for investing activities during 2016 compared with \$2,910 in cash used for investing activities in 2015. The Company acquired Accutronics in 2016 utilizing cash of \$11,161, which was partially offset by the cash acquired from Accutronics of \$1,304. Cash paid for capital expenditures totaled \$1,219 and \$2,910 in 2016 and 2015, respectively. The year-over-year decrease in cash paid for capital expenditures was due primarily to the 2015 payment for test equipment of pertaining to our Communications business that was installed in 2014. Restricted cash was reduced by \$65 and funded to operating cash in 2016 in accordance with the terms of an international 2015 contract.

We used \$173 in cash for financing activities during 2016, compared to \$8,868 in cash for financing activities during 2015. We spent \$607 to repurchase treasury stock under the Company's Share Repurchase Program in 2016 compared to \$9,388 in 2015, and we received \$461 and \$538 in 2016 and 2015, respectively, in funds from the issuance of common stock in connection with the exercise of stock options by our employees. In 2016 and 2015, we used \$27 and \$18, respectively, for tax withholdings related to stock-based awards.

Although we carry a full reserve for our deferred tax asset as of both December 31, 2016 and 2015, we continue to have significant U.S. NOLs available to us to utilize as an offset to taxable income. As of December 31, 2015, none of our U.S. NOLs have expired. See Note 9 in our Notes to the Consolidated Financial Statements for additional information.

Inventory turnover for the year ended December 31, 2016 averaged 2.1 turns, identical to 2015.

As of December 31, 2016, we had made commitments to purchase approximately \$504 of production machinery and equipment, which we expect to fund through operating cash flows.

In January 2016, we acquired Accutronics Limited ("Accutronics") as disclosed in Note 2 to our Consolidated Financial Statements. The purchase price of £7,708 million (approximately \$11.2 million) was funded out of our cash. Based on operating cash flows and working capital management, including reductions in discretionary spending and further reductions of inventory, a large portion of the cash used was restored over the course of 2016.

Debt and Lease Commitments

On May 24, 2013, we entered into a Revolving Credit, Guaranty and Security Agreement (the "Credit Agreement") and related security agreements with PNC Bank, National Association ("PNC") to establish a \$20 million secured asset-based revolving credit facility that includes a \$1 million letter of credit subfacility (the "Credit Facility"). The Credit Agreement provides that the Credit Facility may be increased with PNC's concurrence to \$35 million prior to the last six months of the term and expires on May 24, 2017. The Credit Facility replaces the prior credit facility with RBS Business Capital, a division of RBS Asset Finance, Inc., which expired in accordance with its terms on May 15, 2013, with no debt outstanding.

Our available borrowing limit under the Credit Facility fluctuates from time to time based on a borrowing base formula equal to the sum of up to 85% of eligible accounts receivable plus the least of (a) up to 65% of the eligible inventory and eligible foreign in-transit inventory, (b) up to 85% of the appraised net orderly liquidation value of eligible inventory and eligible foreign in-transit inventory, and (c) \$7.5 million, in each case subject to the definitions in the Credit Agreement and reserves required by PNC.

Interest is payable quarterly and will accrue on outstanding indebtedness under the Credit Agreement at the alternate base rate, as defined in the Credit Agreement, plus the applicable margin or at the one, two or three month LIBOR rate plus the applicable margin as selected by us from time to time and listed below.

| Quarterly Average Undrawn Borrowing Availability | Applicable Margin for Alternate Base Rate Loans | Applicable Margin for LIBOR Rate Loans |
|---|--|---|
| Greater than \$8,000,000 | 1.00% | 2.00% |
| \$5,000,000 up to \$8,000,000 | 1.25% | 2.25% |
| Less than \$5,000,000 | 1.50% | 2.50% |

We must pay a fee on the Credit Facility's unused availability of 0.375% per annum and customary letter of credit fees in addition to various collateral monitoring and related fees and expenses.

In addition to customary affirmative and negative covenants, we must maintain a fixed charge coverage ratio as defined in the Credit Agreement of 1:15 to 1:00 tested quarterly for the four-quarters then ended. For the years ended December 31, 2016 and 2015, we were in compliance with all covenants. The Credit Facility is secured by substantially all our assets.

Any outstanding advances must be repaid upon expiration of the term of the Credit Facility. Payments must be made during the term to the extent outstanding advances exceed the maximum amount then permitted to be drawn as advances under the Credit Facility and from the proceeds of certain transactions. Upon the occurrence of an event of default, the outstanding obligations may be accelerated and PNC will have other customary remedies.

As of December 31, 2016, we had no amount outstanding under the Credit Facility, an applicable interest rate of 4.5% on borrowings below \$1,000, borrowing capacity of \$9,549 in addition to our unrestricted cash on hand of \$10,629, and no outstanding letters of credit related to the Credit Facility.

See Note 6 in the Notes to Consolidated Financial Statements for additional information.

Other Matters

With respect to our battery products, we typically offer warranties against any defects due to product manufacture or workmanship for up to one year from the date of purchase. With respect to our communications accessory products, we typically offer a three-year warranty. We provide for a reserve for these potential warranty expenses, which is based on an analysis of historical warranty issues. There is no assurance that future warranty claims will be consistent with past history, and in the event we experience a significant increase in warranty claims, there is no assurance that our reserves would be sufficient. This could have a materially adverse effect on our business, financial condition and results of operations.

Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements.

Critical Accounting Policies and Estimates

The above discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of these financial statements requires management to make estimates and assumptions that affect amounts reported therein. The estimates and assumptions that require management's most difficult, subjective or complex judgments are described below.

Revenue Recognition:

Product Sales – In general, revenues from the sale of products are recognized when products are shipped. When products are shipped with terms that require transfer of title upon delivery at a customer's location, revenues are recognized on date of delivery. We make a provision at the time the revenue is recognized for warranty costs expected to be incurred. Customers, including distributors, do not have a general right of return on products shipped.

Technology Contracts – We recognize revenue using the proportional method, measured by the percentage of actual costs incurred to date to the total estimated costs to complete the contract. Elements of cost include direct material, labor and overhead. If a loss on a contract is estimated, the full amount of the loss is recognized immediately. We allocate costs to all technology contracts based upon actual costs incurred including an allocation of certain research and development costs incurred.

Deferred Revenue - For each source of revenues, we defer recognition if: (i) evidence of an agreement does not exist, (ii) delivery or service has not occurred, (iii) the selling price is not fixed or determinable, or (iv) collectability is not reasonably assured.

Valuation of Inventory:

Inventories are stated at the lower of cost or market, with cost determined using the first-in, first-out ("FIFO") method. Our inventory includes raw materials, work in process and finished goods. We record provisions for excess, obsolete or slow moving inventory based on changes in customer demand, technology developments or other economic factors. The factors that contribute to inventory valuation risks are our purchasing practices, material and product obsolescence, accuracy of sales and production forecasts, introduction of new products, product lifecycles, product support and foreign regulations governing hazardous materials (see Item 1A – Risk Factors for further information on foreign regulations). We manage our exposure to inventory valuation risks by maintaining safety stocks, minimum purchase lots, managing product end-of-life issues brought on by aging components or new product introductions, and by utilizing certain inventory minimization strategies such as vendor-managed inventories. We believe that the accounting estimate related to valuation of inventories is a "critical accounting estimate" because it is susceptible to changes from period-to-period due to the requirement for management to make estimates relative to each of the underlying factors ranging from purchasing, to sales, to production, to after-sale support. If actual demand, market conditions or product lifecycles are adversely different from those estimated by management, inventory adjustments to lower market values would result in a reduction to the carrying value of inventory, an increase in inventory write-offs and a decrease in gross margins.

Warranties:

We maintain provisions related to normal warranty claims by customers. We evaluate these reserves quarterly based on actual experience with warranty claims to date and our assessment of additional claims in the future. There is no assurance that future warranty claims will be consistent with past history, and in the event we experience a significant increase in warranty claims, there is no assurance that our reserves would be sufficient.

Impairment of Long-Lived Assets:

We regularly assess all of our long-lived assets for impairment when events or circumstances indicate their carrying amounts may not be recoverable. This is accomplished by comparing the expected undiscounted future cash flows of the assets with the respective carrying amount as of the date of assessment. Should aggregate future cash flows be less than the carrying value, a write-down would be required, measured as the difference between the carrying value and the fair value of the asset. Fair value is estimated either through the assistance of an independent valuation or as the present value of expected discounted future cash flows. The discount rate used by us in our evaluation is an industry-based weighted average cost of capital. If the expected undiscounted future cash flows exceed the respective carrying amount as of the date of assessment, no impairment charge is recognized.

Environmental Issues:

Environmental expenditures, if any, that relate to current operations are generally expensed. Remediation costs that relate to an existing condition caused by past operations are accrued when it is probable that these costs will be incurred and can be reasonably estimated.

Goodwill and Other Intangible Assets:

The purchase price paid to effect an acquisition is allocated to the acquired tangible and intangible assets and liabilities at fair value. We do not amortize goodwill and intangible assets with indefinite lives, but instead evaluate these assets for impairment at least annually, or when events indicate that impairment exists. We amortize intangible assets that have definite lives so that the economic benefits of the intangible assets are being utilized over their weighted-average estimated useful life.

The impairment analysis of goodwill consists first of a review of various qualitative factors of the identified reporting units to determine whether it is more likely than not that the fair value of a reporting unit exceeds its carrying amount, including goodwill. This review includes, but is not limited to, an evaluation of the macroeconomic, industry or market, and cost factors relevant to the reporting unit as well as financial performance and entity or reporting unit events that may affect the value of the reporting unit. If this review leads to the determination that it is more likely than not that the fair value of the reporting unit is greater than its carrying amount, further impairment testing is not required. However, if this review cannot support a conclusion that it is more likely than not that the fair value of the reporting unit is greater than its carrying amount, or at our discretion, quantitative impairment steps are performed. Similarly, the analysis for indefinite-lived intangible assets consists of a review of various qualitative factors to determine if it is more likely than not that the indefinite-lived intangible asset is not impaired. If we conclude that it is more likely than not that we cannot support that the indefinite-lived asset is not impaired, or at our discretion, quantitative impairment steps are performed.

The quantitative impairment test for goodwill consists of a comparison of the fair value of the reporting unit with the carrying amount of the reporting unit to which it is assigned. If the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not impaired. If the carrying amount of a reporting unit exceeds its fair value, a second step of the goodwill impairment test is performed to measure the amount of impairment loss, if any. The impairment test for intangible assets with indefinite lives consists of a comparison of the fair value of the intangible assets with their carrying amounts. If the carrying value of the intangible assets exceeds the fair value, an impairment loss is recognized in an amount equal to that excess. We determine the fair value of the reporting unit for goodwill impairment testing based on a discounted cash flow model. We determine the fair value of our intangibles assets with indefinite lives (trademarks) through the relief from royalty valuation approach.

We conducted our annual impairment analysis for goodwill and intangible assets with indefinite lives as of December 31, 2016. For 2016, we identified four goodwill reporting units for analysis. We performed a quantitative analysis on these reporting units as of December 31, 2016. This testing indicated no impairment.

For 2016, we identified four trademarks for analysis. We performed annual quantitative tests on each of these trademarks, and the testing indicated no impairment in 2016. While our testing indicated that the McDowell Research Corporation trademark is not impaired in 2016, it passed by a relatively narrow margin of 15% over the carrying value and is most susceptible to variances in sales from current projections. In 2015, we determined that an impairment of \$150 was required to reduce the carrying value of our McDowell Research Corporation trademark for our Communications Systems business to its estimated fair value.

There is a possibility that our goodwill and other intangible assets, particularly in our Communications Systems business, could be impaired in the future should there be a significant change in our internal forecasts and other assumptions we use in our impairment analysis.

Stock-Based Compensation:

We recognize compensation cost relating to share-based payment transactions in our financial statements. The cost is measured at the grant date, based on the fair value of the award, and is recognized as an expense over the employee's requisite service period (generally the vesting period of the equity award). We calculate expected volatility for stock options by taking an average of historical volatility over the past five years and a computation of implied volatility. The computation of expected term was determined based on historical experience of similar awards, giving consideration to the contractual terms of the stock-based awards and vesting schedules. The interest rate for periods within the contractual life of the award is based on the U.S. Treasury yield in effect at the time of grant. If required, our market based awards are valued using a Monte Carlo simulation.

Income Taxes:

We account for income taxes using the asset and liability method. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax basis of assets and liabilities and are measured using the enacted tax rates and laws that may be in effect when the differences are expected to reverse.

In 2016 and 2015, in the U.S. and certain operations in the U.K., we continued to report a valuation allowance for our deferred tax assets that we believe cannot be offset by reversing temporary differences because based on past history, it is more likely than not that we would not be able to utilize our U.S. and U.K. net operating losses (“NOLs”) that have accumulated over time. The recognition of a valuation allowance on our deferred tax assets resulted from our evaluation of all available evidence, both positive and negative. The assessment of the realizability of the NOLs was based on a number of factors including our history of net operating losses, the volatility of our earnings, our historical operating volatility, our historical inability to accurately forecast earnings for future periods and the continued uncertainty of the general business climate. We concluded that these historical factors represent sufficient negative evidence and have concluded that we should continue to record a full valuation allowance at December 31, 2016. We currently carry a deferred tax asset in China that we have determined does not require a valuation allowance as we are more likely than not to fully utilize the NOL in China. We continually assess the carrying value of this asset based on relevant accounting standards.

Business Combinations:

We account for businesses acquired using the acquisition method of accounting. Under this method, all acquisition-related costs are expensed as incurred. The underlying net assets are recorded at their respective acquisition-date fair values. As part of this process, we identify and attribute values and estimated lives to property and equipment and intangible assets acquired. These determinations involve significant estimates and assumptions, including those with respect to future cash flows, discount rates and asset lives, and therefore require considerable judgment. These determinations affect the amount of depreciation and amortization expense recognized in future periods. The results of operations of acquired businesses are included in the consolidated statements of income and comprehensive income beginning on the respective business's acquisition date.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As a smaller reporting company, we are not required to provide this information.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The financial statements and schedules listed in Item 15(a)(1) are included in this Report beginning on page 39.

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
Ultralife Corporation

We have audited the accompanying consolidated balance sheet of Ultralife Corporation and subsidiaries as of December 31, 2016, and the related consolidated statements of income and comprehensive income, shareholders' equity and cash flows for the year then ended (collectively, the financial statements). 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 audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Ultralife Corporation and subsidiaries as of December 31, 2016, and the results of their operations and their cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

/s/ Freed Maxick CPAs, P.C.
Rochester, New York
February 9, 2017

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of
Ultralife Corporation

We have audited the accompanying consolidated balance sheet of Ultralife Corporation as of December 31, 2015, and the related consolidated statement of income and comprehensive income, shareholders' equity, and cash flows for the year ended December 31, 2015. Ultralife Corporation's management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Ultralife Corporation as of December 31, 2015, and the results of its operations and its cash flows for the year ended December 31, 2015, in conformity with accounting principles generally accepted in the United States of America.

/s/ Bonadio & Co., LLP
Pittsford, New York
March 2, 2016

ULTRALIFE CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands)

| | December 31, | |
|--|------------------|------------------|
| | 2016 | 2015 |
| ASSETS | | |
| Current Assets: | | |
| Cash | \$ 10,629 | \$ 14,393 |
| Restricted Cash | 77 | 140 |
| Trade Accounts Receivable, Net of Allowance for Doubtful Accounts of \$277 and \$300, Respectively | 13,179 | 11,430 |
| Inventories, Net | 23,456 | 23,814 |
| Prepaid Expenses and Other Current Assets | 2,079 | 1,900 |
| Due from Insurance Company | 0 | 177 |
| Deferred Income Taxes | 94 | 92 |
| Total Current Assets | <u>49,514</u> | <u>51,946</u> |
| Property, Equipment and Improvements, Net | 7,999 | 9,038 |
| Goodwill | 19,965 | 16,283 |
| Other Intangible Assets, Net | 7,194 | 3,946 |
| Security Deposits and Other Non-Current Assets | 72 | 309 |
| Total Assets | <u>\$ 84,744</u> | <u>\$ 81,522</u> |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current Liabilities: | | |
| Accounts Payable | \$ 7,292 | \$ 6,494 |
| Accrued Compensation and Related Benefits | 1,258 | 2,377 |
| Accrued Expenses and Other Current Liabilities | 2,606 | 1,749 |
| Income Taxes Payable | 172 | 227 |
| Total Current Liabilities | <u>11,328</u> | <u>10,847</u> |
| Deferred Income Taxes | 5,538 | 4,631 |
| Other Non-Current Liabilities | 18 | 28 |
| Total Liabilities | <u>16,884</u> | <u>15,506</u> |
| Commitments and Contingencies (Note 7) | | |
| Shareholders' Equity: | | |
| Preferred Stock – Par Value \$.10 Per Share; Authorized 1,000,000 Shares; None Issued | - | - |
| Common Stock – Par Value \$.10 Per Share; Authorized 40,000,000 Shares; | | |
| Issued – 19,324,723 Shares and 19,181,815 Shares, Respectively; | | |
| Outstanding – 15,308,971 Shares and 15,322,155 Shares, Respectively | 1,932 | 1,918 |
| Capital in Excess of Par Value | 178,163 | 177,007 |
| Accumulated Deficit | (90,542) | (94,051) |
| Accumulated Other Comprehensive Loss | (3,080) | (907) |
| Treasury Stock - at Cost; 4,015,752 Shares and 3,859,660 Shares at December 31, 2016 and 2015, | | |
| Respectively | <u>(18,443)</u> | <u>(17,808)</u> |
| Total Ultralife Corporation Equity | 68,030 | 66,159 |
| Non-Controlling Interest | (170) | (143) |
| Total Shareholders' Equity | <u>67,860</u> | <u>66,016</u> |
| Total Liabilities and Shareholders' Equity | <u>\$ 84,744</u> | <u>\$ 81,522</u> |

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

ULTRALIFE CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(Dollars in Thousands, Except Per Share Amounts)

| | Years Ended December 31, | |
|--|--------------------------|-----------------|
| | 2016 | 2015 |
| Revenues | \$ 82,460 | \$ 76,427 |
| Cost of Products Sold | 57,352 | 53,111 |
| Gross Profit | <u>25,108</u> | <u>23,316</u> |
| Operating Expenses: | | |
| Research and Development | 5,946 | 5,603 |
| Selling, General and Administrative | 15,399 | 14,233 |
| Intangible Asset Impairment | 0 | 150 |
| Total Operating Expenses | <u>21,345</u> | <u>19,986</u> |
| Operating Income | 3,763 | 3,330 |
| Other (Expense) Income: | | |
| Interest Income | 0 | 3 |
| Interest and Financing Expense | (263) | (248) |
| Miscellaneous | 80 | 65 |
| Income Before Income Taxes | <u>3,580</u> | <u>3,150</u> |
| Income Tax Provision | 98 | 310 |
| Net income | 3,482 | 2,840 |
| Net Loss Attributable to Non-Controlling Interest | 27 | 29 |
| Net Income Attributable to Ultralife Corporation | 3,509 | 2,869 |
| Other Comprehensive Loss: | | |
| Foreign Currency Translation Adjustments | (2,173) | (440) |
| Comprehensive Income Attributable to Ultralife Corporation | <u>\$ 1,336</u> | <u>\$ 2,429</u> |
| Net Income Per Share Attributable to Ultralife Corporation Common Shareholders – Basic: | <u>\$.23</u> | <u>\$.18</u> |
| Net Income Per Share Attributable to Ultralife Corporation Common Shareholders – Diluted: | <u>\$.23</u> | <u>\$.17</u> |
| Weighted Average Shares Outstanding – Basic | <u>15,261</u> | <u>16,182</u> |
| Weighted Average Shares Outstanding – Diluted | <u>15,405</u> | <u>16,458</u> |

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

ULTRALIFE CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(Dollars in Thousands)

| | Common Stock | | Capital in Excess of Par Value | Accumulated Other Comprehensive Income (Loss) | Accumulated Deficit | Treasury Stock | Non- Controlling Interest | Total |
|---|---------------------|----------|---|--|------------------------|-------------------|---------------------------------|-----------|
| | Number of Shares | Amount | | | | | | |
| Balance – December 31, 2014 | 18,941,544 | \$ 1,894 | \$ 175,940 | \$ (467) | \$ (96,920) | \$ (8,420) | \$ (114) | \$ 71,913 |
| Purchases of Stock | | | | | | (9,388) | | (9,388) |
| Vesting of Restricted Shares | 102,334 | 10 | (28) | | | | | (18) |
| Stock Option Exercises | 137,937 | 14 | 524 | | | | | 538 |
| Stock-Based Compensation - | | | | | | | | |
| Stock Options | | | 489 | | | | | 489 |
| Restricted Stock | | | 82 | | | | | 82 |
| Foreign Currency Translation Adjustments | | | | (440) | | | | (440) |
| Net Income | | | | | 2,869 | | (29) | 2,840 |
| Balance – December 31, 2015 | 19,181,815 | \$ 1,918 | \$ 177,007 | \$ (907) | \$ (94,051) | \$ (17,808) | \$ (143) | \$ 66,016 |
| Purchases of Stock | | | | | | (635) | | (635) |
| Vesting of Restricted Shares | 15,900 | 2 | (2) | | | | | - |
| Stock Option Exercises | 127,008 | 12 | 448 | | | | | 460 |
| Stock-Based Compensation - | | | | | | | | |
| Stock Options | | | 676 | | | | | 676 |
| Restricted Stock | | | 34 | | | | | 34 |
| Foreign Currency Translation Adjustments | | | | (2,173) | | | | (2,173) |
| Net Income | | | | | 3,509 | | (27) | 3,482 |
| Balance – December 31, 2016 | 19,324,723 | \$ 1,932 | \$ 178,163 | \$ (3,080) | \$ (90,542) | \$ (18,443) | \$ (170) | \$ 67,860 |

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

ULTRALIFE CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In Thousands)

| | Years ended December 31, | |
|---|--------------------------|------------------|
| | 2016 | 2015 |
| OPERATING ACTIVITIES: | | |
| Net Income | \$ 3,482 | \$ 2,840 |
| Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities: | | |
| Depreciation | 2,223 | 2,401 |
| Amortization of Intangible Assets | 503 | 235 |
| Amortization of Financing Fees | 71 | 71 |
| Intangible asset impairment | - | 150 |
| Stock-Based Compensation | 710 | 571 |
| Loss on Long-Lived Asset Disposals | 29 | 114 |
| Deferred Income Tax Expense | 135 | 183 |
| Provision for allowance for doubtful accounts | (24) | (22) |
| Changes in operating assets and liabilities: | | |
| Accounts Receivable | (667) | (217) |
| Inventories | 1,981 | 2,101 |
| Prepaid Expenses and Other Assets | 730 | (757) |
| Income taxes receivable and payable | (158) | 158 |
| Accounts Payable and Other Liabilities | (1,362) | 723 |
| Net Cash Provided by Operating Activities | <u>7,653</u> | <u>8,551</u> |
| INVESTING ACTIVITIES: | | |
| Acquisition of Accutronics, Net of Cash Acquired | (9,857) | - |
| Cash Paid for Property, Equipment and Improvements | (1,219) | (2,910) |
| Change in Restricted Cash | 65 | - |
| Net Cash Used in Investing Activities | <u>(11,011)</u> | <u>(2,910)</u> |
| FINANCING ACTIVITIES: | | |
| Cash Paid to Repurchase Treasury Stock | (607) | (9,388) |
| Proceeds from Debt Borrowings | 3,030 | - |
| Payments of Debt Borrowings | (3,030) | - |
| Proceeds from Exercise of Stock Options | 460 | 538 |
| Tax Withholdings on Stock-Based Awards | (28) | (18) |
| Net Cash Used in Financing Activities | <u>(175)</u> | <u>(8,868)</u> |
| Effect of Exchange Rate Changes on Cash | <u>(231)</u> | <u>(91)</u> |
| DECREASE IN CASH | (3,764) | (3,318) |
| Cash, Beginning of Year | 14,393 | 17,711 |
| Cash, End of Year | <u>\$ 10,629</u> | <u>\$ 14,393</u> |
| Supplemental Cash Flow Information: | | |
| Construction in Process in Accounts Payable | <u>\$ 83</u> | <u>\$ -</u> |
| Income Taxes Paid | <u>273</u> | <u>52</u> |
| Interest Paid | <u>179</u> | <u>150</u> |

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

ULTRALIFE CORPORATION
Notes to Consolidated Financial Statements
(Dollars in Thousands, Except Per Share Amounts)

Note 1 - Summary of Operations and Significant Accounting Policies

a. *Description of Business*

As used in this annual report, unless otherwise indicated, the terms “we”, “our” and “us” refer to Ultralife Corporation (“Ultralife”) and includes our wholly-owned subsidiaries, ABLE New Energy Co., Limited and its wholly-owned subsidiary ABLE New Energy Co.; Ltd; Ultralife UK LTD and its wholly-owned subsidiary, Accutronics Ltd; Ultralife Batteries (UK) Ltd.; and our majority-owned joint venture Ultralife Batteries India Private Limited.

We offer products and services ranging from power solutions to communications and electronics systems. Through our engineering and collaborative approach to problem solving, we serve government, defense and commercial customers across the globe. We design, manufacture, install and maintain power and communications systems including: rechargeable and non-rechargeable batteries, charging systems, communications and electronics systems and accessories, and custom engineered systems. We sell our products worldwide through a variety of trade channels, including original equipment manufacturers (“OEMs”), industrial and defense supply distributors, and directly to U.S. and international defense departments.

b. *Principles of Consolidation*

The consolidated financial statements are prepared in accordance with generally accepted accounting principles in the United States (“GAAP”) and include the accounts of Ultralife Corporation, our wholly-owned subsidiaries, Ultralife Batteries (UK) Ltd., Ultralife UK LTD, and its wholly-owned subsidiary Accutronics Ltd, ABLE New Energy Co., Limited, and its wholly-owned subsidiary ABLE New Energy Co., Ltd. (“ABLE” collectively), and our majority-owned subsidiary Ultralife Batteries India Private Limited (“India JV”). Intercompany accounts and transactions have been eliminated in consolidation.

c. *Management's Use of Judgment and Estimates*

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at year end and the reported amounts of revenues and expenses during the reporting period. Key areas affected by estimates include: (a) carrying value of goodwill and intangible assets; (b) reserves for deferred tax assets, excess and obsolete inventory, warranties, and bad debts; (c) valuation of assets acquired and liabilities assumed in business combinations; (d) various expense accruals; and (e) stock-based compensation. Our actual results could differ from these estimates.

d. *Reclassifications*

Certain items previously reported in specific financial statement captions are reclassified to conform to the current presentation. There were no material reclassifications for the years ended December 31, 2016 and 2015.

e. *Cash*

Our cash balances may at times exceed federally insured limits. We have not experienced any losses in these accounts and believe we are not exposed to any significant risk with respect to cash.

f. *Accounts Receivable and Allowance for Doubtful Accounts*

We extend credit to our customers in the normal course of business. We perform ongoing credit evaluations and generally do not require collateral. Trade accounts receivable are recorded at their invoiced amounts, net of allowance for doubtful accounts. We evaluate the adequacy of our allowance for doubtful accounts quarterly. Accounts outstanding longer than contractual payment terms are considered past due and are reviewed individually for collectability. We maintain reserves for potential credit losses based upon our loss history and specific receivables aging analysis. Receivable balances are written off when collection is deemed unlikely. Allowance for doubtful accounts was \$277 and \$300 for the years ended December 31, 2016 and 2015, respectively.

g. *Inventories*

Inventories are stated at the lower of cost or market with cost determined under the first-in, first-out (FIFO) method. We record provisions for excess, obsolete or slow-moving inventory based on changes in customer demand, technology developments or other economic factors.

h. *Property, Plant and Equipment*

Property, plant and equipment are stated at cost. Depreciation and amortization are computed using the straight-line method over the estimated useful lives. Estimated useful lives are as follows:

| | |
|--|-------------------------------------|
| Buildings (years) | 10 – 20 |
| Machinery and Equipment (years) | 5 – 10 |
| Furniture and Fixtures (years) | 3 – 10 |
| Computer Hardware and Software (years) | 3 – 5 |
| Leasehold Improvements | Lesser of useful life or lease term |

Betterments, renewals and extraordinary repairs that extend the life of the assets are capitalized. Other repairs and maintenance costs are expensed when incurred. When disposed, the cost and accumulated depreciation applicable to assets retired are removed from the accounts and the gain or loss on disposition is recognized in operating income.

i. *Long-Lived Assets, Goodwill and Intangibles*

We assess all of our long-lived assets for impairment when events or circumstances indicate that their carrying amounts may not be recoverable. For property, plant and equipment and amortizable intangible assets, this is accomplished by comparing the expected undiscounted future cash flows of the assets with the respective carrying amount as of the date of assessment. Should aggregate future cash flows be less than the carrying value, a write-down would be required, measured as the difference between the carrying value and the fair value of the asset. Fair value is estimated as the present value of expected discounted future cash flows. The discount rate used by us in our evaluation is an industry-based weighted average cost of capital. If the expected undiscounted future cash flows exceed the respective carrying amount as of the date of assessment, no impairment is recognized. We did not record any impairments of property, plant and equipment or amortizable intangible assets in the years ended December 31, 2016 or 2015.

We do not amortize goodwill and intangible assets with indefinite lives, but instead measure these assets for impairment as of December 31, and on an interim basis when events or circumstances indicate that impairment may exist. We amortize intangible assets that have definite lives so that the economic benefits of the intangible assets are being recognized as expense over their weighted-average estimated useful lives.

The impairment analysis of goodwill consists first of a review of various qualitative factors of the identified reporting units to determine whether it is more likely than not that the fair value of a reporting unit exceeds its carrying amount, including goodwill. This review includes, but is not limited to, an evaluation of the macroeconomic, industry or market, and cost factors relevant to the reporting unit as well as financial performance and entity or reporting unit events that may affect the value of the reporting unit. If this review leads to the determination that it is more likely than not that the fair value of the reporting unit is greater than its carrying amount, further impairment testing is not required. However, if this review cannot support such a conclusion or we determine to do so at our discretion, we will perform quantitative impairment steps. Similarly, the analysis for indefinite-lived intangible assets consists of review of various qualitative factors to determine if it is more likely than not that the indefinite-lived intangible asset is not impaired. If such a conclusion cannot be supported or at our discretion, we will perform quantitative impairment steps.

The quantitative impairment test for goodwill consists of a comparison of the fair value of the reporting unit with the carrying amount of the reporting unit to which it is assigned. If the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not impaired. If the carrying amount of a reporting unit exceeds its fair value, a second step of the goodwill impairment test is performed to measure the amount of impairment loss, if any. The impairment test for intangible assets with indefinite lives consists of a comparison of the fair value of the intangible assets with their carrying amounts. If the carrying value of the intangible assets exceeds the fair value, an impairment loss is recognized in an amount equal to that excess. We determine the fair value of the reporting unit for goodwill impairment testing based on a discounted cash flow model. We determine the fair value of our intangibles assets with indefinite lives (trademarks) through the relief from royalty valuation approach.

No impairments of long-lived intangible assets were recorded in the year ended December 31, 2016. While our testing indicated that the McDowell Research Corporation trademark is not impaired in 2016, it passed by a relatively narrow margin and is most susceptible to variances in sales from current projections. Due to time delays in the awarding by government/defense customers in recent years of certain large projects in our Communications Systems segment, we recorded a partial impairment of our McDowell Research, Ltd. trademark in the year ended December 31, 2015. This impairment amounted to \$150.

Future amortization expense of amortizable intangible assets will be approximately \$405, \$373, \$352, \$340 and \$321 for the fiscal years ending December 31, 2017 through 2021, respectively.

j. *Translation of Foreign Currency*

The financial statements of our foreign subsidiaries are translated from the functional currency into U.S. dollar equivalents, with translation adjustments recorded as the sole component of accumulated other comprehensive loss on the balance sheets. Exchange gains and (losses) relate to foreign currency transactions and balances denominated in currencies other than the functional currency included in net income for the years ended December 31, 2016 and 2015 were \$86 and \$48, respectively.

k. *Revenue Recognition*

Product Sales – In general, revenues from the sale of products are recognized when products are shipped. When products are shipped with terms that require transfer of title upon delivery at a customer's location, revenues are recognized on the date of delivery. We will make a provision at the time the revenue is recognized for warranty costs expected to be incurred. Customers, including distributors, do not have a general right of return on products shipped.

Deferred Revenue – For each source of revenues, we defer recognition if: (i) evidence of an agreement does not exist, (ii) delivery or service has not occurred, (iii) the selling price is not fixed or determinable, or (iv) collectability is not reasonably assured.

l. *Warranty Reserves*

We estimate future costs associated with expected product failure rates, material usage and service costs in the development of our warranty obligations. Warranty reserves, included in other current liabilities and other long-term liabilities as applicable on our Consolidated Balance Sheets, are based on historical experience of warranty claims. In the event the actual results of these items differ from the estimates, an adjustment to the warranty obligation would be recorded.

m. *Shipping and Handling Costs*

Costs incurred by us related to shipping and handling are included in cost of products sold. Amounts charged to customers pertaining to these costs are reflected as revenue.

n. *Advertising Expenses*

Advertising costs are expensed as incurred and are included in selling, general and administrative expenses in the accompanying Consolidated Statements of Income and Comprehensive Income. Such expenses amounted to \$32 and \$59 for the years ended December 31, 2016 and 2015, respectively.

o. *Research and Development*

Research and development expenditures are charged to operations as incurred. The majority of research and development expenses pertain to salaries and benefits, developmental supplies, depreciation and other contracted services. During 2016 and 2015, we expended \$6,155 and \$6,112, respectively, on research and development, including \$209 and \$509, respectively, on customer sponsored research and development activities, which are included in cost of goods sold. We recognized \$209 and \$509 of revenue relating to these activities during 2016 and 2015, respectively.

p. *Environmental Costs*

Environmental expenditures that relate to current operations are expensed. Remediation costs that relate to an existing condition caused by past operations are accrued when it is probable that these costs will be incurred and can be reasonably estimated.

q. *Income Taxes*

We account for income taxes using the asset and liability method. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax basis of assets and liabilities and are measured using the enacted tax rates and laws that are expected to be in effect when the differences are expected to reverse.

A valuation allowance is required when it is more likely than not that the recorded value of a deferred tax asset will not be realized. As of December 31, 2016, we continued to recognize a valuation allowance in the U.S. and certain U.K. operations on our net deferred tax assets to the extent that temporary tax differences and the U.S. and U.K. net operating loss and tax credit carry-forwards resulting in the deferred tax asset are not able to be offset by future reversing temporary differences. The assessment of the realizability of the U.S. NOL was based on a number of historical factors including, our history of net operating losses, the volatility of our earnings, our historical operating volatility, our historical inability to accurately forecast earnings for future periods and the continued uncertainty of the general business climate as of the end of 2016. We concluded that these historical factors represent sufficient negative evidence and have concluded that we should record a full valuation allowance against these net deferred tax assets. We also recorded a full valuation allowance on our net deferred tax asset for the year ended December 31, 2015.

r. *Concentration Related to Customers and Suppliers*

During the year ended December 31, 2016, we had two major customers, both large defense primary contractors, which together comprised 25% of our revenues. During the year ended December 31, 2015, one of those customers comprised 23% of our sales. There were no other customers that comprised greater than 10% of our total revenues during these years.

Currently, we do not experience significant seasonal trends in our revenues. Since a significant portion of our revenues are based on purchases from U.S. and allied country defense departments, the timing of our sales could be impacted by delays in the government budget process and the decisions to deploy resources to support military purchases of our products.

We generally do not distribute our products to a concentrated geographical area nor is there a significant concentration of credit risks arising from individuals or groups of customers engaged in similar activities, or who have similar economic characteristics. While direct and indirect sales to the U.S. Department of Defense have been substantial during 2016 and 2015, we do not consider this customer to be a significant credit risk. We do not normally obtain collateral on trade accounts receivable.

Certain materials and components used in our products are available only from a single or a limited number of suppliers. As such, some materials and components could become in short supply resulting in limited availability and/or increased costs. Additionally, we may elect to develop relationships with a single or limited number of suppliers for materials and components that are otherwise generally available. Although we believe that alternative suppliers are available to supply materials and components that could replace materials and components currently used and that, if necessary, we would be able to redesign our products to make use of such alternatives, any interruption in the supply from any supplier that serves as a sole source could delay product shipments and have a material adverse effect on our business, financial condition and results of operations. We have experienced interruptions of product deliveries by sole source suppliers in the past.

s. *Fair Value Measurements and Disclosures*

Fair value is defined as the price that would be received for an asset or the exit price that would be paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants on the measurement date. Fair value is estimated by applying the following hierarchy, which prioritizes the inputs used to measure fair value into three levels and bases the categorization within the hierarchy upon the lowest level of input that is available and significant to the fair value measurement:

- Level 1:** Quoted prices in active markets for identical assets or liabilities.
- Level 2:** Observable inputs, other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or that we corroborate with observable market data for substantially the full term of the related assets or liabilities.
- Level 3:** Unobservable inputs supported by little or no market activity that are significant to the fair value of the assets or liabilities.

The fair value of financial instruments approximated their carrying values at December 31, 2016 and 2015. The fair value of cash, trade accounts receivable, trade accounts payable, and accrued liabilities approximates carrying value due to the short-term nature of these instruments.

t. *Earnings Per Share*

Basic earnings per share is computed by dividing net income or loss attributable to Ultralife Corporation by the weighted average number of common shares outstanding for the period. Diluted earnings per share calculations reflect the assumed exercise and conversion of dilutive employee stock options and unvested restricted stock, if any, applying the treasury stock method. Diluted earnings per share in 2016 include 1,238,804 outstanding in-the-money stock options that add 135,458 shares to the number of shares outstanding, and include 15,900 restricted stock units that add 9,538 shares outstanding. Diluted earnings per share in 2015 include 1,312,282 outstanding in-the-money stock options that add 260,318 shares to the number of shares outstanding, and include 32,800 restricted stock units which add 15,385 shares outstanding.

Diluted earnings per share calculations exclude the effect of approximately 1,332,281 and 945,687 employee stock options in 2016 and 2015, respectively, as such options have an exercise price in excess of the weighted average market price of the Company's common stock.

u. *Stock-Based Compensation*

We have various stock-based employee compensation plans that are described more fully in Note 8. The compensation cost relating to share-based payment transactions is measured at the grant date, based on the estimated fair value of the award, and is recognized as expense over the employee's requisite service period (generally the vesting period of the equity award).

v. *Segment Reporting*

We have two operating segments – Battery & Energy Products, and Communications Systems. The basis for determining our operating segments is the manner in which financial information is used in monitoring our operations. Management operates and organizes itself according to business units that comprise unique products and services across geographic locations.

w. *Recent Accounting Pronouncements*

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2014-09 (Topic 606) "Revenue from Contracts with Customer" related to revenue from contracts with customers. Under this standard, revenue is recognized when promised goods or services are transferred to customers in an amount that reflects the consideration that is expected to be received for those goods or services. The updated standard will replace most existing revenue recognition guidance under GAAP and permits the use of either the retrospective or cumulative effect transition method. Topic 606 is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. We do not expect the adoption of Topic 606 to have a material impact on our Consolidated Financial Statements. We do not anticipate early adoption of the standard.

In July 2015, the FASB issued Accounting Standards Update No. 2015-11, "Simplifying the Measurement of Inventory," which simplifies the subsequent measurement of inventory by using only the lower of cost and net realizable value. This standard is effective for fiscal years and interim periods within those years beginning after December 15, 2016, and must be applied on a retrospective basis. The adoption of this standard is not expected to have a material impact on our Consolidated Financial Statements.

In November 2015, the FASB issued Accounting Standards Update No. 2015-17, "Income Taxes, Balance Sheet Classification of Deferred Taxes" which requires that deferred tax assets and liabilities be classified as noncurrent in a classified statement of financial position. The new standard is effective for annual periods beginning after December 15, 2016, and interim periods within that reporting period. The guidance under this new standard may be applied either prospectively or retrospectively to all periods presented. We will apply the standard retrospectively beginning in the first quarter 2017.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, “Leases” requires that lessees recognize a right-to-use asset and related lease liability for all significant financing and operating leases not considered short-term leases, and specifies where in the statement of cash flows the related lease payments are to be presented. The guidance is effective for years beginning after December 15, 2018 and early adoption is permitted. The Company has not yet determined the impact of this new standard on our Consolidated Financial Statements, but believes it may be significant. We have not yet determined whether we will adopt the standard in advance of its required effective date.

In March 2016, the FASB issued Accounting Standards Update No. 2016-09, “Compensation – Stock Compensation (Topic 718)” Improvements to Employee Share-Based Payment Accounting” which involves several aspects of accounting for share-based payment transactions, including income tax consequences, forfeitures and classification on the statement of cash flows. The guidance is effective for annual periods beginning after December 15, 2016, and interim periods within those periods. We will adopt this standard effective January 1, 2017. We do not expect this standard to have a material impact on our Consolidated Financial Statements.

In October 2016, the FASB issued Accounting Standards Update No. 2016-16, “Income Taxes (Topic 740), Intra-Entity Transfers of Assets Other Than Inventory”. The new guidance requires that entities recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs, rather than when the asset is sold to an outside party. The guidance is effective for annual reporting periods beginning after December 15, 2017, including interim periods within those annual reporting periods. Early adoption is permitted. The new guidance requires adoption on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. The company will adopt effective January 1, 2018 and is currently evaluating the impact this guidance will have on our Consolidated Financial Statements.

In August 2016, the FASB issued Accounting Standards Update No. 2016-15, “Statement of Cash Flows (Topic 230), Classification of Certain Cash Receipts and Cash Payments”. The new guidance makes eight targeted changes to how cash receipts and cash payments are presented and classified in the statement of cash flows. The guidance is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity that elects early adoption must adopt all of the amendments in the same period. The new guidance requires adoption on a retrospective basis unless it is impracticable to apply, in which case the company would be required to apply the amendments prospectively as of the earliest date practicable. The company will adopt January 1, 2018 and is currently evaluating the impact this guidance will have on our Consolidated Financial Statements.

Note 2 – Acquisition

On January 13, 2016, Ultralife UK Limited (the “Merger Subsidiary”), a U.K. corporation and a wholly-owned subsidiary of Ultralife Corporation (the “Company”), completed the acquisition of all of the outstanding ordinary shares of Accutronics Limited (“Accutronics”), a U.K. corporation based in Newcastle-under-Lyme, U.K., from Intrinsic Equity Limited, Catapult Growth Fund Limited Partnership, MJF Pension Trustees Limited, Robert Andrew Phillips and Michael Allen (collectively, the “Sellers”). There are no material relationships between the Company or Merger Subsidiary and any of the Sellers, other than pertaining to this acquisition. Accutronics is a leading independent designer and manufacturer of smart batteries and charger systems for high-performance, feature-laden portable and handheld electronic devices and is classified in the Battery & Energy Products segment. The acquisition of Accutronics advances our strategy of commercial revenue diversification and expands our geographic reach within European OEM’s. With industry experts predicting mid-to-high single digit growth in the global medical batteries market, this strategic investment positions Ultralife well for further penetration of and growing revenue streams from an attractive commercial market.

The acquisition was completed pursuant to the terms of the Share Purchase Agreement dated January 13, 2016 by and among the Merger Subsidiary and the Sellers. The Merger Subsidiary paid at the time of closing an aggregate purchase price of £7,575 (\$10,976) in cash, and in exchange the Merger Subsidiary received all of the outstanding shares of Accutronics ordinary stock. Monies to fund the purchase price were advanced to the Merger Subsidiary from the Company’s general corporate funds.

The purchase price was subject to adjustment based on the difference between actual and estimated amounts of working capital of Accutronics as well as the amount of net cash of Accutronics. The adjustment resulted in a final payment to the Sellers in the amount of £133 on February 24, 2016, bringing the total aggregate purchase price to £7,708 (\$11,161).

The purchase price allocation was determined in accordance with the accounting treatment of a business combination in Financial Accounting Standards Board (“FASB”) ASC Topic 805, *Business Combinations*. Under the guidance, the fair value of the consideration was determined and the assets acquired and liabilities assumed have been recorded at their fair values at the date of the acquisition. The excess of the consideration paid over the estimated fair values has been recorded as goodwill.

The allocation of purchase price to the assets acquired and liabilities assumed at the date of the acquisition is presented in the table below (in thousands). Management is responsible for determining the fair value of the tangible and intangible assets acquired and liabilities assumed as of the date of acquisition. Management considered a number of factors, including reference to an analysis performed under FASB ASC Topic 805 solely for the purpose of allocating the purchase price to the assets acquired and liabilities assumed. The Company’s estimates are based upon assumptions believed to be reasonable, but which are inherently uncertain and unpredictable. These valuations require the use of management’s assumptions, which would not reflect unanticipated events and circumstances that occur. The originally reported purchase price allocation has been updated based on information obtained about facts and circumstances that existed as of the acquisition date. As a result, adjustments were made which reduced identifiable intangible assets and property, plant and equipment by \$402 and \$99, respectively, and increased prepaids and other current assets, inventory, deferred income taxes on intangible assets and goodwill by \$291, \$75, \$113 and \$104, respectively.

| | | |
|--|-----------|---------------|
| Cash | \$ | 1,304 |
| Accounts Receivable | | 1,344 |
| Inventory | | 2,167 |
| Prepaids and Other Current Assets | | 584 |
| Property, Plant & Equipment | | 269 |
| Identifiable Intangible Assets | | 4,374 |
| Goodwill | | 4,487 |
| Accounts Payable | | (1,009) |
| Accrued Expenses | | (1,136) |
| Income Taxes Payable | | (111) |
| Non-Current Liabilities | | (209) |
| Deferred Income Taxes | | (74) |
| Deferred Income Taxes on Intangible Assets | | (829) |
| Total Consideration | \$ | 11,161 |

The goodwill included in the Company’s purchase price allocation presented above represents the value of Accutronics assembled and trained workforce, the incremental value that Accutronics engineering and technology will bring to the Company and the revenue growth expected to occur over time attributable to increased market penetration from future new products and customers. The goodwill acquired in connection with the acquisition is not deductible for income tax purposes.

The identifiable intangible assets included in the Company’s purchase price allocation represent customer contracts and relationships of \$2,821, intellectual property of \$1,132 and trade name of \$421 that are amortized straight-line over a period ranging from 10 to 15 years.

During the year ended December 31, 2016, direct acquisition costs of \$251 and increased cost of sales related to purchase accounting adjustments of \$96 for inventory acquired were recorded in the Company’s Consolidated Statement of Income and Comprehensive Income. Accutronics contributed revenue of \$10,362 and operating income of \$436 during the twelve-month period ended December, 2016, reflecting the purchase accounting adjustments and non-recurring costs directly related to the acquisition.

Set forth below is the unaudited pro forma results of the Company and Accutronics for the twelve-month period ended December 31, 2015 as if the acquisition occurred as of January 1, 2015 along with the reported results for the twelve-month period ended December 31, 2016 which includes the consolidation of Accutronics. The results of Accutronics were not material for the period from January 1, 2016 to the acquisition date. The unaudited pro forma results include purchase accounting adjustments to reflect the restatement of inventory to estimated fair value and the resulting increase in cost of sales for the sale of the inventory during this twelve-month period, direct acquisition costs and the amortization of intangible assets resulting from the purchase price allocation.

| | Twelve-Months Ended | |
|--|---------------------|---------------|
| | Dec. 31, 2015 | Dec. 31, 2016 |
| Revenue | \$ 89,534 | \$ 82,460 |
| Operating Income | \$ 3,858 | \$ 3,763 |
| Net Income Attributable to Ultralife Corporation | \$ 3,258 | \$ 3,509 |
| Earnings Per Share: | | |
| Basic | \$.20 | \$.23 |
| Diluted | \$.20 | \$.23 |

The unaudited pro forma results do not reflect the realization of any expected cost savings or other synergies from the acquisition of Accutronics as a result of restructuring activities, other cost savings initiatives or sales synergies following the completion of the business combination. Accordingly, these unaudited pro forma results are presented for informational purposes only and are not necessarily indicative of what the actual results of operations of the combined Company would have been if the acquisition had occurred at the beginning of the 2015 period presented, nor are they indicative of future results of operations.

Note 3 – Share Repurchase Program

On April 28, 2014, the Company’s Board of Directors approved a share repurchase program (the “Share Repurchase Program”) which became effective on May 1, 2014 and under which the Company was authorized to repurchase up to 1.8 million shares of its outstanding common stock over a period not to exceed twelve months. The Share Repurchase Program was extended through June 2, 2016, and the maximum number of shares authorized to be repurchased under the program was increased to 3.4 million shares.

Share repurchases under this program were made in accordance with SEC Rule 10b-18 using a variety of methods, which included open market purchases and block trades in compliance with applicable insider trading and other securities laws and regulations. With the exception of repurchases made during stock trading black-out periods under 10b5-1 Plans, the timing, manner, price and amount of any repurchases were determined at the Company’s discretion. The Share Repurchase Program expired on June 2, 2016 and did not obligate the Company to repurchase any specific number of shares.

In 2016, we repurchased a total of 156,092 shares of our common stock for an aggregate consideration of \$630, of which 149,904 shares were repurchased under the Share Repurchase Program for an aggregate amount (excluding fees and commissions) of \$603. In 2015, we repurchased a total of 2,258,929 shares of our common stock for an aggregate consideration of \$9,388, of which 2,225,437 shares were repurchased under the Share Repurchase Program for an aggregate amount (excluding fees and commissions) of \$9,162.

From the inception of the Share Repurchase Program on May 1, 2014 through its expiration on June 2, 2016, the Company repurchased 2,592,095 shares for an aggregate cost (excluding fees and commissions) of \$10,480.

Note 4 - Supplemental Balance Sheet Information

a. *Inventory, Net*

Inventories are stated at the lower of cost or market with cost determined under the first-in, first-out (FIFO) method. The composition of inventories, net was:

| | December 31, | |
|-------------------|------------------|------------------|
| | 2016 | 2015 |
| Raw Materials | \$ 14,482 | \$ 11,602 |
| Work in Process | 986 | 1,560 |
| Finished Products | 7,988 | 10,652 |
| Total | <u>\$ 23,456</u> | <u>\$ 23,814</u> |

The December 31, 2016 inventories include \$1,443 for Accutronics, which was acquired on January 13, 2016.

b. *Property, Plant and Equipment*

Major classes of property, plant and equipment consisted of the following:

| | December 31, | |
|--------------------------------------|-----------------|-----------------|
| | 2016 | 2015 |
| Land | \$ 123 | \$ 123 |
| Buildings and Leasehold Improvements | 7,757 | 7,490 |
| Machinery and Equipment | 49,722 | 49,609 |
| Furniture and Fixtures | 1,947 | 1,974 |
| Computer Hardware and Software | 5,223 | 4,585 |
| Construction in Progress | 421 | 745 |
| | <u>65,193</u> | <u>64,526</u> |
| Less – Accumulated Depreciation | (57,194) | (55,488) |
| Total | <u>\$ 7,999</u> | <u>\$ 9,038</u> |

Estimated costs to complete construction-in-progress as of December 31, 2016 and 2015 were approximately \$170 and \$180, respectively.

Depreciation expense was \$2,223 and \$2,401 for the years ended December 31, 2016 and 2015, respectively.

c. *Impairment of Goodwill, Intangible Assets and Long-Lived Assets*

We elected to forego the qualitative assessment for our four identified reporting units and conducted a quantitative assessment. The fair value for our reporting units subjected to this quantitative test could not be determined using readily available quoted Level 1 inputs or Level 2 inputs that were observable in active markets. Therefore, we used an income approach to estimate the fair value of the reporting units, using Level 3 inputs. To estimate the fair value of the reporting units, we used significant estimates and judgments, including an assessment of our future revenue prospects, particularly government/defense opportunities, as well as our estimates of the probabilities of the opportunities being funded, awarded, and awarded to us. Other key estimates and factors used in the valuation model included revenue growth rates and profit margins based on internal forecasts, as well as industry and market based terminal growth rates, inputs to the weighted-average cost of capital used to discount future cash flows, and earnings multiples. As a result of the goodwill impairment tests performed during 2016 and 2015, we determined that an impairment was not required.

Similarly, for our four other indefinite-lived intangible assets (trademarks), we elected to forego the qualitative assessment and proceeded to perform quantitative assessments. The fair value for our indefinite-lived intangible assets subjected to this quantitative test could not be determined using readily available quoted Level 1 inputs or Level 2 inputs that were observable in active markets. Therefore, we used a relief from royalty approach, to estimate the fair value of the indefinite-lived intangible assets, using Level 3 inputs. This method also required us to use significant estimates and judgmental factors. The key estimates and factors used in the valuation model included revenue growth rates, as well as industry and market based terminal growth rates, inputs to the weighted-average cost of capital used to discount future cash flows, and determined royalty rates from market data. As a result of the impairment tests performed during 2016, we determined that no impairments were required. As a result of the impairment tests performed during 2015, we determined that an impairment amounting to \$150 was required to reduce the carrying value of one Communications Systems business trademark to its estimated fair value.

There is a possibility that our goodwill and other intangible assets, particularly in our Communications Systems business, could be impaired should there be a significant change in our internal forecasts and other assumptions we use in our impairment analysis.

d. *Goodwill*

The following table summarizes the goodwill activity by segment for the years ended December 31, 2016 and 2015:

| | Battery & Energy Products | Communi- cations Systems | Total |
|--|--|---|------------------|
| Balance – January 1, 2015 | \$ 4,914 | \$ 11,493 | \$ 16,407 |
| Effect of Foreign Currency Translation | (124) | - | (124) |
| Balance – December 31, 2015 | 4,790 | 11,493 | 16,283 |
| Acquisition of Accutronics | 4,487 | - | 4,487 |
| Effect of Foreign Currency Translation | (805) | - | (805) |
| Balance – December 31, 2016 | <u>\$ 8,472</u> | <u>\$ 11,493</u> | <u>\$ 19,965</u> |

e. *Other Intangible Assets*

The composition of intangible assets was:

| | December 31, 2016 | | |
|-------------------------------|--------------------------|-------------------------------------|-----------------|
| | Cost | Accumulated Amortization | Net |
| Trademarks | \$ 3,404 | \$ - | \$ 3,404 |
| Customer Relationships | 6,395 | 3,975 | 2,420 |
| Patents and Technology | 5,455 | 4,417 | 1,038 |
| Distributor Relationships | 377 | 368 | 9 |
| Trade Name | 359 | 36 | 323 |
| Total Other Intangible Assets | <u>\$ 15,990</u> | <u>\$ 8,796</u> | <u>\$ 7,194</u> |

| | December 31, 2015 | | |
|-------------------------------|--------------------------|-------------------------------------|-----------------|
| | Cost | Accumulated Amortization | Net |
| Trademarks | \$ 3,411 | \$ - | \$ 3,411 |
| Patents and Technology | 4,482 | 4,217 | 265 |
| Customer Relationships | 3,971 | 3,716 | 255 |
| Distributor Relationships | 370 | 355 | 15 |
| Total Other Intangible Assets | <u>\$ 12,234</u> | <u>\$ 8,288</u> | <u>\$ 3,946</u> |

Amortization of intangible assets was included in the following financial statement captions:

| | Year ended December 31, | |
|---|--------------------------------|---------------|
| | 2016 | 2015 |
| Research and Development Expense | \$ 200 | \$ 130 |
| Selling, General and Administrative Expense | 303 | 105 |
| Total | <u>\$ 503</u> | <u>\$ 235</u> |

Except for the impairment charge recorded against a Communications Systems trademark in 2015, the change in the cost value of total intangible assets is a result of the acquisition of Accutronics on January 13, 2016 and the effect of foreign currency exchange rate fluctuations.

Note 5 - Operating Leases

We lease various buildings, machinery, land, automobiles and office equipment. Rental expenses for all operating leases were approximately \$668 and \$672 for the years ended December 31, 2016 and 2015, respectively. Future minimum lease payments under non-cancelable operating leases as of December 31, 2016 are as follows:

| 2017 | 2018 | 2019 | 2020 | 2021 |
|--------|--------|--------|--------|------|
| \$ 660 | \$ 558 | \$ 416 | \$ 100 | \$ - |

Note 6 - Debt

Credit Facilities

We are party to a Revolving Credit, Guaranty and Security Agreement (the "Credit Agreement") and related security agreements with PNC Bank, National Association ("PNC") that provides us a \$20 million secured asset-based revolving credit facility that includes a \$1 million letter of credit subfacility (the "Credit Facility"). The Credit Agreement expires on May 24, 2017.

On April 30, 2014, the Company and PNC entered into an amendment (the "Amendment") to the Credit Agreement. The Amendment permits the Company to commence the Share Repurchase Program described in Note 3, provided that (a) the Company is not in default under the Credit Agreement, (b) the Company's undrawn availability under the Credit Agreement is at least \$6 million both prior to and immediately following any repurchase, (c) the Company's undrawn availability under the Credit Agreement plus domestic unrestricted cash is at least \$8 million both prior to and immediately following any repurchase, and (d) the Company uses its unrestricted cash for such repurchases and does not request advances against the Credit Agreement for such purposes. On October 28, 2014, the Company and PNC entered into a second amendment to the Credit Agreement which modifies the definition of EBITDA in the Credit Agreement to include non-cash stock-based compensation expense.

On April 29, 2015, the Company and PNC entered into a third amendment to the Credit agreement which permitted the Company to extend the Share Repurchase Program to April 30, 2016. On June 15, 2015, the Company and PNC entered into a fourth amendment to the Credit Agreement that permitted the expansion of the Share Repurchase Program described in Note 3 and the extension of this program to June 2, 2016. Finally, on January 13, 2016, Company and PNC entered into a fifth amendment to the Credit Agreement which permitted the Company's acquisition of Accutronics Ltd. as described in Note 2 above.

Our available borrowing limit under the Credit Facility fluctuates from time to time based on a borrowing base formula equal to the sum of up to 85% of eligible accounts receivable plus the least of (a) up to 65% of the eligible inventory and eligible foreign in-transit inventory, (b) up to 85% of the appraised net orderly liquidation value of eligible inventory and eligible foreign in-transit inventory, and (c) \$7.5 million, in each case subject to the definitions in the Credit Agreement and reserves required by PNC.

Interest is payable quarterly and will accrue on outstanding indebtedness under the Credit Agreement at the alternate base rate, as defined in the Credit Agreement, plus the applicable margin or at the one, two or three month LIBOR rate plus the applicable margin as selected by us from time to time and listed below.

| Quarterly Average Undrawn Borrowing Availability | Applicable Margin for Alternate Base Rate Loans | Applicable Margin for LIBOR Rate Loans |
|---|--|---|
| Greater than \$8,000,000 | 1.00% | 2.00% |
| \$5,000,000 up to \$8,000,000 | 1.25% | 2.25% |
| Less than \$5,000,000 | 1.50% | 2.50% |

We must pay a fee on the Credit Facility's unused availability of 0.375% per annum and customary letter of credit fees in addition to various collateral monitoring and related fees and expenses.

In addition to customary affirmative and negative covenants, we must maintain a fixed charge coverage ratio as defined in the Credit Agreement of 1.15 to 1.00, tested quarterly for the four-quarters then ended. As of December 31, 2016 we were in compliance with all covenants. The Credit Facility is secured by substantially all our assets.

Any outstanding advances must be repaid upon expiration of the term of the Credit Facility. Payments must be made during the term to the extent outstanding advances exceed the maximum amount then permitted to be drawn as advances under the Credit Facility and from the proceeds of certain transactions. Upon the occurrence of an event of default, the outstanding obligations may be accelerated and PNC will have other customary remedies.

As of December 31, 2016, we had no outstanding balance under the Credit Facility, an applicable interest rate of 4.5%, borrowing capacity of \$9,549 in addition to our unrestricted cash on hand of \$10,629, and no outstanding letters of credit related to the Credit Facility.

Note 7 - Commitments and Contingencies

a. Indemnity

Our organizational documents provide that our directors or officers will be reimbursed for all expenses, to the fullest extent permitted by law arising out of their performance.

b. Purchase Commitments

As of December 31, 2016, we have made commitments to purchase approximately \$504 of production machinery and equipment.

c. China

Our operating facility in China presents risks including, but not limited to, changes in local regulatory requirements, including changes in labor laws, local wage laws, environmental regulations, taxes and operating licenses, compliance with U.S. regulatory requirements, including the Foreign Corrupt Practices Act, uncertainties as to application and interpretation of local laws and enforcement of contract and intellectual property rights, eminent domain claims, labor disputes, rapid changes in government, economic and political policies, and other various contingencies that are outside of our control. Any such event could depress our earnings and have other material adverse effects on our business, financial condition and results of operations.

d. Employment Contracts

We have an employment contract with Michael D. Popielec, our President and Chief Executive Officer, which remains in effect until terminated by either party. This agreement provides for a base salary, as adjusted for increases at the discretion of our Board of Directors, and includes incentive bonuses based upon attainment of specified quantitative and qualitative performance goals. This agreement also provides for severance payments in the event of specified events of termination of employment. In addition, this agreement provides for a lump sum payment in the event of termination of employment in connection with a change in control.

As part of our employment commencement process, employees are required to enter into agreements providing for confidentiality of certain information and the assignment of rights to inventions made by them while employed by us. These agreements also contain certain non-competition and non-solicitation provisions effective during the employment term and for varying periods thereafter depending on position and location. There can be no assurance that we will be able to enforce these agreements. All of our employees agree to abide by the terms of a Code of Ethics policy that provides for the confidentiality of certain information received during the course of their employment.

e. *Product Warranties*

We estimate future costs associated with expected product failure rates, material usage and service costs in the development of our warranty obligations. Warranty reserves are based on historical experience of warranty claims and generally will be estimated as a percentage of sales over the warranty period. In the event the actual results of these items differ from the estimates, an adjustment to the warranty obligation would be recorded. Changes in our product warranty liability during the years ended December 31, 2016 and 2015 were as follows:

| | 2016 | 2015 |
|--|---------------|---------------|
| Balance, January 1 | \$ 192 | \$ 376 |
| Provision (reversal) for warranties issued | 39 | (90) |
| Settlements made | (59) | (94) |
| Balance, December 31 | <u>\$ 172</u> | <u>\$ 192</u> |

f. *Legal Matters –*

We are subject to legal proceedings and claims that arise in the normal course of business. We believe that the final disposition of such matters will not have a material adverse effect on our financial position, results of operations or cash flows.

Dreamliner Litigation

In July 2013, an unoccupied Boeing 787 Dreamliner aircraft operated by Ethiopian Airlines (“EA”) was damaged by a fire while parked at London Heathrow Airport. We participated in and provided technical assistance in support of an investigation of this incident conducted by U.K. and U.S. regulatory authorities as well as by the manufacturer of the aircraft, as we are one of many downstream suppliers to that manufacturer. A final report was issued by the Air Accidents Investigative Branch - UK Civil Aviation regulatory authority, with findings indicating that the fire was primarily caused by circumstances related to the plane’s emergency locator transmitter (“ELT”) manufactured and installed by another company.

A component of the ELT is a battery pack which incorporates Ultralife’s industry-standard Lithium Manganese Dioxide non-rechargeable D-cell. Ultralife has had this cell in production since 2001, with millions of units produced. The cell is widely-used for global defense and commercial applications. This battery product has gone through rigorous safety and qualification testing, including United Nations Transport of Dangerous Goods, Manual of Tests and Criteria, and is authorized for use in aerospace applications under Technical Standard Order C142.

On May 4, 2015, we were notified of a lawsuit in which we were named, along with other suppliers to the aircraft manufacturer, concerning that 2013 fire. The suit was filed by EA in the Commercial Court, Queen’s Bench Division of the High Court of Justice, London and seeks as damages \$42,000 plus other unspecified amounts, including those for loss of use and diminution in value of the aircraft. We maintain liability and products liability insurance through reputable providers, and in accordance with our corporate practices, immediately advised and referred this matter to our insurers. We are working with those insurers and their counsel to actively defend against this action, which is ongoing.

At this time, we believe that there is not a reasonable possibility that this incident will result in a material financial exposure to the Company.

Arista Power Litigation

Since September 2011, we have been pursuing legal action against Arista Power, Inc. (“Arista”) and our former employee, David Modeen, for, among other things, alleged breach of certain agreements, duties and obligations, including misappropriation of our confidential information and trade secrets, tortious interference, and breach of contract. On January 12, 2016, Arista filed for liquidation under Chapter 7 of the bankruptcy laws of the United States, without accurately identifying our ongoing lawsuit against them. Although we have not withdrawn our lawsuit, nor has it been dismissed, the Company did not submit a Proof of Claim in connection with Arista’s bankruptcy filing, nor does it intend to actively pursue its claims against Arista at this time.

Note 8 - Shareholders' Equity

a. *Stock-Based Compensation Expense*

We recorded non-cash stock compensation expense in each period as follows:

| | 2016 | 2015 |
|-------------------------|---------------|---------------|
| Stock Options | \$ 676 | \$ 489 |
| Restricted Stock Grants | 34 | 82 |
| Total | <u>\$ 710</u> | <u>\$ 571</u> |

These are more fully discussed as follows:

b. *Stock Options*

We have various stock-based employee compensation plans, for which compensation cost is recognized in the financial statements. The cost is measured at the grant date, based on the fair value of the award, and is recognized as an expense over the employee's requisite service period (generally the vesting period of the equity award).

Our shareholders have approved various equity-based plans that permit the grant of stock options, restricted stock and other equity-based awards. In addition, our shareholders have approved the grant of stock options outside of these plans.

In June 2004, our shareholders adopted the 2004 Long-Term Incentive Plan ("2004 LTIP") pursuant to which we were authorized to issue up to 750,000 shares of common stock and grant stock options, restricted stock awards, stock appreciation rights and other stock-based awards. Through shareholder approved amendments to the LTIP in 2006, 2008, 2011, and 2013, the total number of shares authorized under the LTIP was increased to 2,900,000.

In June 2014, our shareholders approved the 2014 Long-Term Incentive Plan ("2014 LTIP") as the successor plan to the 2004 LTIP that expired on June 10, 2014. Under the 2014 LTIP, a total of 1,750,000 shares of Common Stock will be available for grant of awards. However, of the total number of shares of common stock available for awards under the 2014 LTIP, no more than 800,000 shares of Common Stock may be used for awards other than stock options and stock appreciation rights. Grants under the 2014 LTIP may be awarded through June 2, 2024.

Stock options granted under the LTIPs are either Incentive Stock Options ("ISOs") or Non-Qualified Stock Options ("NQSOs"). Key employees are eligible to receive ISOs and NQSOs; however, directors and consultants are eligible to receive only NQSOs. Most ISOs vest over a three-year period and expire on the seventh anniversary of the grant date. All NQSOs issued to non-employee directors vest immediately and expire on the seventh anniversary of the grant date. As of December 31, 2016, there were 1,243,697 stock options outstanding under the 2004 LTIP and 679,884 stock options outstanding under the 2014 LTIP.

On December 30, 2010, pursuant to the terms of his employment agreement, we granted our President and Chief Executive Officer, Michael D. Popielec, options to purchase shares of common stock under the 2004 LTIP as follows: (i) 50,000 shares at \$6.42, vesting in annual increments of 12,500 shares over a four-year period commencing December 30, 2011; (ii) 250,000 shares at \$6.42, vesting in annual increments of 62,500 shares over a four-year period commencing December 30, 2011; (iii) 200,000 shares at \$10.00, with vesting to begin on the date the stock reaches a closing price of \$10.00 per share for 15 trading days within a 30-day trading period, with such vesting in annual increments of 50,000 shares over the four anniversary dates of that date; and (iv) 200,000 shares at \$15.00, with vesting to begin on the date the stock reaches a closing price of \$15.00 per share for 15 trading days within a 30-day trading period, with such vesting in annual increments of 50,000 shares over the four anniversary dates of that date. All such options in items (i) and (ii) shall expire on December 30, 2017. All such options in items (iii) and (iv) shall expire as of the later of December 30, 2017 and five years after the initial vesting commences, but in no event later than December 30, 2020. The market-based conditions for the stock options in items (iii) and (iv) had not been met as of December 31, 2016. The options set forth in items (ii), (iii) and (iv) were subject to shareholder approval of an amendment to the 2004 LTIP, which approval was obtained on June 7, 2011.

On January 3, 2011, pursuant to the terms of his employment agreement, we granted our President and Chief Executive Officer, Michael D. Popielec, an option to purchase 50,000 shares of common stock at \$6.58 under the 2004 LTIP. The option vested in annual increments of 12,500 shares over a four-year period commencing December 30, 2011. The option expires on December 30, 2017.

As of December 31, 2016, there was \$505 of total unrecognized compensation costs related to outstanding stock options, which we expect to recognize over a weighted average period of 1.1 years.

We use the Black-Scholes option-pricing model to estimate fair value of stock-based awards. The following weighted average assumptions were used to value options granted during the years ended December 31, 2016 and 2015:

| | Years Ended December 31, | |
|--|--------------------------|--------|
| | 2016 | 2015 |
| Risk-free interest rate | 1.36% | 0.72% |
| Volatility factor | 48.20% | 48.54% |
| Dividends | 0.00% | 0.00% |
| Weighted average expected life (years) | 4.83 | 4.15 |
| Forfeiture rate | 10.0% | 13.8% |

We used a Monte Carlo simulation option-pricing model to estimate the fair value of market performance stock-based awards, of which there were no new awards in the years ended December 31, 2016 or 2015.

We calculate expected volatility for stock options by taking an average of historical volatility over the expected term. The computation of expected term was determined based on historical experience of similar awards, giving consideration to the contractual terms of the stock-based awards and vesting schedules. The interest rate for periods within the contractual life of the award is based on the U.S. Treasury yield in effect at the time of grant. Forfeiture rates are calculated by dividing unvested shares forfeited by beginning shares outstanding. The pre-vesting forfeiture rate is calculated yearly and is determined using a historical twelve-quarter rolling average of the forfeiture rates.

The following tables summarize data for the stock options issued by us:

Year Ended December 31, 2016

| | Number of Shares | Weighted Average Exercise Price Per Share | Weighted Average Remaining Contractual Term | Aggregate Intrinsic Value |
|---|---------------------|---|---|---------------------------------|
| Shares under Option – January 1 | 2,257,969 | \$ 6.30 | | |
| Options Granted | 369,550 | 4.69 | | |
| Options Exercised | (152,789) | 3.86 | | |
| Options Forfeited or Expired | (151,149) | 6.09 | | |
| Shares under option – December 31 | <u>2,323,581</u> | <u>\$ 6.22</u> | <u>3.31</u> | <u>\$ 1,101</u> |
| Vested and Expected to Vest - December 31 | <u>2,192,138</u> | <u>\$ 6.31</u> | <u>2.98</u> | <u>\$ 1,006</u> |
| Options Exercisable – December 31 | <u>1,302,390</u> | <u>\$ 5.05</u> | <u>1.92</u> | <u>\$ 669</u> |

Year Ended December 31, 2015

| | Number of Shares | Weighted Average Exercise Price Per Share |
|-----------------------------------|---------------------|---|
| Shares under Option – January 1 | 2,056,122 | \$ 6.66 |
| Options Granted | 411,250 | 4.68 |
| Options Exercised | (137,937) | 3.90 |
| Options Forfeited or Expired | (71,466) | 11.86 |
| Shares under option – December 31 | <u>2,257,969</u> | <u>\$ 6.30</u> |
| Options Exercisable – December 31 | <u>1,255,736</u> | <u>\$ 5.22</u> |

The following table represents additional information about stock options outstanding at December 31, 2016:

| Range of Exercise Prices | Option Outstanding | | | Options Exercisable | |
|--------------------------|---|---|---------------------------------|--|---------------------------------|
| | Number of Outstanding Options – December 31, 2016 | Weighted-Average Remaining Contractual Life | Weighted-Average Exercise Price | Number of Options Exercisable at December 31, 2016 | Weighted-Average Exercise Price |
| \$3.22 - \$3.99 | 608,200 | 3.68 | \$ 3.76 | 394,218 | \$ 3.75 |
| \$4.00 - \$4.99 | 686,548 | 3.62 | \$ 4.40 | 396,006 | 4.45 |
| \$5.00 - \$9.99 | 628,833 | 2.17 | \$ 6.58 | 512,166 | 6.52 |
| \$10.00 - \$15.00 | 400,000 | 4.00 | \$ 12.50 | - | - |
| \$3.22 - \$15.00 | <u>2,323,581</u> | <u>3.31</u> | <u>\$ 6.22</u> | <u>1,302,390</u> | <u>\$ 5.05</u> |

The weighted average fair value of options granted during the years ended December 31, 2016 and 2015 was \$2.01 and \$2.32, respectively. The total intrinsic value of options (which is the amount by which the stock price exceeded the exercise price of the options on the date of exercise) exercised during the years ended December 31, 2016 and 2015 was \$149 and \$364, respectively.

Cash received from option exercises under our stock-based compensation plans for the years ended December 31, 2016 and 2015 was \$460 and \$538, respectively. There were no excess tax benefits realized in accumulated paid-in capital on exercised options for the years ended December 31, 2016 and 2015.

c. *Restricted Stock Awards*

During 2014, we awarded 49,200 restricted stock units under the 2014 LTIP to certain key employees. These units vest over three years and we estimated their weighted average grant date fair value to be \$3.24 per share. \$34 and \$82 of expense was recorded in 2016 and 2015, respectively, relating to these units. In September 2016, 15,900 shares of the awarded restricted stock vested and the Company repurchased 4,131 shares to satisfy the statutory tax withholding on shares vested for certain employees.

At December 31, 2016, there was \$11 of unrecognized compensation expense related to restricted stock grants.

d. *Reserved Shares*

We have reserved 901,700 shares of common stock under the various stock option plans, warrants and restricted stock awards as of December 31, 2016.

Note 9 - Income Taxes

Our income tax provision consists of:

| | Years Ended December 31, | |
|----------------------------|--------------------------|---------------|
| | 2016 | 2015 |
| Current: | | |
| Federal | \$ (70) | \$ 4 |
| State | 20 | 15 |
| Foreign | 13 | 111 |
| | <u>(37)</u> | <u>130</u> |
| Deferred: | | |
| Federal | 220 | 169 |
| State | - | - |
| Foreign | (85) | 11 |
| | <u>135</u> | <u>180</u> |
| Total income tax provision | <u>\$ 98</u> | <u>\$ 310</u> |

The deferred income tax provision is primarily due to the recognition of deferred tax liabilities relating to goodwill and certain intangible assets that cannot be predicted to reverse for book purposes during our loss carry-forward periods offset by the deferred tax benefit of the amortization of certain intangible assets of Accutronics (U.K.). The current income tax provision is primarily due to the income reported for Accutronics (U.K.) while the remaining expense is primarily due to state taxes. The benefit associated with the current income tax provision is primarily related to an excess accrual of income taxes in prior years. In 2015, the deferred provision was reduced by a deferred tax benefit amounting to \$51 relating to our \$150 impairment of a trademark.

Deferred income taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amount used for income tax purposes. Significant components of our deferred tax liabilities and assets are as follows:

| | Years Ended December 31, | |
|---|--------------------------|-----------------|
| | 2016 | 2015 |
| Deferred Tax Liabilities: | | |
| Property, Plant and Equipment | \$ - | \$ - |
| Intangible Assets | 5,471 | 4,631 |
| Total Deferred Tax Liabilities | <u>5,471</u> | <u>4,631</u> |
| Deferred Tax Assets: | | |
| Property, Plant and Equipment | 77 | 288 |
| Net Operating Loss Carry-Forwards | 27,127 | 27,283 |
| Tax Credit Carry-Forwards | 1,704 | 1,596 |
| Intangible Assets | 2,923 | 3,391 |
| Accrued Expenses, Reserves and Other | 1,527 | 2,127 |
| Total Deferred Tax Assets | <u>33,358</u> | <u>34,685</u> |
| Valuation Allowance for Deferred Tax Assets | <u>(33,331)</u> | <u>(34,593)</u> |
| Net Deferred Tax Assets | <u>27</u> | <u>92</u> |
| Net Deferred Tax Liabilities | <u>\$ 5,444</u> | <u>\$ 4,539</u> |

Net deferred tax liabilities are comprised of the following balance sheet amounts:

| | Years Ended December 31, | |
|--------------------------------------|--------------------------|-------------------|
| | 2016 | 2015 |
| Current Deferred Tax Assets | \$ 94 | \$ 92 |
| Non-Current Deferred Tax Liabilities | (5,538) | (4,631) |
| | <u>\$ (5,444)</u> | <u>\$ (4,539)</u> |

The valuation allowance for deferred tax assets decreased by \$1,262 and increased by \$6,642 in the years ended December 31, 2016 and 2015, respectively. The 2016 decrease in the valuation allowance was due to the reduction of deferred tax assets due to the Company's pretax income in 2016. The 2015 increase in the valuation allowance included an increase of \$7,296 relating to the release of our unrecognized tax benefit during 2015 (see below). Excluding the effect of the release of the unrecognized tax benefit during 2015, the valuation allowance would have decreased by \$654.

In 2016 and 2015, in the U.S. and certain operations in the U.K., we continue to report a valuation allowance for our deferred tax assets that cannot be offset by reversing temporary differences. We continue to conclude that, based on historical factors, it is more likely than not that we will not fully utilize our U.S. and U.K. NOLs that have accumulated over time. The recognition of a valuation allowance on our deferred tax assets results from our evaluation of all available evidence, both positive and negative. The assessment of the realizability of the NOLs is based on a number of factors including, our history of net operating losses, the volatility of our earnings, our historical operating volatility, our historical inability to accurately forecast earnings for future periods and the continued uncertainty of the general business climate as of the end of 2016. We believe that these historical factors represent negative evidence sufficient to conclude that we should record a full valuation allowance against our deferred tax assets. In both 2016 and 2015, we have not recorded a valuation allowance against our other foreign deferred tax assets as we believe that it is more likely than not that they will be realized. We continually assess the carrying value of this asset based on relevant accounting standards.

As of December 31, 2016, we have domestic and foreign NOLs totaling approximately \$70,976 and \$12,760, respectively, and domestic tax credits of approximately \$1,704, available to reduce future taxable income. Included in our NOL carry-forward are foreign loss carry-forwards of approximately \$12,760, nearly all of which can be carried forward indefinitely. The domestic NOL carry-forward of \$70,976 expires beginning in 2019, through 2034. The domestic NOL carry-forward includes approximately \$3,223 for which a benefit will be recorded in capital in excess of par value when realized.

At December 31, 2016, the undistributed earnings of the Company's foreign operations were indefinitely reinvested in those operations.

For financial reporting purposes, income (loss) from continuing operations before income taxes is as follows:

| | Years Ended December 31, | |
|---------------|---------------------------------|-----------------|
| | 2016 | 2015 |
| United States | \$ 2,803 | \$ 2,582 |
| Foreign | 777 | 568 |
| | <u>\$ 3,580</u> | <u>\$ 3,150</u> |

The provision for income taxes differs from the amount of income tax determined by applying the applicable U.S. statutory federal income tax rate to income (loss) from continuing operations before income taxes as follows:

| | Years Ended December 31, | |
|--|---------------------------------|-------------|
| | 2016 | 2015 |
| Statutory Income Tax Rate | 34.0% | 34.0% |
| (Increase) Decrease in Tax Provision Resulting From: | | |
| Equity Compensation | 9.6 | 2.2 |
| Income Tax Credits | (6.2) | (4.5) |
| Foreign Tax Rates | (2.2) | (2.2) |
| Release of Unrecognized Tax Benefits | - | (231.6) |
| Valuation Allowance | (30) | 210.9 |
| Excess Accrual | (5.2) | - |
| Other | 2.7 | 1.0 |
| Effective Income Tax Rate | <u>2.7%</u> | <u>9.8%</u> |

Accounting for Uncertainty in Income Taxes

Our unrecognized tax benefits related to uncertain tax positions at December 31, 2014 related to Federal and various state jurisdictions. We recorded the release of uncertain tax positions in 2015 relating to the conclusion of a federal tax examination, resulting in a \$21.4 million increase in the amount of our reported domestic NOL carry-forward. The following table summarizes the activity related to our unrecognized tax benefits:

| | Years Ended December 31, | |
|--|---------------------------------|-------------|
| | 2016 | 2015 |
| Balance – beginning of year | \$ - | \$ 7,296 |
| Increases related to current year tax positions | - | - |
| Increases related to prior year tax positions | - | - |
| Decreases related to prior year tax positions | - | - |
| Expiration of statute of limitations for assessment of taxes | - | - |
| Settlements of examinations | - | (7,296) |
| Balance – end of year | <u>\$ -</u> | <u>\$ -</u> |

The total unrecognized tax benefit balances at January 1, 2015 of \$7,296 was comprised of tax benefits that, if recognized, would result in a deferred tax asset and a corresponding increase in our valuation allowance. As a result, because the benefit would be offset by an increase in the valuation allowance, there would be no net effect on our effective tax rate or income tax provision. We recorded the release of this unrecognized tax benefit amount during 2015 upon the conclusion of a federal tax examination, resulting in a \$21.4 million increase in the amount of our reported domestic NOL carry-forward. There were no unrecognized tax benefits at December 31, 2016.

We are not required to accrue interest and penalties as the unrecognized tax benefits have been recorded as a decrease in our NOL. Interest and penalties would begin to accrue in the period in which the NOLs related to the uncertain tax positions are utilized. We do not expect our unrecognized tax benefits to change significantly over the next twelve months.

As a result of our operations, we file income tax returns in various jurisdictions including U.S. federal, U.S. state and foreign jurisdictions. We are routinely subject to examination by taxing authorities in these various jurisdictions. Our U.S. tax matters for the years 2001 through 2016 remain subject to examination by the Internal Revenue Service ("IRS") due to our NOL carry-forwards. Our U.S. tax matters for the years 2001 through 2016 remain subject to examination by various state and local tax jurisdictions due to our NOL carry-forwards. Our tax matters for the years 2009 through 2016 remain subject to examination by the respective foreign tax jurisdiction authorities.

Note 10 - 401(k) Retirement Benefit Plan

We maintain a defined contribution 401(k) plan covering substantially all employees. Employees can contribute a portion of their salary or wages as prescribed under Section 401(k) of the Internal Revenue Code and, subject to certain limitations, we may, at the discretion of our Board of Directors, authorize an employer contribution based on a portion of the employees' contributions. Since January 2010, we have matched 50% on the first 4% contributed by an employee, or a maximum of 2% of the employee's income. For 2016 and 2015, we contributed \$191 and \$201, respectively, to the 401(k) plan.

Note 11 - Business Segment Information

We report our results in two operating segments: Battery & Energy Products and Communications Systems. The Battery & Energy Products segment includes: Lithium 9-volt, cylindrical and various other non-rechargeable batteries, in addition to rechargeable batteries, uninterruptable power supplies, charging systems and accessories. The Communications Systems segment includes: RF amplifiers, power supplies, cable and connector assemblies, amplified speakers, equipment mounts, case equipment, integrated communication system kits and communications and electronics systems design. We believe that reporting performance at the gross profit level is the best indicator of segment performance. As such we report segment performance at the gross profit level and operating expenses as Corporate charges.

2016:

| | Battery & Energy Products | Communications Systems | Corporate | Total |
|--|---------------------------------|---------------------------|------------------|------------------|
| Revenue | \$ 64,753 | \$ 17,707 | \$ - | \$ 82,460 |
| Segment Contribution | 19,580 | 5,528 | (21,345) | 3,763 |
| Interest Expense, Net | | | (263) | (263) |
| Miscellaneous | | | 80 | 80 |
| Income Tax Provision | | | (98) | (98) |
| Non-Controlling Interest | | | 27 | 27 |
| Net Income Attributable to Ultralife | | | | \$ 3,509 |
| Total Assets | \$ 39,691 | \$ 32,021 | \$ 13,032 | \$ 84,744 |
| Capital Expenditures | 852 | 158 | 367 | 1,377 |
| Goodwill | 8,472 | 11,493 | | 19,965 |
| Depreciation and Amortization of Intangible Assets | 2,042 | 541 | 143 | 2,726 |
| Stock-Based Compensation | 403 | 110 | 197 | 710 |

2015:

| | Battery & Energy Products | Communications Systems | Corporate | Total |
|--|---------------------------------|---------------------------|------------------|------------------|
| Revenue | \$ 65,272 | \$ 11,155 | \$ - | \$ 76,427 |
| Segment Contribution | 18,698 | 4,618 | (19,986) | 3,330 |
| Interest Expense, Net | | | (245) | (245) |
| Miscellaneous | | | 65 | 65 |
| Income Tax Provision | | | (310) | (310) |
| Non-Controlling Interest | | | 29 | 29 |
| Net Loss Attributable to Ultralife | | | | \$ 2,869 |
| Total Assets | \$ 35,295 | \$ 28,849 | \$ 17,378 | \$ 81,522 |
| Capital Expenditures | 355 | 973 | 562 | 1,890 |
| Goodwill | 4,790 | 11,493 | | 16,283 |
| Depreciation and Amortization of Intangible Assets | 1,625 | 98 | 984 | 2,707 |
| Intangible Asset Impairment | | 150 | | 150 |
| Stock-Based Compensation | 46 | 3 | 522 | 571 |

U.S. and Non-U.S. Revenue Information¹:

| 2016: | Total Revenue | United States | Non-United States |
|---------------------------|--------------------------|--------------------------|------------------------------|
| Battery & Energy Products | \$ 64,753 | \$ 29,587 | \$ 35,166 |
| Communications Systems | 17,707 | 15,507 | 2,200 |
| Total | \$ 82,460 | \$ 45,094 | \$ 37,366 |
| | | 55% | 45% |

| 2015: | Total Revenue | United States | Non-United States |
|---------------------------|--------------------------|--------------------------|------------------------------|
| Battery & Energy Products | \$ 65,272 | \$ 37,106 | \$ 28,166 |
| Communications Systems | 11,155 | 9,635 | 1,520 |
| Total | \$ 76,427 | \$ 46,741 | \$ 29,686 |
| | | 61% | 39% |

¹ Sales classified to U.S. include shipments to U.S.-based prime contractors which in some cases may serve non-U.S. projects

Long-lived assets (including goodwill and intangible assets) held outside the U.S., principally in the United Kingdom and China, were \$11,652 and \$4,748 at December 31, 2016 and 2015, respectively.

Commercial and Government/Defense Revenue Information:

| 2016: | Total Revenue | Commercial | Government/ Defense |
|---------------------------|--------------------------|-------------------|--------------------------------|
| Battery & Energy Products | \$ 64,753 | \$ 40,886 | \$ 23,867 |
| Communications Systems | 17,707 | - | 17,707 |
| Total | \$ 82,460 | \$ 40,886 | \$ 41,574 |
| | | 50% | 50% |

| 2015: | Total Revenue | Commercial | Government/ Defense |
|---------------------------|--------------------------|-------------------|--------------------------------|
| Battery & Energy Products | \$ 65,272 | \$ 33,367 | \$ 31,905 |
| Communications Systems | 11,155 | - | 11,155 |
| Total | \$ 76,427 | \$ 33,367 | \$ 43,060 |
| | | 44% | 56% |

Note 12 – Due from Insurance Company

In June 2011, we experienced a fire that damaged certain inventory and machinery and equipment at our facility in China. The fire occurred after business hours and was fully extinguished quickly with no injuries, and the plant was back in full operation shortly thereafter with no significant disruption in supply or service to customers. We maintain adequate insurance coverage for this operation.

The total amount of the loss pertaining to assets and the related expenses was approximately \$1,589, including damaged inventory, business interruption and lost profits. We have pursued a claim against our insurance policy, with the majority of our insurance claim related to the recovery of damaged inventory. We had received payments in June 2012 and April 2013 totaling approximately \$1,286 as a partial payment on our insurance claim, which resulted in no gain or loss being recognized. Since the filing of the claim and through June 26, 2016, we reflected a receivable from the insurance company of \$177, net of our deductible of approximately \$126, representing additional proceeds expected to be received. On September 6, 2016, our claim was finalized with the insurance company resulting in a \$55 loss included in our 2016 results.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation Of Disclosure Controls And Procedures – Our president and chief executive officer (principal executive officer) and our chief financial officer and treasurer (principal financial officer) have evaluated our disclosure controls and procedures (as defined in Securities Exchange Act Rule 13a-15(e)) as of the end of the period covered by this annual report. Based on this evaluation, our president and chief executive officer and chief financial officer and treasurer concluded that our disclosure controls and procedures were effective as of such date.

Changes In Internal Controls Over Financial Reporting – There has been no change in our internal control over financial reporting (as defined in Securities Exchange Act Rule 13a-15(f)) that occurred during the fourth quarter of the fiscal year covered by this annual report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Management’s Report on Internal Control over Financial Reporting – Our management team is responsible for establishing and maintaining adequate internal control over our financial reporting. Our internal control over financial reporting is a process designed 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. Because of the inherent limitations of internal control systems, our internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with policies or procedures may deteriorate.

Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2016. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”) in *Internal Control-Integrated Framework (2013)*. Based on our assessment, we concluded that, as of December 31, 2016, our internal control over financial reporting was effective based on those criteria.

ITEM 9B. OTHER INFORMATION

None.

PART III

The information required by Part III, other than as set forth in Item 12, and each of the following items is omitted from this report and will be presented in our definitive proxy statement ("Proxy Statement") to be filed pursuant to Regulation 14A, not later than 120 days after the end of the fiscal year covered by this report, in connection with our 2017 Annual Meeting of Shareholders, which information included therein is incorporated herein by reference.

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The sections entitled "Election of Directors", "Executive Officers", "Section 16(a) Beneficial Ownership Reporting Compliance" and "Corporate Governance" in the Proxy Statement are incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

The sections entitled "Executive Compensation", "Directors Compensation", "Employment Arrangements" and "Compensation and Management Committee" in the Proxy Statement are incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The section entitled "Security Ownership of Certain Beneficial Owners" and "Security Ownership of Management" in the Proxy Statement is incorporated herein by reference.

Equity Compensation Plan Information

| Plan Category | Number of securities to be issued upon exercise of outstanding options, warrants and rights (a) | Weighted-average exercise price of outstanding options, warrants and rights (b) | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c) |
|--|--|--|--|
| Equity compensation plans approved by security holders | 2,323,581 | \$ 6.22 | 901,700 |
| Equity compensation plans not approved by security holders | - | - | - |
| Total | <u>2,323,581</u> | <u>\$ 6.22</u> | <u>901,700</u> |

See Note 8 in Notes to Consolidated Financial Statements for additional information.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The section entitled "Corporate Governance - General" in the Proxy Statement is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The section entitled "Proposal to Ratify the Selection of Independent Registered Accounting Firm - Principal Accountant Fees and Services" in the Proxy Statement is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a) Documents filed as part of this report:

1. Financial Statements

The financial statements and schedules required by this Item 15 are set forth in Part II, Item 8 of this report.

(b) Exhibits. The following exhibits are filed as a part of this report:

| Exhibit Index | Description of Document | Incorporated By Reference from: |
|---------------|---|---|
| 2.1 | Stock Purchase Agreement by and between BCF Solutions, Inc. and Ultralife Corporation | Exhibit 2.1 of the Form 10-Q for the quarter ended September 30, 2012, filed November 8, 2012 |
| 2.2 | Stock Purchase Agreement Relating to Accutronics Limited by and between Robert Andrew Phillips and Others and Ultralife Corporation | Exhibit 2.2 of the Form 10-K for the year ended December 31, 2015, filed March 2, 2016 |
| 3.1 | Restated Certificate of Incorporation | Exhibit 3.1 of the Form 10-K for the year ended December 31, 2008, filed March 13, 2009 |
| 3.2 | Amended and Restated By-laws | Exhibit 3.2 of the Form 8-K filed December 9, 2011 |
| 4.1 | Specimen Stock Certificate | Exhibit 4.1 of the Form 10-K for the year ended December 31, 2008, filed March 13, 2009 |
| 10.1* | Technology Transfer Agreement relating to Lithium Batteries | Exhibit 10.19 of our Registration Statement on Form S-1 filed on October 7, 1994, File No. 33-84888 (the "1994 Registration Statement") |
| 10.2* | Technology Transfer Agreement relating to Lithium Batteries | Exhibit 10.20 of the 1994 Registration Statement |
| 10.3* | Amendment to the Agreement relating to rechargeable batteries | Exhibit 10.24 of our Form 10-K for the fiscal year ended June 30, 1996 (this Exhibit may be found in SEC File No. 0-20852) |
| 10.4† | Ultralife Corporation 2014 Long-Term Incentive Plan | Appendix A to our Definitive Proxy Statement filed on April 21, 2014 |
| 10.5† | Ultralife Batteries, Inc. Amended and Restated 2004 Long-Term Incentive Plan | Exhibit 99.2 of our Registration Statement on Form S-8 filed on July 26, 2004, File No. 333-117662 |
| 10.6† | Amendment No. 1 to Ultralife Batteries, Inc. Amended and Restated 2004 Long-Term Incentive Plan | Exhibit 99.3 of our Registration Statement on Form S-8 filed August 18, 2006, File No. 333-136737 |
| 10.7† | Amendment No. 2 to Ultralife Batteries, Inc. Amended and Restated 2004 Long-Term Incentive Plan | Exhibit 99.4 of our Registration Statement on Form S-8 filed November 13, 2008, File No. 333-155349 |
| 10.8† | Amendment No. 3 to Ultralife Batteries, Inc. Amended and Restated 2004 Long-Term Incentive Plan | Exhibit 99.5 of our Registration Statement on Form S-8 filed November 13, 2008, File No. 333-155349 |
| 10.9† | Employment Agreement between the Registrant and Peter F. Comerford | Exhibit 10.30 of the Form 10-K for the year ended December 31, 2009, filed March 16, 2010 |
| 10.10† | Employment Agreement between the Registrant and Michael D. Popielec dated December 6, 2010 | Exhibit 10.40 of the Form 10-K for the year ended December 31, 2010, filed March 15, 2011 |

| | | |
|---------|---|--|
| 10.11† | Revised definition of “Change in Control” for Ultralife Corporation Amended and Restated 2004 Long-Term Incentive Plan | Exhibit 10.1 of the Form 8-K filed on May 26, 2011 |
| 10.12 | Settlement Agreement between the Registrant and the United States of America dated June 1, 2011 | Exhibit 10.1 of the Form 8-K filed on June 2, 2011 |
| 10.13† | Amendment No. 4 to Ultralife Corporation Amended and Restated 2004 Long-Term Incentive Plan | Exhibit 4.5 of the Registration Statement on Form S-8 filed on January 30, 2012, File No. 333-179235 |
| 10.14† | Amendment No. 5 to Ultralife Corporation Amended and Restated 2004 Long-Term Incentive Plan | Exhibit 10.1 of the Form 8-K filed on May 26, 2011 |
| 10.15 | Revolving Credit, Guaranty, and Security Agreement between Ultralife Corporation and PNC Bank, National Association, dated May 24, 2013 | Exhibit 10.1 of the Form 10-Q for the quarter ended June 30, 2013, filed August 9, 2013 |
| 10.16† | Retirement and Consulting Agreement, Release and Waiver of All Claims, between Ultralife Corporation and Peter F. Comerford, dated May 28, 2013 | Exhibit 10.1 of the Form 10-Q for the quarter ended June 30, 2013, filed August 9, 2013 |
| 10.17† | Restricted Stock Unit Agreement between Ultralife Corporation and Michael D. Popielec. Dated June 4, 2013 | Exhibit 10.1 of the Form 10-Q for the quarter ended June 30, 2013, filed August 9, 2013 |
| 10.18† | Amended No. 6. to Ultralife Corporation Amended and Restated 2004 Long-Term Incentive Plan | Appendix A of Form DEF 14A filed on April 22, 2013 |
| 10.19 | Amendment No. 1, dated April 30, 2014, to the Revolving Credit, Guaranty, and Security Agreement between Ultralife Corporation and PNC Bank, National Association, dated May 24, 2013 | Exhibit 10.1 of the Form 10-Q for the quarter ended March 30, 2014, filed May 9, 2014 |
| 10.20 | Amendment No. 2, dated October 28, 2014, to the Revolving Credit, Guaranty, and Security Agreement between Ultralife Corporation and PNC Bank, National Association, dated May 24, 2013 | Exhibit 10.1 of the Form 10-Q for the quarter ended September 28, 2014, filed November 3, 2014 |
| 10.21 | Amendment No. 3, dated April 30, 2015, to the Revolving Credit, Guaranty, and Security Agreement between Ultralife Corporation and PNC Bank, National Association, dated May 24, 2013 | Exhibit 10.1 of the Form 8-K filed on April 30, 2015 |
| 10.22 | Amendment No. 4, dated June 5, 2015, to the Revolving Credit, Guaranty, and Security Agreement between Ultralife Corporation and PNC Bank, National Association, dated May 24, 2013 | Exhibit 10.1 of the Form 8-K filed on June 5, 2015 |
| 10.23 | Amendment No. 5, dated January 13, 2016, to the Revolving Credit, Guaranty, and Security Agreement between Ultralife Corporation and PNC Bank, National Association, dated May 24, 2013 | Exhibit 10.1 of the Form 8-K filed on January 20, 2016 |
| 21 | Subsidiaries | Filed herewith |
| 23.1 | Consent of Freed Maxick CPAs, P.C. | Filed herewith |
| 23.2 | Consent of Bonadio & Co., LLP | Filed herewith |
| 31.1 | CEO 302 Certifications | Filed herewith |
| 31.2 | CFO 302 Certifications | Filed herewith |
| 32 | 906 Certifications | Filed herewith |
| 100.INS | XBRL Instance Document | Filed herewith |
| 100.SCH | XBRL Taxonomy Extension Schema Document | Filed herewith |
| 100.CAL | XBRL Taxonomy Calculation Linkbase Document | Filed herewith |
| 100.LAB | XBRL Taxonomy Label Linkbase Document | Filed herewith |
| 100.PRE | XBRL Taxonomy Presentation Linkbase Document | Filed herewith |
| 100.DEF | XBRL Taxonomy Definition Document | Filed herewith |

* Confidential treatment has been granted as to certain portions of this exhibit.

† Management contract or compensatory plan or arrangement.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

ULTRALIFE CORPORATION

Date: February 9, 2017

/s/ Michael D. Popielec
Michael D. Popielec
President, Chief Executive Officer and Director

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

Date: February 9, 2017

/s/ Michael D. Popielec
Michael D. Popielec
President, Chief Executive Officer and Director
(Principal Executive Officer)

Date: February 9, 2017

/s/ Philip A. Fain
Philip A. Fain
Chief Financial Officer and Treasurer
(Principal Financial Officer and Principal
Accounting Officer)

Date: February 9, 2017

/s/ Steven M. Anderson
Steven M. Anderson (Director)

Date: February 9, 2017

/s/ Thomas L. Saeli
Thomas L. Saeli (Director)

Date: February 9, 2017

/s/ Robert W. Shaw II
Robert W. Shaw II (Director)

Date: February 9, 2017

/s/ Ranjit C. Singh
Ranjit C. Singh (Director)

Date: February 9, 2017

/s/ Bradford T. Whitmore
Bradford T. Whitmore (Director)

Index to Exhibits

| | |
|---------|--|
| 21 | Subsidiaries |
| 23.1 | Consent of Freed Maxick, CPAs. P.C. |
| 23.2 | Consent of Bonadio & Co., LLP |
| 31.1 | Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2 | Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32 | 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.LAB | XBRL Taxonomy Label Linkbase Document |
| 101.PRE | XBRL Taxonomy Presentation Linkbase Document |
| 101.DEF | XBRL Taxonomy Definition Document |

SUBSIDIARIES

We have a 100% ownership interest in Ultralife Batteries (UK) LTD, incorporated in the United Kingdom.

We have a 100% ownership interest in ABLE New Energy Co., Limited, incorporated in Hong Kong, which has a 100% ownership interest in ABLE New Energy Co., Ltd, incorporated in the People's Republic of China.

We have a 100% ownership interest in Ultralife Energy Services Corporation, incorporated in Florida.

We have a 51% ownership interest in Ultralife Batteries India Private Limited, incorporated in India.

Through our ownership interest in Ultralife UK LTD, we have a 100% controlling interest in Accutronics, Ltd., also incorporated in the United Kingdom

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We hereby consent to the incorporation by reference in the Registration Statements on Forms S-8 (Nos. 333-117662, 333-136737, 333-155349, 333-179235 and 333-203037) of our report dated February 9, 2017 on the consolidated financial statements of Ultralife Corporation for the year ended December 31, 2016, which appear in this Form 10-K.

/s/ Freed Maxick CPAs, P.C.
Rochester, New York
February 9, 2017

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We hereby consent to the incorporation by reference in the Registration Statements on Forms S-8 (Nos. 333-117662, 333-136737, 333-155349, 333-179235 and 333-203037) of our report dated March 2, 2016 on the consolidated financial statements of Ultralife Corporation for the year ended December 31, 2015, which appear in this Form 10-K.

/s/ Bonadio & Co., LLP
Pittsford, New York
February 9, 2017

I, Michael D. Popielec, certify that:

1. I have reviewed this annual report on Form 10-K of Ultralife 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(s) 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, or caused 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(s) 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 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 9, 2017

/s/ Michael D. Popielec

Michael D. Popielec

President and Chief Executive Officer

I, Philip A. Fain, certify that:

1. I have reviewed this annual report on Form 10-K of Ultralife 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(s) 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, or caused 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(s) 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 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 9, 2017

/s/ Philip A. Fain

Philip A. Fain

Chief Financial Officer and Treasurer

Section 1350 Certification

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (“Section 906”), Michael D. Popielec and Philip A. Fain, the President and Chief Executive Officer and Chief Financial Officer and Treasurer, respectively, of Ultralife Corporation, certify that (i) the Annual Report on Form 10-K for the year ended December 31, 2016 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and (ii) the information contained in such report fairly presents, in all material respects, the financial condition and results of operations of Ultralife Corporation.

A signed original of this written statement required by Section 906 has been provided to Ultralife Corporation and will be retained by Ultralife Corporation and furnished to the Securities and Exchange Commission or its staff upon request.

Date: February 9, 2017

/s/ Michael D. Popielec

Michael D. Popielec

President and Chief Executive Officer

Date: February 9, 2017

/s/ Philip A. Fain

Philip A. Fain

Chief Financial Officer and Treasurer

This certification is being furnished as required by Rule 13a-14(b) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and Section 1350 of Chapter 63 of Title 18 of the United States Code, and shall not be deemed “filed” for purposes of Section 18 of the Exchange Act or otherwise subject to the liability of that Section. This certification shall not be deemed to be incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Exchange Act, except to the extent that we specifically incorporate this certification by reference.