

RICHARDSON ELECTRONICS LTD/DE  
Form 10-K  
July 29, 2016

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, DC 20549**

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**FORM 10-K**

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

**For the fiscal year ended May 28, 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: 0-12906**

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**(Exact name of registrant as specified in its charter)**

**Delaware** **36-2096643**  
**(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)**

**40W267 Keslinger Road, P.O. Box 393, LaFox, Illinois 60147-0393**

**(Address of principal executive offices)**

**Registrant's telephone number, including area code: (630) 208-2200**

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

|  |                                       |
|--|---------------------------------------|
| <b>Title of each class</b>                       | <b>Common stock, \$0.05 Par Value</b> |
| <b>Name of each exchange of which registered</b> | <b>NASDAQ Global Select Market</b>    |

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

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Indicate by check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes      No

Indicate by check mark whether the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act

Yes      No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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      No

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

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

|   |                           |
|---|---------------------------|
| Large Accelerated Filer   | Accelerated Filer         |
| Non-Accelerated Filer (Do not check if a smaller reporting company) | Smaller reporting company |

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

The aggregate market value of the registrant's common stock held by non-affiliates of the registrant as of November 28, 2015, was approximately \$61.0 million.

As of July 25, 2016, there were outstanding 10,702,932 shares of Common Stock, \$0.05 par value and 2,140,631 shares of Class B Common Stock, \$0.05 par value, which are convertible into Common Stock of the registrant on a one-for-one basis.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's Proxy Statement for the Annual Meeting of Stockholders scheduled to be held October 4, 2016, which will be filed pursuant to Regulation 14A, are incorporated by reference in Part III of this report. Except as specifically incorporated herein by reference, the abovementioned Proxy Statement is not deemed filed as part of this report.

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## **Forward Looking Statements**

Certain statements in this report may constitute “forward-looking” statements within the meaning of the Private Securities Litigation Reform Act of 1995. The terms “may”, “should”, “could”, “anticipate”, “believe”, “continues”, “estimate”, “expect”, “intend”, “objective”, “plan”, “potential”, “project”, and similar expressions are intended to identify forward-looking statements. These statements are not guarantees of future performance and involve risks, uncertainties, and assumptions that are difficult to predict. These statements are based on management’s current expectations, intentions, or beliefs and are subject to a number of factors, assumptions, and uncertainties that could cause actual results to differ materially from those described in the forward-looking statements. Factors that could cause or contribute to such differences or that might otherwise impact the business include the risk factors set forth in Item 1A of this Form 10-K. We undertake no obligation to update any such factor or to publicly announce the results of any revisions to any forward-looking statements contained herein whether as a result of new information, future events, or otherwise.

In addition, while we do, from time to time, communicate with securities analysts, it is against our policy to disclose to them any material non-public information, or other confidential commercial information. Accordingly, stockholders should not assume that we agree with any statement or report issued by any analyst irrespective of the content of the statement or report. Thus, to the extent that reports issued by securities analysts contain any projections, forecasts, or opinions, such reports are not our responsibility.

## **PART I**

### **ITEM 1. Business**

#### ***General***

Richardson Electronics, Ltd. is a leading global provider of engineered solutions, power grid and microwave tubes and related consumables; power conversion and RF and microwave components; high value displays, flat panel detector solutions and replacement parts for diagnostic imaging equipment; and customized display solutions. We serve customers in the alternative energy, healthcare, aviation, broadcast, communications, industrial, marine, medical, military, scientific and semiconductor markets. The Company’s strategy is to provide specialized technical expertise and “engineered solutions” based on our core engineering and manufacturing capabilities. The Company provides solutions and adds value through design-in support, systems integration, prototype design and manufacturing, testing, logistics, and aftermarket technical service and repair through its global infrastructure.

Our products include electron tubes and related components, microwave generators, subsystems used in semiconductor manufacturing, and visual technology solutions. These products are used to control, switch or amplify electrical power signals, or are used as display devices in a variety of industrial, commercial, medical, and communication applications.

During the first quarter of fiscal 2015, we created a new strategic business unit called Richardson Healthcare (“Healthcare”). As hospitals remain under pressure to reduce costs while serving a much larger customer base, there is a growing demand for independent sources of high-value replacement parts for diagnostic imaging. Having access to parts that are tested and in stock enables hospitals to terminate expensive service contracts with the Original Equipment Manufacturers (“OEM”) and instead use third party service providers or in-house technicians. With our global infrastructure, technical sales team, and experience servicing the healthcare market, we are well positioned to take advantage of this market opportunity. Over time, our plan is to expand our position from being the leader in power grid tubes to a key player in the high-growth, high-profile healthcare industry.

Our fiscal year 2016 began on May 31, 2015, and ended on May 28, 2016. Unless otherwise noted, all references in this document to a particular year shall mean our fiscal year.

## ***Geography***

We currently have operations in the following major geographic regions: North America, Asia/Pacific, Europe, and Latin America.

Selected financial data attributable to each segment and geographic region for fiscal 2016, 2015, and 2014 is set forth in Note 11 “Segment and Geographic Information” of the notes to our consolidated financial statements in Part II, Item 8 of this Annual Report on Form 10-K.

We have three operating and reportable segments, which we define as follows:

### ***Power and Microwave Technologies Group***

Power and Microwave Technologies Group (“PMT”), launched in July 2015, combines Electron Device Group’s (“EDG”) core engineered solutions, power grid and microwave tube business with new RF and power technologies. As a manufacturer and authorized distributor, PMT’s strategy is to provide specialized technical expertise and engineered solutions based on our core engineering and manufacturing capabilities. We provide solutions and add value through design-in support, systems integration, prototype design and manufacturing, testing, logistics, and aftermarket technical service and repair—all through our existing global infrastructure. PMT’s focus is on products for power, RF and microwave applications for customers in alternative energy, aviation, broadcast, communications, industrial, marine, medical, military, scientific, and semiconductor markets. PMT focuses on various applications including broadcast transmission, CO2 laser cutting, diagnostic imaging, dielectric and induction heating, high energy transfer, high voltage switching, plasma, power conversion, radar, and radiation oncology. PMT also offers its customers technical services for both microwave and industrial equipment.

PMT represents leading manufacturers of electron tubes and components used in semiconductor manufacturing equipment and industrial power applications. Among the suppliers they support are Amperex, CPI, Draloric, Eimac, General Electric, Hitachi, Jennings, L3, MaCom, National, NJRC, Thales, Toshiba, and Vishay.

PMT’s inventory levels reflect our commitment to maintain an inventory of a broad range of products for customers who are buying products for replacement of components used in critical equipment. PMT also sells a number of products representing trailing edge technology. While the market for these trailing edge technology products is declining, PMT is increasing its market share. PMT often buys products it knows it can sell ahead of any supplier

price increases. As manufacturers for these products exit the business, PMT has the option to purchase a substantial portion of their remaining inventory.

PMT has distribution agreements with many of its suppliers; most of these agreements provide exclusive distribution rights which often include global responsibility. The agreements are typically long term, and usually contain provisions permitting termination by either party if there are significant breaches which are not cured within a reasonable period of time. Although some of these agreements allow PMT to return inventory periodically, others do not, in which case PMT may have obsolete inventory that they cannot return to the supplier.

PMT's suppliers provide warranty coverage for the products and allow return of defective products, including those returned to PMT by its customers. For information regarding the warranty reserves, see Note 3 "Significant Accounting Policies" of the notes to our consolidated financial statements in Part II, Item 8 of this Annual Report on Form 10-K.

In addition to third party products, we sell proprietary products principally under certain trade names we own including: *Amperex*®, *Cetron*®, and *National*®. Our proprietary products include thyratrons and rectifiers, power tubes, ignitrons, magnetrons, phototubes, microwave generators, and liquid crystal display monitors. The materials used in the manufacturing process consist of glass bulbs and tubing, nickel, stainless steel and other metals, plastic and metal bases, ceramics, and a wide variety of fabricated metal components. These materials are generally readily available, but some components may require long lead times for production, and some materials are subject to shortages or price fluctuations based on supply and demand.



### *Canvys*

Canvys provides customized display solutions serving the corporate enterprise, financial, healthcare, industrial, and medical original equipment manufacturers (“OEM”) markets. Our engineers design, manufacture, source, and support a full spectrum of solutions to match the needs of our customers. We offer custom display solutions that include touch screens, protective panels, custom enclosures, specialized cabinet finishes, and application specific software packages. Our volume commitments are much lower than those of the large display manufacturers, making us the ideal choice for companies with very specific design requirements. We partner with both private label manufacturing companies and leading branded hardware vendors to offer the high quality liquid crystal displays, mounting devices, and customized computing platforms.

We have long-standing relationships with key component and finished goods manufacturers including 3M, LG, NEC Displays, and several key Asian display manufacturers that manufacture products to our specifications. We believe supplier relationships, combined with our engineering design and manufacturing capabilities and private label partnerships, allow us to maintain a well-balanced and technologically advanced offering of customer specific display solutions.

### *Healthcare*

Healthcare, included in Canvys prior to fiscal year 2015, manufactures, distributes and services high value replacement parts for the healthcare market including hospitals, medical centers, independent service organizations, and multi-vendor service providers. Products include power grid tubes, hydrogen thyratrons, klystrons, magnetrons; Image Systems medical displays and workstations for picture archiving and communication systems (“PACS”); visual solutions for operating rooms/surgical environments; digital radiography solutions including replacement flat panel detectors and upgrades; and additional replacement components currently under development for the diagnostic imaging service market. Through a combination of newly developed products and partnerships, service offerings, and training programs, we believe we can help our customers improve efficiency and deliver better clinical outcomes while lowering the cost of healthcare delivery.

### *Sales and Product Management*

As of the end of fiscal 2016, we employed 179 sales and product management personnel worldwide. In addition, we have authorized representatives, who are not our employees, selling our products primarily in regions where we do not have a direct sales presence.

We offer various credit terms to qualifying customers as well as cash in advance and credit card terms. We establish credit limits for each customer and routinely review delinquent and aging accounts.

### ***Distribution***

We maintain approximately 110,700 part numbers in our product inventory database and we estimate that more than 90% of orders received by 6:00 p.m. local time are shipped complete the same day if product is in stock. Customers can access our products on our web sites, *www.rell.com*, *www.rellhealthcare.com*, *www.canvys.com*, and *www.rellaser.com*, through electronic data interchange, or by telephone. Customer orders are processed by our regional sales offices and supported primarily by one of our distribution facilities in LaFox, Illinois; Amsterdam, Netherlands; Marlborough, Massachusetts; Plymouth, Minnesota; Donaueschingen, Germany; or Singapore, Singapore. We also have satellite warehouses in Sao Paulo, Brazil; Shanghai, China; Bangkok, Thailand; and Hook, United Kingdom. Our data processing network provides on-line, real-time interconnection of all sales offices and central distribution operations, 24 hours per day, seven days per week. Information on stock availability, pricing in local currency, cross-reference information, customers, and market analyses are obtainable throughout the entire distribution network.

### ***International Sales***

During fiscal 2016, approximately 54% of our sales were made outside the U.S. We continue to pursue new international sales to further expand our geographic reach.

### ***Employees***

As of May 28, 2016, we employed 373 full-time individuals. Of these, 241 were located in the United States and 132 were located internationally. The worldwide employee base included 179 in sales and product management and an additional 194 employees in distribution support, administrative positions, and value-add and manufacturing. All of our employees are non-union, and we consider our relationships with our employees to be good.

### ***Website Access to SEC Reports***

We maintain an Internet website at [www.rell.com](http://www.rell.com). Our Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities and Exchange Act of 1934 are accessible through our website, free of charge, as soon as reasonably practicable after these reports are filed electronically with the Securities and Exchange Commission. Interactive Data Files pursuant to Rule 405 of Regulation S-T, of these filing dates, formatted in Extensible Business Reporting Language (“XBRL”) are accessible as well. To access these reports, go to our website at [www.rell.com](http://www.rell.com). The foregoing information regarding our website is provided for convenience and the content of our website is not deemed to be incorporated by reference in this report filed with the Securities and Exchange Commission.

## **ITEM 1A. Risk Factors**

Investors should consider carefully the following risk factors in addition to the other information included and incorporated by reference in this Annual Report on Form 10-K that we believe are applicable to our businesses and the industries in which we operate. While we believe we have identified the key risk factors affecting our businesses, there may be additional risks and uncertainties that are not presently known or that are not currently believed to be significant that may adversely affect our results of operations.

### ***We may not achieve our plan for sales growth and margin targets.***

We have established both margin and expense targets to grow our sales with new and existing customers. If we do not achieve our growth objectives, the complexity of our global infrastructure makes it difficult to leverage our fixed cost structure to align with the size of our operations. Factors that could have a significant effect on our ability to achieve these goals include the following:

- Failure to achieve our sales and margin growth objectives in our product lines and business units;
- Failure to identify, consummate and successfully integrate acquisitions;
- Declining gross margin reflecting competitive pricing pressures or product mix; and,
- Limitations on our ability to leverage our support-function cost structure while maintaining an adequate structure to achieve our growth objectives.

### ***We have historically incurred significant charges for inventory obsolescence, and may incur similar charges in the future.***

We maintain significant inventories in an effort to ensure that customers have a reliable source of supply. Our products generally support industrial machinery that is powered by tube technology. As technology evolves and this capital equipment is replaced, the market for our products potentially declines. In addition, the market for many of our other products is characterized by rapid change resulting from the development of new technologies, evolving industry standards, frequent new product introductions by some of our suppliers and changing end-user demand, which can contribute to the decline in value or obsolescence of our inventory. We do not have many long-term supply contracts with our customers. If we fail to anticipate the changing needs of our customers or we fail to accurately forecast customer demand, our customers may not place orders with us, and we may accumulate significant inventories of products which we may be unable to sell or return to our vendors. This may result in a decline in the

value of our inventory.

***We face competitive pressures that could have a material adverse effect on our business.***

Our overall competitive position depends on a number of factors including price, engineering capability, vendor representation, product diversity, lead times and the level of customer service. There are very few vacuum tube competitors in the markets we serve. There are also a limited number of Chinese manufacturers whose ability to produce vacuum tubes has progressed over the past several years. The most significant competitive risk comes from technical obsolescence. Canvys faces many competitors in the markets we serve. Increased competition may result in price reductions, reduced margins, or a loss of market share, any of which could materially and adversely affect our business, operating results, and financial condition. As we expand our business and pursue our growth initiatives, we may encounter increased competition from current and/or new competitors. Our failure to maintain and enhance our competitive position could have a material adverse effect on our business.

***A single stockholder has voting control over us.***

As of July 25, 2016, Edward J. Richardson, our Chairman, Chief Executive Officer and President, beneficially owned approximately 99% of the outstanding shares of our Class B common stock, representing approximately 66% of the voting power of the outstanding common stock. This share ownership permits Mr. Richardson to exert control over the outcome of stockholder votes, including votes concerning the election of directors, by-law amendments, possible mergers, corporate control contests, and other significant corporate transactions.

***We are dependent on a limited number of vendors to supply us with essential products.***

Our principal products are capacitors, vacuum tubes and related products, microwave generators, and high voltage power supplies. The products we supply are currently produced by a relatively small number of manufacturers. One of our suppliers represents 11% of our total sales volume. Our success depends, in large part, on maintaining current vendor relationships and developing new relationships. To the extent that our significant suppliers are unwilling or unable to continue to do business with us, or extend lead times, or limit supplies due to capacity constraints, or other factors, there could be a material adverse effect on our business.

***International operations represent a significant percentage of our business and present a variety of risks which could impact our results.***

Because we source and sell our products worldwide, our business is subject to risks associated with doing business internationally. These risks include the costs and difficulties of managing foreign entities, limitations on the repatriation and investment of funds, cultural differences that affect customer preferences and business practices, unstable political or economic conditions, trade protection measures and import or export licensing requirements, and changes in tax laws.

We also face exposure to fluctuations in foreign currency exchange rates because we conduct business outside of the United States. Price increases caused by currency exchange rate fluctuations may make our products less competitive or may have an adverse effect on our margins. Our international revenues and expenses generally are derived from sales and operations in currencies other than the U.S. dollar. Accordingly, when the U.S. dollar strengthens in relation to the base currencies of the countries in which we sell our products, our U.S. dollar reported net revenue and income will decrease. We currently do not engage in any currency hedging transactions. We cannot predict whether foreign currency exchange risks inherent in doing business in foreign countries will have a material adverse effect on our operations and financial results in the future.

***Repatriation of cash held by our foreign subsidiaries to fund U.S. operations or strategic opportunities may be restricted or may subject us to a significant tax liability.***

As of May 28, 2016, \$52.7 million of cash, cash equivalents was held by our foreign subsidiaries. Some of these subsidiaries are located in jurisdictions which require foreign government approval before a cash repatriation can occur. In addition, under current tax law, repatriation of this cash may trigger significant adverse tax consequences in the U.S.

If the cash generated by our domestic operations is not sufficient to fund our domestic operations and our broader corporate initiatives, such as stock repurchases, dividends, acquisitions, and other strategic opportunities, we may need to raise additional funds through public or private debt or equity financings, or we may need to obtain new credit facilities to the extent we are unable to, or choose not to, repatriate our overseas cash. Such additional financing may not be available on terms favorable to us, or at all, and any new equity financings or offerings would dilute our current stockholders' ownership interests in us. Furthermore, lenders may not agree to extend us new, additional or continuing credit. In any such case, our business, operating results or financial condition could be adversely impacted.

### ***BREXIT/Europe***

In a non-binding referendum on the United Kingdom's membership in the European Union in June 2016, a majority of those who voted approved the United Kingdom's withdrawal from the European Union. Any withdrawal by the United Kingdom from the European Union ("Brexit") would occur after, or possibly concurrently with, a process of negotiation regarding the future terms of the United Kingdom's relationship with the European Union, which could result in the United Kingdom losing access to certain aspects of the single EU market and the global trade deals negotiated by the European Union on behalf of its members. The Brexit vote and the perceptions as to the impact of the withdrawal of the United Kingdom may adversely affect business activity, political stability and economic conditions in the United Kingdom, the European Union and elsewhere. Any of these developments, or the perception that any of these developments are likely to occur, could have a material adverse effect on economic growth or business activity in the United Kingdom, the Eurozone, or the European Union, and could result in the relocation of businesses, cause business interruptions, lead to economic recession or depression, and impact the stability of the financial markets, availability of credit, political systems or financial institutions and the financial and monetary system. Given that we conduct a substantial portion of our business in the European Union, these developments could have a material adverse effect on our business, financial position, liquidity and results of operations. The uncertainty concerning the timing and terms of the exit could also have a negative impact on the growth of the European economy and cause greater volatility in all of the global currencies that we currently use to transact business.

***We rely heavily on information technology systems which, if not properly functioning, could materially adversely affect our business.***

We rely on our information technology systems to process, analyze, and manage data to facilitate the purchase, manufacture, and distribution of our products, as well as to receive, process, bill, and ship orders on a timely basis. A significant disruption or failure in the design, operation, security or support of our information technology systems could significantly disrupt our business.

Our information technology systems may be subject to cyber attacks, security breaches or computer hacking. Experienced computer programmers and hackers may be able to penetrate our security controls and misappropriate or compromise sensitive personal, proprietary or confidential information, create system disruptions or cause shutdowns. They also may be able to develop and deploy viruses, worms and other malicious software programs that attack our systems or otherwise exploit any security vulnerabilities. Our systems and the data stored on those systems may also be vulnerable to security incidents or security attacks, acts of vandalism or theft, coordinated attacks by activist entities, misplaced or lost data, human errors, or other similar events that could negatively affect our systems and its data, as well as the data of our business partners. Further, third parties, such as hosted solution providers, that provide services to us, could also be a source of security risk in the event of a failure of their own security systems and infrastructure.

The costs to mitigate or address security threats and vulnerabilities before or after a cyber incident could be significant. Our remediation efforts may not be successful and could result in interruptions, delays or cessation of service, and loss of existing or potential suppliers or customers. In addition, breaches of our security measures and the unauthorized dissemination of sensitive personal, proprietary or confidential information about us, our business partners or other third parties could expose us to significant potential liability and reputational harm. As threats related to cyber attacks develop and grow, we may also find it necessary to make further investments to protect our data and infrastructure, which may impact our profitability. As a global enterprise, we could also be negatively impacted by existing and proposed laws and regulations, as well as government policies and practices related to cybersecurity, privacy, data localization and data protection.

***Our products may be found to be defective or our services performed may result in equipment or product damage and, as a result, warranty and/or product liability claims may be asserted against us.***

Many of our components are sold at prices that are significantly lower than the cost of the equipment or other goods in which they are incorporated. Since a defect or failure in a product could give rise to failures in the equipment that incorporates them, we may face claims for damages that are disproportionate to the revenues and profits we receive from the components involved in the claims. While we typically have provisions in our agreements with our suppliers that hold the supplier accountable for defective products, and we and our suppliers generally exclude consequential



damages in our standard terms and conditions, our ability to avoid such liabilities may be limited as a result of various factors, including the inability to exclude such damages due to the laws of some of the countries where we do business. Our business could be adversely affected as a result of a significant quality or performance issues in the components sold by us if we are required to pay for the damages. Although we have product liability insurance, such insurance is limited in coverage and amount.

***Substantial defaults by our customers on our accounts receivable or the loss of significant customers could have a significant negative impact on our business.***

We extend credit to our customers. The failure of a significant customer or a significant group of customers to timely pay all amounts due could have a material adverse effect on our financial condition and results of operations. The extension of credit involves considerable judgment and is based on management's evaluation of factors which include such things as a customer's financial condition, payment history, and the availability of collateral to secure customers' receivables.

***Failure to successfully implement our growth initiatives, or failure to realize the benefits expected from these initiatives if implemented, may create ongoing operating losses or otherwise adversely affect our business, operating results and financial condition.***

Our growth strategy focuses on expanding our healthcare and our power conversion businesses. On June 15, 2015, we acquired certain assets, including inventory, receivables, fixed assets, and certain other assets, of International Medical Equipment and Services, Inc. (“IMES”), for a purchase price of \$12.2 million. In July 2015, we launched Power and Microwave Technologies Group (“PMT”), which combines our core engineered solutions, power grid and microwave tube business with new RF and power technologies. We may be unable to implement our growth initiatives or reach profitability in the near future or at all, due to many factors, including factors outside of our control. If our investments in these growth initiatives do not yield anticipated returns for any reason, our business, operating results and financial condition may be adversely affected.

***We may not be successful in identifying, consummating and integrating future acquisitions.***

As part of our growth strategy, our intent is to acquire additional businesses or assets. We may not be able to identify attractive acquisition candidates or complete the acquisition of identified candidates at favorable prices and upon advantageous terms. Also, acquisitions are accompanied by risks, such as potential exposure to unknown liabilities and the possible loss of key employees and customers of the acquired business. In addition, we may not obtain the expected benefits or cost savings from acquisitions. Acquisitions are subject to risks associated with financing the acquisition, and integrating the operations, personnel and systems of the acquired businesses. If any of these risks materialize, they may result in disruptions to our business and the diversion of management time and attention, which could increase the costs of operating our existing or acquired businesses or negate the expected benefits of the acquisitions.

***Economic weakness and uncertainty could adversely affect our revenues and gross margins.***

Our revenues and gross profit margins depend significantly on global economic conditions, the demand for our products and services and the financial condition of our customers. Economic weakness and uncertainty have in the past resulted, and may result in the future, in decreased revenues and gross profit margins. Economic weakness and uncertainty also make it more difficult for us to forecast overall supply and demand with a great deal of confidence.

Our operating results during fiscal 2016 reflect an increase in our net loss. There can be no assurance that we will experience a recovery in the near future; nor is there any assurance that such worldwide economic volatility experienced recently will not continue.

***Major disruptions to our logistics capability could have a material adverse impact on our operations.***

Our global logistics services are operated through specialized and centralized distribution centers. We depend on third party transportation service providers for the delivery of products to our customers. A major interruption or disruption in service at any of our distribution centers for any reason (such as natural disasters, pandemics, or significant disruptions of services from our third party providers) could cause cancellations or delays in a significant number of shipments to customers and, as a result, could have a severe impact on our business, operations and financial performance.

***We may be subject to intellectual property rights claims, which are costly to defend, could require payment of damages or licensing fees, and/or could limit our ability to use certain technologies in the future.***

Substantial litigation and threats of litigation regarding intellectual property rights exist in the display systems and electronics industries. From time to time, third parties, including certain companies in the business of acquiring patents with the intention of aggressively seeking licensing revenue from purported infringers, may assert patent and/or other intellectual property rights to technologies that are important to our business. In any dispute involving products that we have sold, our customers could also become the target of litigation. We are obligated in many instances to indemnify and defend our customers if the products we sell are alleged to infringe any third party's intellectual property rights. In some cases, depending on the nature of the claim, we may be able to seek indemnification from our suppliers for our self and our customers against such claims, but there is no assurance that we will be successful in obtaining such indemnification or that we are fully protected against such claims. Any infringement claim brought against us, regardless of the duration, outcome or size of damage award, could result in substantial cost, divert our management's attention, be time consuming to defend, result in significant damage awards, cause product shipment delays, or require us to enter into royalty or other licensing agreements.

Additionally, if an infringement claim is successful we may be required to pay damages or seek royalty or license arrangements which may not be available on commercially reasonable terms. The payment of any such damages or royalties may significantly increase our operating expenses and harm our operating results and financial condition. Also, royalty or license arrangements may not be available at all. We may have to stop selling certain products or certain technologies, which could affect our ability to compete effectively.

Potential lawsuits, with or without merit, may divert management's attention, and we may incur significant expenses in our defense. In addition, we may be required to pay damage awards or settlements, become subject to injunctions or other equitable remedies, or determine to abandon certain lines of business, that may cause a material adverse effect on our results of operations, financial position, and cash flows.

***If we fail to maintain an effective system of internal controls or discover material weaknesses in our internal controls over financial reporting, we may not be able to detect fraud or report our financial results accurately or timely.***

An effective internal control environment is necessary for us to produce reliable financial reports and is an important part of our effort to prevent financial fraud. We are required to periodically evaluate the effectiveness of the design and operation of our internal controls over financial reporting. Based on these evaluations, we may conclude that enhancements, modifications, or changes to internal controls are necessary or desirable. While management evaluates the effectiveness of our internal controls on a regular basis, these controls may not always be effective. There are inherent limitations on the effectiveness of internal controls, including fraud, collusion, management override, and failure in human judgment. In addition, control procedures are designed to reduce rather than eliminate business risks.

If we fail to maintain an effective system of internal controls, or if management or our independent registered public accounting firm discovers material weaknesses in our internal controls, we may be unable to produce reliable financial reports or prevent fraud. In addition, we may be subject to sanctions or investigation by regulatory authorities, such as the Securities and Exchange Commission or NASDAQ. Any such actions could result in an adverse reaction in the financial markets due to a loss of confidence in the reliability of our financial statements.

***If we are deemed to be an investment company, we will be required to meet burdensome compliance requirements and restrictions on our activities.***

We currently have significant cash and investments. If we are deemed to be an "investment company" as defined under the Investment Company Act of 1940 (the "Investment Company Act"), the nature of our investments may be subject to various restrictions. We do not believe that our principal activities subject us to the Investment Company Act. If we

are deemed to be subject to the Investment Company Act, compliance with required additional regulatory burdens would increase our operating expenses.

*The company's goodwill and identifiable intangible assets could become impaired, which could reduce the value of our assets and reduce our net income in the year in which the write-off occurs.*

Our goodwill and intangible assets could become impaired, which could reduce the value of our assets and reduce our net income in the year in which the write-off occurs. We ascribe value to certain intangible assets, which consist of customer lists and trade names resulting from acquisitions. We may incur an impairment charge on goodwill or on intangible assets if we determine that the fair value of the intangible assets are less than their current carrying values. We evaluate whether events have occurred that indicate all, or a portion, of the carrying amount of goodwill or intangible assets may no longer be recoverable. If this is the case, an impairment charge to earnings would be necessary.

#### **ITEM 1B. Unresolved Staff Comments**

None.

**ITEM 2. Properties**

The Company owns two facilities and leases 30 facilities. We own our corporate facility and largest distribution center, which is located on approximately 100 acres in LaFox, Illinois and consists of approximately 242,000 square feet of manufacturing, warehouse, and office space. We maintain geographically diverse facilities because we believe this provides value to our customers and suppliers, and limits market risk and exchange rate exposure. We consider our properties to be well maintained, in sound condition, and adequate for our present needs. The extent of utilization varies from property to property and from time to time during the year.

Our facility locations, their primary use, and segments served are as follows:

| <b>Location</b>            | <b>Leased/Owned</b> | <b>Use</b>                                 | <b>Segment</b>        |
|----------------------------|---------------------|--|-----------------------|
| Woodland Hills, California | Leased              | Sales                                      | PMT                   |
| Farmington, Connecticut    | Leased              | Sales                                      | PMT                   |
| Brooksville, Florida       | Leased              | Sales                                      | PMT                   |
| Fort Lauderdale, Florida   | Leased              | Sales                                      | PMT                   |
| LaFox, Illinois *          | Owned               | Corporate/Sales/Distribution/Manufacturing | PMT/Canvys/Healthcare |
| Rockland, Massachusetts    | Leased              | Sales                                      | PMT                   |
| Marlborough, Massachusetts | Leased              | Sales/Distribution/Manufacturing           | Canvys                |
| Plymouth, Minnesota        | Leased              | Sales/Distribution/Manufacturing           | Healthcare            |
| Mint Hill, North Carolina  | Leased              | Sales                                      | PMT                   |
| Fort Mill, South Carolina  | Leased              | Sales/Distribution/Testing/Repair          | Healthcare            |
| Sao Paulo, Brazil          | Leased              | Sales/Distribution                         | PMT                   |
| Beijing, China             | Leased              | Sales                                      | PMT                   |
| Shanghai, China            | Leased              | Sales/Distribution                         | PMT                   |
| Shenzhen, China            | Leased              | Sales                                      | PMT                   |
| Nanterre, France           | Leased              | Sales                                      | PMT                   |
| Donaueschingen, Germany    | Leased              | Sales/Distribution/Manufacturing           | Canvys                |
| Meerbusch, Germany         | Leased              | Sales/Distribution/Testing                 | PMT                   |
| Puchheim, Germany          | Leased              | Sales                                      | PMT                   |
| Mumbai, India              | Leased              | Sales                                      | PMT                   |
| Florence, Italy            | Owned               | Sales                                      | PMT                   |
| Milan, Italy               | Leased              | Sales                                      | PMT                   |
| Tokyo, Japan               | Leased              | Sales                                      | PMT                   |
| Mexico City, Mexico        | Leased              | Sales                                      | PMT                   |
| Amsterdam, Netherlands     | Leased              | Sales/Distribution/Manufacturing           | PMT/Healthcare        |
| Singapore, Singapore       | Leased              | Sales/Distribution                         | PMT                   |
| Seoul, South Korea         | Leased              | Sales                                      | PMT                   |
| Madrid, Spain              | Leased              | Sales                                      | PMT                   |
| Taipei, Taiwan             | Leased              | Sales                                      | PMT/Canvys            |
| Bangkok, Thailand          | Leased              | Sales/Distribution                         | PMT                   |

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|                             |        |                                   |            |
|-----------------------------|--------|-----------------------------------|------------|
| Dubai, United Arab Emirates | Leased | Sales/Distribution/Testing/Repair | PMT        |
| Hook, United Kingdom        | Leased | Sales/Distribution/Testing/Repair | PMT        |
| Lincoln, United Kingdom     | Leased | Sales                             | PMT/Canvys |

\*LaFox, Illinois is also the location of our corporate headquarters.

### **ITEM 3. Legal Proceedings**

From time to time, we or our subsidiaries are involved in pending judicial proceedings concerning matters arising in the ordinary course of our business. While the outcome of litigation is subject to uncertainties, based on information at the time the financial statements were issued, we do not believe that the outcome of any current claims will have a material adverse effect on our consolidated financial position, results of operations, or cash flows.



**PART II****ITEM 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities***Unregistered Sales of Equity Securities*

None.

*Share Repurchases*

| Period                                | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Dollar Amount of Shares Purchased Under the Plans or Programs | Amounts Remaining Under the Share Repurchase Authorization |
|---------------------------------------|----------------------------------|------------------------------|--|---|--|
| May 31, 2015                          |                                  |                              |  |   | \$ 14,625,569  |
| June 1, 2015 - June 27, 2015          | —                                | \$ —                         | —  | \$ —  | \$ 14,625,569  |
| June 28, 2015 - July 25, 2015         | —                                | \$ —                         | —  | \$ —  | \$ 14,625,569  |
| July 26, 2015 - August 29, 2015       | 567,213                          | \$ 5.83                      | 567,213  | \$ 3,307,543  | \$ 11,318,026  |
| August 30, 2015 - September 26, 2015  | 172,519                          | \$ 5.93                      | 172,519  | \$ 1,023,272  | \$ 10,294,754  |
| September 27, 2015 - October 24, 2015 | 115,132                          | \$ 5.94                      | 115,132  | \$ 683,901  | \$ 9,610,853   |
| October 25, 2015 - November 28, 2015  | —                                | \$ —                         | —  | \$ —  | \$ 9,610,853   |
| November 29, 2015 - December 26, 2015 | —                                | \$ —                         | —  | \$ —  | \$ 9,610,853   |
| December 27, 2015 - January 23, 2016  | —                                | \$ —                         | —  | \$ —  | \$ 9,610,853   |
| January 24, 2016 - February 27, 2016  | —                                | \$ —                         | —  | \$ —  | \$ 9,610,853   |
| February 28, 2016 - March 26, 2016    | —                                | \$ —                         | —  | \$ —  | \$ 9,610,853   |
| March 27, 2016 - April 23, 2016       | —                                | \$ —                         | —  | \$ —  | \$ 9,610,853   |
| April 24, 2016 - May 28, 2016         | —                                | \$ —                         | —  | \$ —  | \$ 9,610,853   |

*Dividends*

Our quarterly dividend was \$0.06 per common share and \$0.054 per Class B common share. Annual dividend payments for fiscal year 2016 and fiscal year 2015 were approximately \$3.1 million and \$3.3 million, respectively. All future payments of dividends are at the discretion of the Board of Directors. Dividend payments will depend on earnings, capital requirements, operating conditions, and such other factors that the Board may deem relevant.

***Common Stock Information***

Our common stock is traded on the NASDAQ Global Select Market (“NASDAQ”) under the trading symbol (“RELL”). There is no established public trading market for our Class B common stock. As of July 25, 2016, there were approximately 576 stockholders of record for the common stock and approximately 16 stockholders of record for the Class B common stock. The following table sets forth the high and low closing sales price per share of RELL common stock as reported on the NASDAQ for the periods indicated.

**High and Low Closing Prices of Common Stock**

| Fiscal Quarter | 2016   |        | 2015    |        |
|----------------|--------|--------|---------|--------|
|                | High   | Low    | High    | Low    |
| First          | \$8.39 | \$5.47 | \$10.63 | \$9.93 |
| Second         | \$6.24 | \$5.55 | \$10.14 | \$9.71 |
| Third          | \$5.72 | \$4.75 | \$10.15 | \$9.10 |
| Fourth         | \$5.35 | \$4.90 | \$9.18  | \$8.65 |

***Performance Graph***

The following graph compares the performance of our common stock for the periods indicated with the performance of the NASDAQ Composite Index and NASDAQ Electronic Components Index. The graph assumes \$100 invested on the last day of our fiscal year 2011, in our common stock, the NASDAQ Composite Index, and NASDAQ Electronic Components Index. Total return indices reflect reinvestment of dividends at the closing stock prices at the date of the dividend declaration.

\*\$100 invested on 5/28/11 in stock or 5/31/11 in index, including reinvestment of dividends.

Indexes calculated on month-end basis.

**ITEM 6. Selected Financial Data****Five-Year Financial Review**

*This information should be read in conjunction with our consolidated financial statements, accompanying notes, and Management's Discussion and Analysis of Financial Condition and Results of Operations included elsewhere herein.*

|   | <b>Fiscal Year Ended <sup>(1)</sup></b>    |                 |                 |                 |                 |
|---|--|-----------------|-----------------|-----------------|-----------------|
|   | (in thousands , except per share amounts ) |                 |                 |                 |                 |
|   | May 28,<br>2016                            | May 30,<br>2015 | May 31,<br>2014 | June 1,<br>2013 | June 2,<br>2012 |
| <u>Statements of Income (Loss)</u>                          |  |                 |                 |                 |                 |
| Net sales   | \$142,016                                  | \$136,957       | \$137,960       | \$141,066       | \$157,836       |
| Continuing Operations                                       |  |                 |                 |                 |                 |
| Income (loss) from continuing operations before tax         | (6,220 )                                   | (6,994 )        | (652 )          | \$642           | \$7,656         |
| Income tax provision (benefit)                              | 546  | (1,466 )        | (307 )          | 160             | (334 )          |
| Income (loss) from continuing operations                    | \$(6,766 )                                 | \$(5,528 )      | \$(345 )        | \$482           | \$7,990         |
| Discontinued Operations                                     |  |                 |                 |                 |                 |
| Income (loss) from discontinued operations                  | —  | (31 )           | (170 )          | \$766           | \$536           |
| Net income (loss)   | \$(6,766 )                                 | \$(5,559 )      | \$(515 )        | \$1,248         | \$8,526         |
| Per Share Data  |  |                 |                 |                 |                 |
| Net income (loss) per Common share - Basic:                 |  |                 |                 |                 |                 |
| Income (loss) from continuing operations                    | \$(0.53 )                                  | \$(0.41 )       | \$(0.03 )       | \$0.03          | \$0.48          |
| Income (loss) from discontinued operations                  | —  | —               | (0.01 )         | 0.05            | 0.03            |
| Total net income (loss) per Common share - Basic:           | \$(0.53 )                                  | \$(0.41 )       | \$(0.04 )       | \$0.08          | \$0.51          |
| Net income (loss) per Class B common share - Basic:         |  |                 |                 |                 |                 |
| Income (loss) from continuing operations                    | \$(0.47 )                                  | \$(0.36 )       | \$(0.02 )       | \$0.03          | \$0.43          |
| Income (loss) from discontinued operations                  | —  | —               | (0.01 )         | 0.05            | 0.03            |
| Total net income (loss) per Class B common share - Basic:   | \$(0.47 )                                  | \$(0.36 )       | \$(0.03 )       | \$0.08          | \$0.46          |
| Net income (loss) per Common share - Diluted:               |  |                 |                 |                 |                 |
| Income (loss) from continuing operations                    | \$(0.53 )                                  | \$(0.41 )       | \$(0.03 )       | \$0.03          | \$0.47          |
| Income (loss) from discontinued operations                  | —  | —               | (0.01 )         | 0.05            | 0.03            |
| Total net income (loss) per Common share - Diluted:         | \$(0.53 )                                  | \$(0.41 )       | \$(0.04 )       | \$0.08          | \$0.50          |
| Net income (loss) per Class B common share - Diluted:       |  |                 |                 |                 |                 |
| Income (loss) from continuing operations                    | \$(0.47 )                                  | \$(0.36 )       | \$(0.02 )       | \$0.03          | \$0.43          |
| Income (loss) from discontinued operations                  | —  | —               | (0.01 )         | 0.05            | 0.03            |
| Total net income (loss) per Class B common share - Diluted: | \$(0.47 )                                  | \$(0.36 )       | \$(0.03 )       | \$0.08          | \$0.46          |
| Cash Dividend Data  |  |                 |                 |                 |                 |
| Dividends per common share                                  | \$0.24                                     | \$0.24          | \$0.24          | \$0.24          | \$0.20          |
| Dividends per Class B common share <sup>(2)</sup>           | \$0.22                                     | \$0.22          | \$0.22          | \$0.22          | \$0.18          |

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Balance Sheet Data

|                      |           |           |           |           |           |
|----------------------|-----------|-----------|-----------|-----------|-----------|
| Total assets         | \$168,130 | \$184,994 | \$203,545 | \$217,318 | \$231,423 |
| Stockholders' equity | \$141,675 | \$156,652 | \$174,845 | \$185,239 | \$200,213 |

(1) Our fiscal year ends on the Saturday nearest the end of May. Each of the fiscal years presented contain 52/53 weeks.

(2) The dividend per Class B common share is 90% of the dividend per Class A common share.

## ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the consolidated financial statements and related notes.

Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is intended to assist the reader in better understanding our business, results of operations, financial condition, changes in financial condition, critical accounting policies and estimates, and significant developments. MD&A is provided as a supplement to, and should be read in conjunction with, our consolidated financial statements and the accompanying notes appearing elsewhere in this filing. This section is organized as follows:

### •Business Overview

**Results of Continuing Operations** - an analysis and comparison of our consolidated results of operations for the fiscal years ended May 28, 2016, May 30, 2015, and May 31, 2014, as reflected in our consolidated statements of comprehensive income (loss).

**Liquidity, Financial Position, and Capital Resources** - a discussion of our primary sources and uses of cash for the fiscal years ended May 28, 2016, May 30, 2015, and May 31, 2014, and a discussion of changes in our financial position.

### Business Overview

Richardson Electronics, Ltd. is a leading global provider of engineered solutions, power grid and microwave tubes and related consumables; power conversion and RF and microwave components; high value displays, flat panel detector solutions and replacement parts for diagnostic imaging equipment; and customized display solutions. We serve customers in the alternative energy, healthcare, aviation, broadcast, communications, industrial, marine, medical, military, scientific and semiconductor markets. The Company's strategy is to provide specialized technical expertise and "engineered solutions" based on our core engineering and manufacturing capabilities. The Company provides solutions and adds value through design-in support, systems integration, prototype design and manufacturing, testing, logistics, and aftermarket technical service and repair through its global infrastructure.

Our products include electron tubes and related components, microwave generators, subsystems used in semiconductor manufacturing, and visual technology solutions. These products are used to control, switch or amplify electrical power signals, or are used as display devices in a variety of industrial, commercial, medical, and communication applications.

On June 15, 2015, Richardson Electronics, Ltd (“the Company”), acquired certain assets of International Medical Equipment and Services, Inc. (“IMES”), for a purchase price of \$12.2 million. This includes the purchase of inventory, receivables, fixed assets, and certain other assets of the Company. The Company did not acquire any liabilities of IMES. The total consideration paid excludes transaction costs.

IMES, based in South Carolina, provides reliable, cost-saving solutions worldwide for major brands of CT and MRI equipment. This acquisition positions Richardson Healthcare to provide cost effective diagnostic imaging replacement parts and training to hospitals, diagnostic imaging centers, medical institutions, and independent service organizations. IMES offers an extensive selection of replacement parts, as well as an interactive training center, on-site test bays and experienced technicians who provide 24/7 customer support. Replacement parts are readily available and triple tested to provide peace of mind when uptime is critical. IMES core operations will remain in South Carolina. Richardson Healthcare plans to expand IMES’ replacement parts and training offerings geographically leveraging the Company’s global infrastructure. During the fourth quarter of fiscal 2016, IMES opened up their first foreign location in Amsterdam.

We have three operating and reportable segments, which we define as follows:

Power and Microwave Technologies Group (“PMT”), launched in July 2015, combines Electron Device Group’s (“EDG”) core engineered solutions, power grid and microwave tube business with new RF and power technologies. As a manufacturer and authorized distributor, PMT’s strategy is to provide specialized technical expertise and engineered solutions based on our core engineering and manufacturing capabilities. We provide solutions and add value through design-in support, systems integration, prototype design and manufacturing, testing, logistics, and aftermarket technical service and repair—all through our existing global infrastructure. PMT’s focus is on products for power, RF and microwave applications for customers in alternative energy, aviation, broadcast, communications, industrial, marine, medical, military, scientific, and semiconductor markets. PMT focuses on various applications including broadcast transmission, CO2 laser cutting, diagnostic imaging, dielectric and induction heating, high energy transfer, high voltage switching, plasma, power conversion, radar, and radiation oncology. PMT also offers its customers technical services for both microwave and industrial equipment.

Canvys provides customized display solutions serving the corporate enterprise, financial, healthcare, industrial, and medical original equipment manufacturers (“OEM”) markets.

Healthcare manufactures, distributes and services high value replacement parts for the healthcare market including hospitals, medical centers, independent service organizations, and multi-vendor service providers. Products include power grid tubes, hydrogen thyratrons, klystrons, magnetrons; Image Systems medical displays and workstations for picture archiving and communication systems (“PACS”); visual solutions for operating rooms/surgical environments; digital radiography solutions including replacement flat panel detectors and upgrades; and additional replacement components currently under development for the diagnostic imaging service market. Through a combination of newly developed products and partnerships, service offerings, and training programs, we believe we can help our customers improve efficiency and deliver better clinical outcomes while lowering the cost of healthcare delivery.

We currently have operations in the following major geographic regions: North America, Asia/Pacific, Europe, and Latin America.

## **Results of Continuing Operations**

### ***Overview - Fiscal Year Ended May 28, 2016***

- Net sales for fiscal 2016 were \$142.0 million, up 3.7%, compared to net sales of \$137.0 during fiscal 2015.
- Gross margin was 31.6% of net sales for fiscal year 2016, compared to 30.0% of net sales for fiscal 2015.
- Selling, general, and administrative expenses increased to \$51.6 million, or 36.4% of net sales, for fiscal 2016, compared to \$49.2 million, or 35.9% of net sales, for fiscal 2015.
- Operating loss during fiscal 2016 was \$6.6 million, compared to \$8.1 million for fiscal 2015.
- Other income for fiscal 2016 was \$0.3 million, compared to other income of \$1.1 million for fiscal 2015.
- Loss from continuing operations during fiscal 2016 was \$6.8 million versus a loss of \$5.5 million during fiscal 2015.
- There were no results from discontinued operations during fiscal 2016, compared to loss from discontinued operations, net of tax, of less than \$0.1 million during fiscal 2015.
- Net loss during fiscal 2016 was \$6.8 million, compared to net loss of \$5.6 million during fiscal 2015.



*Net Sales and Gross Profit Analysis*

Net sales by segment and percent change for fiscal 2016, 2015, and 2014 were as follows (*in thousands*):

| Net Sales  | FY 2016   | FY 2015   | FY 2014   | <b>FY16 vs. FY15</b><br><b>% Change</b> | <b>FY15 vs. FY14</b><br><b>% Change</b> |
|------------|-----------|-----------|-----------|---|---|
| PMT        | \$105,554 | \$105,748 | \$103,274 | (0.2<br>%)                              | 2.4<br>%                                |
| Canvys     | 23,453    | 24,645    | 27,857    | (4.8<br>%)                              | (11.5<br>%)                             |
| Healthcare | 13,009    | 6,564     | 6,829     | 98.2<br>%                               | (3.9<br>%)                              |
| Total      | \$142,016 | \$136,957 | \$137,960 | 3.7<br>%                                | (0.7<br>%)                              |

During fiscal 2016 consolidated net sales increased by 3.7% compared to fiscal 2015. Sales for PMT declined by 0.2% and Canvys declined by 4.8%, offset by a 98.2% increase in sales for Healthcare. During fiscal 2015 consolidated net sales decreased 0.7% compared to fiscal 2014.

Gross profit by segment and percent of segment net sales for fiscal 2016, 2015, and 2014 were as follows (*in thousands*):

| Gross Profit | FY 2016  |       | FY 2015  |       | FY 2014  |       |
|--------------|----------|-------|----------|-------|----------|-------|
| PMT          | \$33,088 | 31.3% | \$33,098 | 31.3% | \$31,610 | 30.6% |
| Canvys       | 6,017    | 25.7% | 6,457    | 26.2% | 7,588    | 27.2% |
| Healthcare   | 5,730    | 44.0% | 1,583    | 24.1% | 1,816    | 26.6% |
| Total        | \$44,835 | 31.6% | \$41,138 | 30.0% | \$41,014 | 29.7% |

Gross profit reflects the distribution and manufacturing product margin less manufacturing variances, inventory obsolescence charges, customer returns, scrap and cycle count adjustments, engineering costs, unabsorbed manufacturing labor and overhead, and other provisions.

Consolidated gross profit was \$44.8 million during fiscal 2016, compared to \$41.1 million during fiscal 2015. Consolidated gross margin as a percentage of net sales increased to 31.6% during fiscal 2016, from 30.0% during fiscal 2015. Gross margin during fiscal 2016 included expense related to inventory provisions for PMT of \$0.3 million, \$0.4 million for Canvys, and less than \$0.1 million for Healthcare. Gross margin during fiscal 2015 included expense related to inventory provisions for PMT of \$0.1 million, \$0.1 million for Canvys, and less than \$0.1 million for Healthcare.

Consolidated gross profit was \$41.1 million during fiscal 2015, compared to \$41.0 million during fiscal 2014. Consolidated gross margin as a percentage of net sales increased slightly to 30.0% during fiscal 2015, from 29.7% during fiscal 2014. Gross margin during fiscal 2015 included expense related to inventory provisions for PMT of \$0.1 million, \$0.1 million for Canvys, and less than \$0.1 million for Healthcare. Gross margin during fiscal 2014 included expense related to inventory provisions for PMT of \$0.6 million and \$0.2 million for Canvys.

### ***Power and Microwave Technologies Group***

Net sales for PMT decreased 0.2% to \$105.6 million during fiscal 2016, from \$105.7 million during fiscal 2015. We recognized a large tube order for a military application and sales of power conversion and RF and microwave components increased. This was offset by a decline in the broadcast market along with specialty products manufactured in LaFox and sold primarily into the semiconductor capital equipment market. Gross margin as a percentage of net sales remained flat at 31.3% during fiscal 2016 compared to fiscal 2015.

Net sales for PMT increased 2.4% to \$105.7 million during fiscal 2015, from \$103.3 million during fiscal 2014. Net sales of engineered solutions including continuous wave magnetrons and related assemblies sold primarily into the semiconductor wafer fabrication market as well as microwave generators increased. Net sales of tubes also increased in the laser, aviation, and marine markets, offset by declines primarily in the industrial and broadcast markets. Gross margin as a percentage of sales increased to 31.3% during fiscal 2015 compared to 30.6% during fiscal 2014 primarily due to shifts in product and geographic mix.

### *Canvys*

Net sales for Canvys decreased 4.8% to \$23.5 million during fiscal 2016, from \$24.6 million during fiscal 2015. Sales in the North American OEM markets were down due to specific customers going through acquisitions within our customer base that disrupted the day to day business and delays in new programs. Gross margin as a percentage of net sales declined to 25.7% during fiscal 2016 as compared to 26.2% during fiscal 2015, primarily due to the devaluation of the Euro.

Net sales for Canvys decreased 11.5% to \$24.6 million during fiscal 2015, from \$27.9 million during fiscal 2014. Sales in the North America and European OEM markets were down due to delays in new programs which had a loss of several customers that concluded programs. Gross margin as a percentage of net sales declined to 26.2% during fiscal 2015 as compared to 27.2% during fiscal 2014, primarily due to the devaluation of the euro and increased engineering and freight costs.

**Healthcare**

Net Sales for Healthcare increased 98.2% to \$13.0 million during fiscal 2016, from \$6.6 million during fiscal 2015. The acquisition of IMES during fiscal 2016 resulted in \$7.6 million in sales, however sales in the Picture Archiving and Communication Systems (PACS) display market were down \$1.2 million driven by budget concerns and a difficult capital market for hospitals. Gross margin as a percentage of net sales increased to 44.0% during fiscal year 2016, compared to 24.1% during fiscal year 2015. This increase is primarily due to the significantly higher gross margins of the IMES business acquired during fiscal 2016.

Net Sales for Healthcare (previously part of our Canvys business) decreased 3.9% to \$6.6 million during fiscal 2015, from \$6.8 million during fiscal 2014. Sales were down in the Picture Archiving and Communication Systems (PACS) display market driven by budget concerns and a difficult capital market for hospitals. Gross margin as a percentage of net sales decreased to 24.1% during fiscal year 2015, compared to 26.6% during fiscal year 2014 due to competitive pricing pressure and shifts in product mix.

**Sales by Geographic Area**

On a geographic basis, our sales are categorized by destination: North America; Europe; Asia/Pacific; Latin America; and Other.

Net sales by geographic area and percent change for fiscal 2016, 2015, and 2014 were as follows (*in thousands*):

| Net Sales     | FY 2016   | FY 2015   | FY 2014   | <b>FY16 vs. FY15<br/>% Change</b> | <b>FY15 vs. FY14<br/>% Change</b> |        |    |
|---------------|-----------|-----------|-----------|-----------------------------------|-----------------------------------|--------|----|
| North America | \$66,365  | \$59,742  | \$57,137  | 11.1                              | %                                 | 4.6    | %  |
| Asia/Pacific  | 24,564    | 24,605    | 24,069    | (0.2                              | %)                                | 2.2    | %  |
| Europe        | 44,634    | 44,425    | 47,610    | 0.5                               | %                                 | (6.7   | %) |
| Latin America | 6,347     | 8,275     | 8,936     | (23.3                             | %)                                | (7.4   | %) |
| Other (1)     | 106       | (90 )     | 208       | (217.8                            | %)                                | (143.3 | %) |
| Total         | \$142,016 | \$136,957 | \$137,960 | 3.7                               | %                                 | (0.7   | %) |

Gross profit by geographic area and percent of geographic net sales for fiscal 2016, 2015, and 2014 were as follows (*in thousands*):

| Gross Profit (Loss) | FY 2016  |       | FY 2015  |       | FY 2014  |       |
|---------------------|----------|-------|----------|-------|----------|-------|
| North America       | \$23,506 | 35.4% | \$20,352 | 34.1% | \$18,905 | 33.1% |
| Asia/Pacific        | 8,212    | 33.4% | 7,967    | 32.4% | 7,849    | 32.6% |
| Europe              | 13,541   | 30.3% | 14,051   | 31.6% | 15,506   | 32.6% |
| Latin America       | 2,397    | 37.8% | 3,082    | 37.2% | 3,231    | 36.2% |
| Other (1)           | (2,821)  |       | (4,314)  |       | (4,477)  |       |
| Total               | \$44,835 | 31.6% | \$41,138 | 30.0% | \$41,014 | 29.7% |

(1) Other primarily includes net sales not allocated to a specific geographical region, unabsorbed value-add costs, and unallocated freight expenses.

We sell our products to customers in diversified industries and perform periodic credit evaluations of our customers' financial condition. Terms are generally on open account, payable net 30 days in North America, and vary throughout Asia/Pacific, Europe, and Latin America. Estimates of credit losses are recorded in the financial statements based on monthly reviews of outstanding accounts.

#### ***Selling, General, and Administrative Expenses***

Selling, general, and administrative expenses ("SG&A") increased during fiscal 2016 to \$51.6 million from \$49.2 million during fiscal 2015. SG&A as a percentage of sales from continuing operations, increased to 36.4% during fiscal 2016 from 35.9% during fiscal 2015. The increase in SG&A was due to \$5.0 million related to IMES and additional investments in our Richardson Healthcare business to support its growth and \$0.7 million in for PMT to support the power conversion growth initiatives, partially offset by decreases of \$1.9 million in IT services, \$0.9 million in our other support functions, and \$0.5 million in Canvys.

Selling, general, and administrative expenses (“SG&A”) increased during fiscal 2015 to \$49.2 million from \$43.5 million during fiscal 2014. SG&A as a percentage of sales from continuing operations, increased to 35.9% during fiscal 2015 from 31.5% during fiscal 2014. The increase in SG&A costs of \$5.7 million during fiscal 2015, compared to fiscal 2014, includes \$3.9 million of expenses related to our new IT system implementation and \$2.4 million related to our engineered solutions and healthcare growth initiatives, partially offset by other decreases in our administrative expenses of \$0.6 million.

### ***Impairment of Goodwill***

The Company reported \$6.3 million of goodwill on its balance sheet as of May 28, 2016. The results of our goodwill impairment tests as of February 28, 2016, indicated that the balance of goodwill reported, entirely attributed to the acquisition of IMES completed during the first quarter of fiscal 2016, was not impaired.

The Company did not have any goodwill on its balance sheet as of May 30, 2015, and May 31, 2014. The results of our goodwill impairment tests as of March 1, 2014, our measurement date, indicated that the balance of goodwill reported, entirely attributed to our PMT reporting unit, was fully impaired. The goodwill impairment test revealed that there was no implied goodwill value as of the measurement date. As a result, we recorded a pre-tax goodwill impairment charge of \$1.7 million during fiscal year 2014. Additionally, a \$0.4 million tax benefit was recorded related to the goodwill impairment.

### ***Other Income/Expense***

Other income/expense was income of \$0.3 million during fiscal 2016, compared to income of \$1.1 million during fiscal 2015. Fiscal 2016 includes \$0.6 million of investment income, partially offset by \$0.2 million of foreign exchange losses. Fiscal 2015 includes \$1.0 million of investment income. Other income of \$3.5 million during fiscal 2014 included an antitrust class action lawsuit settlement of \$2.5 million and \$1.0 million of investment income. Our foreign exchange gains and losses are primarily due to the translation of U.S. dollars held in non-U.S. entities. We currently do not utilize derivative instruments to manage our exposure to foreign currency.

### ***Income Tax Provision (Benefit)***

Our income tax provision from continuing operations during fiscal year 2016 was \$0.5 million. Our income tax benefit for fiscal year 2015 and fiscal year 2014 was \$1.5 million and \$0.3 million, respectively. The effective income

tax rates for continuing operations during fiscal 2016, 2015, and 2014, were 8.8%, (20.9)%, and (47.0)%, respectively. The difference between the effective tax rates as compared to the U.S. federal statutory rate of 34% during 2016, 2015, and 2014 is primarily driven by the impact of recording a valuation allowance against all of our U.S. state and federal net deferred tax assets, changes in our geographical distribution of income (loss), repatriation of foreign earnings, and our recording of uncertain tax positions with respect to ASC 740-30, Income Taxes - Other Considerations or Special Areas ("ASC 740-30").

As of May 28, 2016, we had approximately \$5.7 million of net deferred tax assets for federal net operating loss ("NOL") carryforwards, compared to \$3.0 million as of May 30, 2015. Net deferred tax assets for domestic state NOL carryforwards amounted to approximately \$2.7 million, compared to \$2.4 million during fiscal year 2015. Net deferred tax assets related to foreign NOL carryforwards totaled approximately \$0.6 million with various or indefinite expiration dates. The amount of net deferred tax assets related to foreign NOL carryforwards was the same as the fiscal year 2015. We also have a net deferred tax asset of \$0.3 million related to foreign tax credit carryforwards as of May 28, 2016 and May 30, 2015. The changes in balances from prior year for the federal NOL carryforwards is driven by current year forecast taxable losses. We do not have any alternative minimum tax credit carryforward as of May 28, 2016.

We have historically determined that certain undistributed earnings of our foreign subsidiaries, to the extent of cash available, will be repatriated to the U.S. Accordingly, we have provided a deferred tax liability totaling \$6.7 million and \$4.8 million as of May 28, 2016 and May 30, 2015, respectively, on foreign earnings of \$48.7 million and \$38.2 million, respectively. The increase year over year primarily relates to the change in management's assertion for RELL China. As of the fourth quarter of fiscal 2016, we changed our assertion to no longer be permanently reinvested in China. In addition, as of May 28, 2016, \$5.7 million of cumulative positive earnings of some of our foreign subsidiaries are still considered permanently reinvested pursuant to ASC 740-30, Income Taxes - Other Considerations or Special Areas ("ASC 740-30"). Due to various tax attributes that are continuously changing, it is not practicable to determine what, if any, tax liability might exist if such earnings were to be repatriated.

Management assesses the available positive and negative evidence to estimate if sufficient future taxable income will be generated to use the existing deferred tax assets. A significant component of objective evidence evaluated was the cumulative income or loss incurred in each jurisdiction over the three-year period ended May 28, 2016. Such objective evidence limits the ability to consider subjective evidence such as future income projections. We considered other positive evidence in determining the need for a valuation allowance in the U.S. including the repatriation of foreign earnings which we do not consider permanently reinvested in certain of our foreign subsidiaries. The weight of this positive evidence is not sufficient to outweigh other negative evidence in evaluating our need for a valuation allowance in the U.S. jurisdiction.

As of May 28, 2016, a valuation allowance of \$5.9 million has been established to record only the portion of the deferred tax asset that will more likely than not be realized. There has been an increase in the valuation allowance from May 30, 2015 in the amount of \$0.7 million. The valuation allowance on deferred tax assets in foreign jurisdictions relates to jurisdictions where historical taxable losses have been incurred. We also recorded a valuation allowance for all domestic federal and state net deferred tax assets considering the significant cumulative losses in the U.S. jurisdiction, the reversal of the deferred tax liability for foreign earnings, and no forecast of additional U.S. income. The amount of the deferred tax asset considered realizable, however, could be adjusted if estimates of future taxable income during the carryforward period are increased, or if objective negative evidence in the form of cumulative losses is no longer present and additional weight may be given to subjective evidence such as our projections for growth.

Income taxes paid, including foreign estimated tax payments, were \$0.7 million, \$0.5 million, and \$2.1 million, during fiscal 2016, 2015, and 2014, respectively.

In the normal course of business, we are subject to examination by taxing authorities throughout the world. Generally, years prior to fiscal 2006 are closed for examination under the statute of limitation for U.S. federal, U.S. state and local, or non-U.S. tax jurisdictions. We are under examination in the state of Illinois for fiscal years 2012 and 2013. We are currently under examination in Thailand for fiscal years 2008 through 2011 and France for fiscal years 2013 through 2015. Our primary foreign tax jurisdictions are Germany and the Netherlands. After the closure of the Germany tax audit for fiscal years 2009 through 2011, we have tax years open in Germany beginning in fiscal 2012 and the Netherlands beginning in fiscal 2010.

The uncertain tax positions from continuing operations as of May 28, 2016 and May 30, 2015, totaled \$0.1 million. We record penalties and interest relating to uncertain tax positions in the income tax expense line item within the unaudited consolidated statements of comprehensive income (loss). It is not expected that there will be a change in the unrecognized tax benefits within the next 12 months.

### *Discontinued Operations*



During fiscal year 2011, we completed the sale of the assets primarily used or held for use in, and certain liabilities of our RF, Wireless, and Power Division (“RFPD”), as well as certain other Company assets, including our information technology assets, to Arrow Electronics, Inc. (“Arrow”) in exchange for \$238.8 million (“the Transaction”). In accordance with Accounting Standards Codification (“ASC”) 205-20, Presentation of Financial Statements - Discontinued Operations (“ASC 205-20”), we reported the financial results of RFPD as a discontinued operation. Refer to Note 5 “Discontinued Operations” of the notes to our consolidated financial statements in Part II, Item 8 of this Annual Report on Form 10-K.

**Financial Summary - Discontinued Operations**

Summary financial results for fiscal 2016, 2015, and 2014 are presented in the following table (*in thousands*):

|  | Fiscal 2016 | Fiscal 2015 | Fiscal 2014 |
|--|-------------|-------------|-------------|
| Net sales  | \$ —        | \$ —        | \$ 402      |
| Gross loss <sup>(1)</sup>                                    | —           | —           | (330 )      |
| Selling, general, and administrative expenses <sup>(2)</sup> | —           | —           | 215         |
| Income tax provision (benefit) <sup>(3)</sup>                | —           | 31          | (375 )      |
| Loss from discontinued operations, net of tax                | —           | (31 )       | (170 )      |

*Notes:*

- (1) *Gross loss for fiscal year 2014 includes unabsorbed manufacturing labor and overhead expenses related to the Manufacturing Agreement with RFPD which ended March 1, 2014.*
- (2) *Selling, General and Administrative expenses in fiscal year 2014 related primarily to professional fees for tax audits resulting from the Transaction.*
- (3) *The income tax provision for fiscal year 2015 was the result of an income tax audit as a result of the Transaction. The income tax benefits in fiscal year 2014 relates to the reversal of tax reserves.*

**Liquidity, Financial Position, and Capital Resources**

Our growth and cash needs have been primarily financed through income from operations and cash on hand.

Cash and cash equivalents were \$60.4 million at May 28, 2016. Investments included CD's and time deposits, classified as short-term investments were \$2.3 million and long-term investments were \$7.8 million including equity securities of \$0.6 million. Cash and investments at May 28, 2016, consisted of \$18.1 million in North America, \$12.6 million in Europe, \$0.7 million in Latin America, and \$39.1 million in Asia/Pacific. We plan to repatriate \$11.3 million to the U.S. from China during our first quarter of fiscal 2017.

Cash and cash equivalents were \$74.5 million at May 30, 2015. Investments included CD's and time deposits, classified as short-term investments were \$23.7 million and long-term investments were \$11.5 million including equity securities of \$0.6 million. Cash and investments at May 30, 2015, consisted of \$51.1 million in North America, \$16.6 million in Europe, \$0.7 million in Latin America, and \$41.3 million in Asia/Pacific.

We believe we will continue to have sufficient liquidity to fund our future growth strategies for our business in the foreseeable future.

### *Cash Flows from Operating Activities*

Negative cash flow from operating activities primarily resulted from our net loss, adjusted for non-cash items, and changes in our operating assets and liabilities.

Operating activities used \$13.6 million of cash during fiscal 2016. We had net loss of \$6.8 million during fiscal 2016, which included non-cash stock-based compensation expense of \$0.5 million associated with the issuance of stock option awards and depreciation and amortization expense of \$2.4 million associated with our property and equipment as well as amortization of our intangible assets. Changes in our operating assets and liabilities, net of effects of acquired business, was a use of cash of \$9.7 million during fiscal 2016, due primarily to the increase in inventories of \$5.2 million, the increase in accounts receivable of \$3.5 million, the decrease in our accounts payable of \$0.9 million, the decrease in accrued liabilities of \$1.0 million, and the decrease in income tax receivable of \$0.9 million. The increase, or use of cash, for our inventory was primarily due to purchases related to our power conversion and Healthcare growth initiatives. The decrease in accounts payable is due to larger purchases of fixed assets and inventory primarily related to our Healthcare initiative where shorter payment terms are required. The decrease in accrual liabilities is due primarily to a \$0.7 million decrease in our severance accrual.

Operating activities, which include our discontinued operations, used \$9.8 million of cash during fiscal 2015. We had net loss of \$5.6 million during fiscal 2015, which included non-cash stock-based compensation expense of \$0.7 million associated with the issuance of stock option awards primarily to our directors and officers and depreciation and amortization expense of \$1.7 million associated with our property and equipment as well as amortization of our intangible assets. Changes in our operating assets and liabilities, net of effects of acquired businesses and foreign exchange, was a \$5.0 million use of cash during fiscal 2015. This use of cash is primarily due to increases in our accounts receivable of \$4.5 million and inventory purchases of \$7.5 million, partially offset by a decrease in our income tax receivable of \$2.0 million and an increase in our accounts payable of \$4.2 million. The increase in inventory and accounts payable relates to additional purchases to support our engineered solutions and Healthcare growth initiatives. The increase in accounts receivable relate to slower collections during our focus on the implementation of our global IT platform.

### ***Cash Flows from Investing Activities***

The cash flow from investing activities has consisted primarily of purchases and maturities of investments and capital expenditures.

Cash provided by investing activities of \$8.2 million during fiscal 2016, included proceeds from the maturities of investments of \$27.0 million and proceeds from the sale of our building in Spain of \$0.4 million, offset by the acquisition of IMES of \$12.2 million, purchases of investments of \$2.2 million, and \$4.8 million in capital expenditures. Capital expenditures relates primarily to our Healthcare growth initiatives and capital for our new IT system.

Cash used by investing activities during fiscal 2015 was \$6.9 million. This included proceeds from the maturities of investments of \$33.6 million, offset by the purchase of investments of \$35.6 million, and \$4.7 million in capital expenditures, primarily related to a new ERP system implementation.

Our purchases and proceeds from investments consist of time deposits and CDs. Purchasing of future investments may vary from period to period due to interest and foreign currency exchange rates.

### ***Cash Flows from Financing Activities***

The cash flow from financing activities primarily consists of repurchases of common stock and cash dividends paid.

Cash used in financing activities during fiscal 2016 was \$8.0 million. This included \$5.0 million of cash used to repurchase common stock and \$3.1 million in dividends paid, offset by \$0.1 million of proceeds from the issuance of common stock from stock option exercises. The repurchase of common stock relates to our share repurchase authorizations. Cash dividends paid of \$3.1 million were approved by the Board of Directors.

Cash used in financing activities during fiscal 2015 was \$6.9 million. This included \$3.9 million of cash used to repurchase common stock and \$3.3 million in dividends paid, offset by \$0.3 million of proceeds from the issuance of common stock from stock option exercises. The repurchase of common stock relates to our share repurchase authorizations. Cash dividends paid of \$3.3 million were approved by the Board of Directors.

All future payments of dividends are at the discretion of the Board of Directors. Dividend payments will depend on earnings, capital requirements, operating conditions, and such other factors that the Board may deem relevant.

### Contractual Obligations

Contractual obligations by expiration period are presented in the table below as of May 28, 2016 (*in thousands*):

|                                  | <b>Less than<br/>1 year</b> | <b>1 - 3<br/>years</b> | <b>4 - 5<br/>years</b> | <b>More than<br/>5 years</b> | <b>Total</b>   |
|----------------------------------|-----------------------------|------------------------|------------------------|------------------------------|----------------|
| Lease obligations <sup>(1)</sup> | <b>\$ 1,599</b>             | <b>\$3,737</b>         | <b>\$787</b>           | <b>\$ 185</b>                | <b>\$6,308</b> |

*(1) Lease obligations are related to certain warehouse and office facilities under non-cancelable operating leases.*

We believe that the existing sources of liquidity, including current cash, will provide sufficient resources to meet known capital requirements and working capital needs for the fiscal year ending May 27, 2017.

### **Critical Accounting Policies and Estimates**

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (“GAAP”) requires management to make significant estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Management continuously evaluates its critical accounting policies and estimates, including the allowance for doubtful accounts, revenue recognition, inventory obsolescence, goodwill and other intangible assets, loss contingencies, and income taxes. Management bases the estimates on historical experience and on various other assumptions believed to be reasonable under the circumstances, however, actual results could differ from those estimates.

The policies discussed below are considered by management to be critical to understanding our financial position and the results of operations. Their application involves significant judgments and estimates in preparation of our consolidated financial statements. For all of these policies, management cautions that future events rarely develop exactly as forecasted, and the best estimates routinely require adjustment.

#### ***Allowance for Doubtful Accounts***

Our allowance for doubtful accounts includes estimated losses that result from uncollectible receivables. The estimates are influenced by the following: continuing credit evaluation of customers’ financial conditions; aging of receivables, individually and in the aggregate; a large number of customers which are widely dispersed across geographic areas; collectability and delinquency history by geographic area; and the fact that no single customer accounts for more than 10% of net sales. Significant changes in one or more of these considerations may require adjustments affecting net income and net carrying value of accounts receivable. The allowance for doubtful accounts was approximately \$0.4 million as of May 28, 2016, and \$0.3 million as of May 30, 2015.

#### ***Revenue Recognition***

Our product sales are recognized as revenue upon shipment, when title passes to the customer, when delivery has occurred or services have been rendered, and when collectability is reasonably assured. We also record estimated

discounts and returns based on our historical experience. Our products are often manufactured to meet the specific design needs of our customers' applications. Our engineers work closely with customers to ensure that our products will meet their needs. Our customers are under no obligation to compensate us for designing the products we sell.

### ***Inventories***

Our worldwide inventories are stated at the lower of cost or market, generally using a weighted-average cost method. Our inventories included approximately \$40.0 million of finished goods, \$4.4 million of raw materials, and \$1.0 million of work-in-progress as of May 28, 2016, as compared to approximately \$33.7 million of finished goods, \$3.2 million of raw materials, and \$1.9 million of work-in-progress as of May 30, 2015.

Provisions for obsolete or slow moving inventories are recorded based upon regular analysis of stock rotation privileges, obsolescence, the exiting of certain market segments, and assumptions about future demand and market conditions. If future demand, changes in the industry, or market conditions differ from management's estimates, additional provisions may be necessary.

We recorded provisions to our inventory reserves of \$0.7 million, \$0.2 million, and \$0.8 million during fiscal 2016, 2015, and 2014, respectively, which were included in cost of sales. The provisions were primarily for obsolete and slow moving parts. The parts were written down to estimated realizable value.

### ***Goodwill and Other Intangible Assets***

We test goodwill for impairment annually and whenever events or circumstances indicate an impairment may have occurred, such as a significant adverse change in the business climate, loss of key personnel or a decision to sell or dispose of a reporting unit.

During the fourth quarter of each fiscal year, our goodwill balances are reviewed for impairment using the third quarter as the measurement date. If after reviewing the totality of events or circumstances as provided in ASU 2011-08 we determine that it is not likely that the fair value of a reporting unit exceeds its carrying amount, then we test for impairment through the application of a fair value based test. We estimate the fair value of each of our reporting units based on projected future operating results, market approach, and discounted cash flows. Projected future operating results and cash flows used for valuation purposes may reflect considerable improvements relative to historical periods with respect to, among other things, revenue growth and operating margins. Although we believe our projected future operating results and cash flows and related estimates regarding fair values are based on reasonable assumptions, historically, projected operating results and cash flows have not always been achieved.

In accordance with ASC 350 “*Intangibles - Goodwill and Other*”, if indicators of impairment are deemed to be present, we would perform an interim impairment test and any resulting impairment loss would be charged to expense in the period identified.

Our goodwill impairment testing follows the two-step process as defined in ASC 350. The first step in the process compares the fair value of the reporting unit to its carrying value. If the carrying value of the reporting unit exceeds its fair value, the second step of the impairment test is performed to measure the amount of impairment loss to be recognized. In the second step, the fair value of the reporting unit resulting from the first step of the evaluation is allocated to the fair value of all of the assets and liabilities of the reporting unit in order to determine an implied goodwill value. This allocation is similar to the purchase price allocation performed in purchase accounting. If the carrying amount of the goodwill reported exceeds the implied goodwill value, an impairment loss should be recognized in an amount equal to that excess.

Intangible assets are initially recorded at their fair market values determined on quoted market prices in active markets, if available, or recognized valuation models. Intangible assets that have finite useful lives are amortized on a straight-line basis over their useful lives. Our intangible assets represent the fair value for trade name, customer relationships, non-compete agreements, and technology acquired in connection with the acquisitions.

### ***Long-Lived Assets***

We review property and equipment, definite-lived intangible assets, and other long-lived assets for impairment whenever adverse events or changes in circumstances indicate that the carrying amounts of such assets may not be recoverable.

### ***Loss Contingencies***



We accrue a liability for loss contingencies when it is probable that a liability has been incurred and the amount can be reasonably estimated. When only a range of possible losses can be established, the most probable amount in the range is accrued. If no amount within this range is a better estimate than any other amount within the range, the minimum amount in the range is accrued. If we determine that there is at least a reasonable possibility that a loss may have been incurred, we will include a disclosure describing the contingency.

### *Income Taxes*

We recognize deferred tax assets and liabilities based on the differences between financial statement carrying amounts and the tax bases of assets and liabilities. We regularly review our deferred tax assets for recoverability and determine the need for a valuation allowance based on a number of factors, including both positive and negative evidence. These factors include historical taxable income or loss, projected future taxable income or loss, the expected timing of the reversals of existing temporary differences, and the implementation of tax planning strategies. In circumstances where we, or any of our affiliates, have incurred three years of cumulative losses which constitute significant negative evidence, positive evidence of equal or greater significance is needed to overcome the negative evidence before a tax benefit is recognized for deductible temporary differences and loss carryforwards. See Note 9 “Income Taxes” of the notes to our consolidated financial statements in Part II, Item 8 of this Annual Report on Form 10-K for further information.

### *New Accounting Pronouncements*

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606). ASU 2014-09 is principles based guidance that can be applied to all contracts with customers, enhancing comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets. The core principle of the guidance is that entities should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The guidance details the steps entities should apply to achieve the core principle. For public entities, ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period; early adoption is not permitted. We are currently evaluating the impact that the adoption of ASU 2014-09 will have on our financial condition, results of operations and disclosures.

In February 2016, the FASB issued ASU 2016-02, “Leases.” ASU 2016-02 establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Company is currently evaluating the potential impact of the adoption of ASU 2016-02 on the Company’s consolidated financial statements.

In July 2015, the FASB issued ASU 2015-11, “Simplifying the Measurement of Inventory.” ASU 2015-11 requires inventory within the scope of the ASU (e.g., first-in, first-out (“FIFO”) or average cost) to be measured using the lower of cost and net realizable value. Inventory excluded from the scope of the ASU (i.e., last-in, first-out (“LIFO”) or the retail inventory method) will continue to be measured at the lower of cost or market. The ASU also amends some of the other guidance in Topic 330, “Inventory,” to more clearly articulate the requirements for the measurement and disclosure of inventory. However, those amendments are not intended to result in any changes to current practice. ASU 2015-11 is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The adoption of this standard is not expected to have a significant impact on the Company’s consolidated financial statements.

In November 2015, the FASB issued ASU No. 2015-17, *Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes*, eliminating the current requirement for companies to present deferred tax assets and liabilities as current and noncurrent. Instead, companies will be required to classify all deferred tax assets and liabilities as noncurrent. This ASU is effective for annual periods beginning on or after December 15, 2016, including interim periods within those annual periods. The adoption of this guidance will result in a balance sheet reclassification and require related disclosure revisions in the Company’s consolidated financial statements.

In March 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-09, “Compensation—Stock Compensation: Improvements to Employee Share-Based Payment Accounting.” ASU 2016-09 introduces targeted amendments intended to simplify the accounting for stock compensation. Specifically, the ASU requires all excess tax benefits and tax deficiencies (including tax benefits of dividends on share-based payment awards) to be recognized as income tax expense or benefit in the income statement. The tax effects of exercised or vested awards should be treated as discrete items in the reporting period in which they occur. An entity also should recognize excess tax benefits, and assess the need for a valuation allowance, regardless of whether the benefit reduces

taxes payable in the current period. That is, off balance sheet accounting for net operating losses stemming from excess tax benefits would no longer be required and instead such net operating losses would be recognized when they arise. Existing net operating losses that are currently tracked off balance sheet would be recognized, net of a valuation allowance if required, through an adjustment to opening retained earnings in the period of adoption. Entities will no longer need to maintain and track an “APIC pool.” The ASU also requires excess tax benefits to be classified along with other income tax cash flows as an operating activity in the statement of cash flows.

In addition, ASU 2016-09 elevates the statutory tax withholding threshold to qualify for equity classification up to the maximum statutory tax rates in the applicable jurisdiction(s). The ASU also clarifies that cash paid by an employer when directly withholding shares for tax withholding purposes should be classified as a financing activity.

ASU 2016-09 provides an optional accounting policy election (with limited exceptions), to be applied on an entity-wide basis, to either estimate the number of awards that are expected to vest (consistent with existing U.S. GAAP) or account for forfeitures when they occur. ASU 2016-09 is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The Company is currently evaluating the potential impact of the adoption of this standard on the Company’s consolidated financial statements.

## **ITEM 7A. Quantitative and Qualitative Disclosures about Market Risk**

### **Risk Management and Market Sensitive Financial Instruments**

We are exposed to many different market risks with the various industries we serve. The primary financial risk we are exposed to is foreign currency exchange, as certain operations, assets, and liabilities of ours are denominated in foreign currencies. We manage these risks through normal operating and financing activities.

The interpretation and analysis of these disclosures should not be considered in isolation since such variances in exchange rates would likely influence other economic factors. Such factors, which are not readily quantifiable, would likely also affect our operations. Additional disclosure regarding various market risks are set forth in Part I, Item 1A, "Risk Factors" of our Annual Report on this Form 10-K.

### **Foreign Currency Exposure**

Even though we take into account current foreign currency exchange rates at the time an order is taken, our financial statements, denominated in a non-U.S. functional currency, are subject to foreign exchange rate fluctuations.

Our foreign denominated assets and liabilities are cash, accounts receivable, inventory, accounts payable and intercompany receivables and payables, as we conduct business in countries of the European Union, Asia/Pacific and, to a lesser extent, Canada and Latin America. We do manage foreign exchange exposures by using currency clauses in certain sales contracts and we also have local debt to offset asset exposures. We have not used any derivative instruments nor entered into any forward contracts in fiscal 2016, fiscal 2015, or fiscal 2014.

Had the U.S. dollar changed unfavorably 10% against various foreign currencies, foreign denominated net sales would have been lower by an estimated \$9.9 million during fiscal 2016, an estimated \$9.6 million during fiscal 2015, and an estimated \$13.8 million during fiscal 2014. Total assets would have declined by an estimated \$6.5 million as of the fiscal year ended May 28, 2016, and an estimated \$23.1 million as of the fiscal year ended May 30, 2015, while the total liabilities would have decreased by an estimated \$0.9 million as of the fiscal year ended May 28, 2016, and an estimated \$0.9 million as of the fiscal year ended May 30, 2015.

The interpretation and analysis of these disclosures should not be considered in isolation since such variances in exchange rates would likely influence other economic factors. Such factors, which are not readily quantifiable, would likely also affect our operations.

**ITEM 8. Financial Statements and Supplementary Data****Richardson Electronics, Ltd.****Audited Consolidated Balance Sheets***(in thousands, except per share amounts)*

|   | <b>May 28,<br/>2016</b> | <b>May 30,<br/>2015</b> |
|---|-------------------------|-------------------------|
| Assets  |                         |                         |
| Current assets:   |                         |                         |
| Cash and cash equivalents   | \$60,454                | \$74,535                |
| Accounts receivable, less allowance of \$364 and \$283  | 24,928                  | 20,753                  |
| Inventories, net  | 45,422                  | 38,769                  |
| Prepaid expenses and other assets   | 1,758                   | 1,696                   |
| Deferred income taxes   | 1,078                   | 804                     |
| Income tax receivable   | 17                      | 929                     |
| Investments - current   | 2,268                   | 23,692                  |
| Total current assets  | 135,925                 | 161,178                 |
| Non-current assets:   |                         |                         |
| Property, plant and equipment, net  | 12,986                  | 10,081                  |
| Goodwill  | 6,332                   | —                       |
| Intangible assets, net  | 3,818                   | 743                     |
| Non-current deferred income taxes   | 1,270                   | 1,443                   |
| Investments - non-current   | 7,799                   | 11,549                  |
| Total non-current assets  | 32,205                  | 23,816                  |
| Total assets  | \$168,130               | \$184,994               |
| Liabilities and Stockholders' Equity  |                         |                         |
| Current liabilities:  |                         |                         |
| Accounts payable  | \$14,896                | \$15,768                |
| Accrued liabilities   | 9,135                   | 10,144                  |
| Total current liabilities   | 24,031                  | 25,912                  |
| Non-current liabilities:  |                         |                         |
| Non-current deferred income tax liabilities   | 1,457                   | 1,209                   |
| Other non-current liabilities   | 967                     | 1,221                   |
| Total non-current liabilities   | 2,424                   | 2,430                   |
| Total liabilities   | 26,455                  | 28,342                  |
| Stockholders' equity  |                         |                         |
| Common stock, \$0.05 par value; issued and outstanding 10,703 shares at May 28, 2016, and 11,530 shares at May 30, 2015       | 535                     | 577                     |
| Class B common stock, convertible, \$0.05 par value; issued and outstanding 2,141 shares at May 28, 2016, and at May 30, 2015 | 107                     | 107                     |

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|   |           |           |
|---|-----------|-----------|
| Preferred stock, \$1.00 par value, no shares issued                               | —         | —         |
| Additional paid-in-capital  | 58,969    | 63,252    |
| Common stock in treasury, at cost, no shares at May 28, 2016, and at May 30, 2015 | —         | —         |
| Retained earnings   | 79,292    | 89,141    |
| Accumulated other comprehensive income  | 2,772     | 3,575     |
| Total stockholders' equity  | 141,675   | 156,652   |
| Total liabilities and stockholders' equity  | \$168,130 | \$184,994 |

**Richardson Electronics, Ltd.****Audited Consolidated Statements of Comprehensive Income (Loss)***(in thousands, except per share amounts)*

|  | Fiscal Year Ended |                 |                 |
|--|-------------------|-----------------|-----------------|
|  | May 28,<br>2016   | May 30,<br>2015 | May 31,<br>2014 |
| Statements of Comprehensive Income (Loss)            |                   |                 |                 |
| Net sales  | \$142,016         | \$136,957       | \$137,960       |
| Cost of sales  | 97,181            | 95,819          | 96,946          |
| Gross profit   | 44,835            | 41,138          | 41,014          |
| Selling, general, and administrative expenses        | 51,632            | 49,229          | 43,496          |
| Impairment of goodwill                               | —                 | —               | 1,671           |
| Gain on disposal of assets                           | (244 )            | (5 )            | —               |
| Operating loss                                       | (6,553 )          | (8,086 )        | (4,153 )        |
| Other (income) expense:                              |                   |                 |                 |
| Investment/interest income                           | (562 )            | (999 )          | (1,018 )        |
| Foreign exchange (gain) loss                         | 212               | (185 )          | 84              |
| Proceeds from legal settlement                       | —                 | —               | (2,547 )        |
| Other, net   | 17                | 92              | (20 )           |
| Total other income                                   | (333 )            | (1,092 )        | (3,501 )        |
| Loss from continuing operations before income taxes  | (6,220 )          | (6,994 )        | (652 )          |
| Income tax provision (benefit)                       | 546               | (1,466 )        | (307 )          |
| Loss from continuing operations                      | (6,766 )          | (5,528 )        | (345 )          |
| Loss from discontinued operations, net of tax        | —                 | (31 )           | (170 )          |
| Net loss   | (6,766 )          | (5,559 )        | (515 )          |
| Foreign currency translation gain (loss), net of tax | (759 )            | (6,504 )        | 1,216           |
| Fair value adjustments on investments gain (loss)    | (44 )             | 22              | 30              |
| Comprehensive income (loss)                          | \$(7,569 )        | \$(12,041 )     | \$731           |
| Loss per Common share - Basic:                       |                   |                 |                 |
| Loss from continuing operations                      | \$(0.53 )         | \$(0.41 )       | \$(0.03 )       |
| Loss from discontinued operations                    | —                 | —               | (0.01 )         |
| Total loss per Common share - Basic:                 | \$(0.53 )         | \$(0.41 )       | \$(0.04 )       |
| Loss per Class B common share - Basic:               |                   |                 |                 |
| Loss from continuing operations                      | \$(0.47 )         | \$(0.36 )       | \$(0.02 )       |
| Loss from discontinued operations                    | —                 | —               | (0.01 )         |
| Total loss per Class B common share - Basic:         | \$(0.47 )         | \$(0.36 )       | \$(0.03 )       |
| Loss per Common share - Diluted:                     |                   |                 |                 |
| Loss from continuing operations                      | \$(0.53 )         | \$(0.41 )       | \$(0.03 )       |
| Loss from discontinued operations                    | —                 | —               | (0.01 )         |
| Total loss per Common share - Diluted:               | \$(0.53 )         | \$(0.41 )       | \$(0.04 )       |
| Loss per Class B common share - Diluted:             |                   |                 |                 |
| Loss from continuing operations                      | \$(0.47 )         | \$(0.36 )       | \$(0.02 )       |



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|  |           |           |           |
|--|-----------|-----------|-----------|
| Loss from discontinued operations              | —         | —         | (0.01 )   |
| Total loss per Class B common share - Diluted: | \$(0.47 ) | \$(0.36 ) | \$(0.03 ) |
| Weighted average number of shares:             |           |           |           |
| Common shares - Basic                          | 10,908    | 11,682    | 11,915    |
| Class B common shares - Basic                  | 2,141     | 2,151     | 2,250     |
| Common shares - Diluted                        | 10,908    | 11,682    | 11,915    |
| Class B common shares - Diluted                | 2,141     | 2,151     | 2,250     |
| Dividends per common share                     | \$0.240   | \$0.240   | \$0.240   |
| Dividends per Class B common share             | \$0.220   | \$0.220   | \$0.220   |

**Richardson Electronics, Ltd.****Audited Consolidated Statements of Cash Flows***(in thousands)*

|   | Fiscal Year Ended |                 |                 |
|---|-------------------|-----------------|-----------------|
|   | May 28,<br>2016   | May 30,<br>2015 | May 31,<br>2014 |
| Operating activities:   |                   |                 |                 |
| Net loss  | \$(6,766 )        | \$(5,559 )      | \$(515 )        |
| Adjustments to reconcile net loss to cash provided by (used in) operating activities: |                   |                 |                 |
| Depreciation and amortization   | 2,381             | 1,707           | 1,094           |
| Loss (gain) on sale of investments  | 1                 | (27 )           | (27 )           |
| Gain on disposal of assets  | (244 )            | (5 )            | —               |
| Share-based compensation expense  | 548               | 726             | 759             |
| Deferred income taxes   | 201               | (1,604 )        | (1,005 )        |
| Impairment of goodwill  | —                 | —               | 1,671           |
| Change in assets and liabilities, net of effect of acquired business:                 |                   |                 |                 |
| Accounts receivable   | (3,521 )          | (4,495 )        | 195             |
| Income tax receivable   | 912               | 1,959           | 3,541           |
| Inventories   | (5,175 )          | (7,519 )        | 1,517           |
| Prepaid expenses and other assets   | (16 )             | (888 )          | 96              |
| Accounts payable  | (899 )            | 4,207           | (2,072 )        |
| Accrued liabilities   | (1,027 )          | 1,480           | (723 )          |
| Long-term liabilities-accrued pension   | (465 )            | —               | 133             |
| Other   | 486               | 238             | (51 )           |
| Net cash (used in) provided by operating activities                                   | (13,584)          | (9,780 )        | 4,613           |
| Investing activities:   |                   |                 |                 |
| Cash consideration paid for acquired business   | (12,209)          | —               | (973 )          |
| Capital expenditures  | (4,813 )          | (4,737 )        | (2,781 )        |
| Proceeds from sales of assets   | 402               | —               | —               |
| Proceeds from maturity of investments   | 27,026            | 33,617          | 342,279         |
| Purchases of investments  | (2,151 )          | (35,550 )       | (331,023)       |
| Proceeds from sales of available-for-sale securities                                  | 268               | 227             | 176             |
| Purchases of available-for-sale securities  | (268 )            | (227 )          | (176 )          |
| Other   | (20 )             | (248 )          | 98              |
| Net cash provided by (used in) investing activities                                   | 8,235             | (6,918 )        | 7,600           |
| Financing activities:   |                   |                 |                 |
| Repurchase of common stock  | (5,015 )          | (3,945 )        | (8,739 )        |
| Proceeds from issuance of common stock  | 142               | 324             | 190             |
| Cash dividends paid   | (3,079 )          | (3,260 )        | (3,341 )        |
| Other   | (4 )              | 3               | 37              |
| Net cash used in financing activities   | (7,956 )          | (6,878 )        | (11,853 )       |

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|  |          |          |           |
|--|----------|----------|-----------|
| Effect of exchange rate changes on cash and cash equivalents | (776 )   | (4,641 ) | 390       |
| Increase (decrease) in cash and cash equivalents             | (14,081) | (28,217) | 750       |
| Cash and cash equivalents at beginning of period             | 74,535   | 102,752  | 102,002   |
| Cash and cash equivalents at end of period                   | \$60,454 | \$74,535 | \$102,752 |
| Supplemental Disclosure of Cash Flow Information:            |          |          |           |
| Cash paid during the fiscal year for:                        |          |          |           |
| Interest   | —        | —        | —         |
| Income taxes   | 715      | 495      | 2,094     |

**Richardson Electronics, Ltd.****Audited Consolidated Statements of Stockholders' Equity***(in thousands)*

|  | Common | Class B<br>Common | Par<br>Value | Additional<br>Paid In<br>Capital | Common<br>Stock in<br>Treasury | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income | Total      |
|--|--------|-------------------|--------------|----------------------------------|--------------------------------|----------------------|---|------------|
| Balance June 1, 2013:                    | 12,263 | 2,491             | \$ 738       | \$ 73,979                        | \$(105 )                       | \$ 101,816           | \$ 8,811  | \$ 185,239 |
| Comprehensive income<br>(loss)           |        |                   |              |                                  |                                |                      |   |            |
| Net loss                                 | —      | —                 | —            | —                                | —                              | (515 )               | —   | (515 )     |
| Foreign currency translation             | —      | —                 | —            | —                                | —                              | —                    | 1,216   | 1,216      |
| Fair value adjustments on<br>investments | —      | —                 | —            | —                                | —                              | —                    | 30  | 30         |
| Share-based compensation:                |        |                   |              |                                  |                                |                      |   |            |
| Non-vested restricted stock              | —      | —                 | —            | 18                               | —                              | —                    | —   | 18         |
| Stock options                            | —      | —                 | —            | 741                              | —                              | —                    | —   | 741        |
| Common stock:                            |        |                   |              |                                  |                                |                      |   |            |
| Options exercised                        | 32     | —                 | 2            | 195                              | —                              | —                    | —   | 197        |
| Cancelled shares                         | —      | (300 )            | —            | —                                | —                              | —                    | —   | —          |
| Convert Class B to Common                | 300    | —                 | —            | —                                | —                              | —                    | —   | —          |
| Repurchase of common<br>stock            | —      | —                 | —            | —                                | (8,739 )                       | —                    | —   | (8,739 )   |
| Cancellation of treasury<br>stock        | (764 ) | —                 | (38 )        | (8,791 )                         | 8,829                          | —                    | —   | —          |
| Other                                    | 4      | —                 | —            | (1 )                             | 1                              | (1 )                 | —   | (1 )       |
| Dividends paid to:                       |        |                   |              |                                  |                                |                      |   |            |
| Common (\$0.24 per share)                | —      | —                 | —            | —                                | —                              | (2,853 )             | —   | (2,853 )   |
| Class B (\$0.22 per share)               | —      | —                 | —            | —                                | —                              | (488 )               | —   | (488 )     |
| Balance May 31, 2014:                    | 11,835 | 2,191             | \$ 702       | \$ 66,141                        | \$(14 )                        | \$ 97,959            | \$ 10,057                                       | \$ 174,845 |
| Comprehensive loss                       |        |                   |              |                                  |                                |                      |   |            |
| Net loss                                 | —      | —                 | —            | —                                | —                              | (5,559 )             | —   | (5,559 )   |
| Foreign currency translation             | —      | —                 | —            | —                                | —                              | —                    | (6,504 )  | (6,504 )   |
| Fair value adjustments on<br>investments | —      | —                 | —            | —                                | —                              | —                    | 22  | 22         |
| Share-based compensation:                |        |                   |              |                                  |                                |                      |   |            |
| Stock options                            | —      | —                 | —            | 726                              | —                              | —                    | —   | 726        |
| Common stock:                            |        |                   |              |                                  |                                |                      |   |            |
| Options exercised                        | 47     | —                 | 2            | 322                              | —                              | —                    | —   | 324        |
| Convert Class B to Common                | 50     | (50 )             | —            | —                                | —                              | —                    | —   | —          |
| Repurchase of common<br>stock            | —      | —                 | —            | —                                | (3,945 )                       | —                    | —   | (3,945 )   |

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|                                       |        |       |        |           |          |          |          |           |
|---------------------------------------|--------|-------|--------|-----------|----------|----------|----------|-----------|
| Cancellation of treasury stock        | (401 ) | —     | (20 )  | (3,939 )  | 3,959    | —        | —        | —         |
| Other                                 | (1 )   | —     | —      | 2         | —        | 1        | —        | 3         |
| Dividends paid to:                    |        |       |        |           |          |          |          |           |
| Common (\$0.24 per share)             | —      | —     | —      | —         | —        | (2,794 ) | —        | (2,794 )  |
| Class B (\$0.22 per share)            | —      | —     | —      | —         | —        | (466 )   | —        | (466 )    |
| Balance May 30, 2015:                 | 11,530 | 2,141 | \$ 684 | \$ 63,252 | \$—      | \$89,141 | \$ 3,575 | \$156,652 |
| Comprehensive loss                    |        |       |        |           |          |          |          |           |
| Net loss                              | —      | —     | —      | —         | —        | (6,766 ) | —        | (6,766 )  |
| Foreign currency translation          | —      | —     | —      | —         | —        | —        | (759 )   | (759 )    |
| Fair value adjustments on investments | —      | —     | —      | —         | —        | —        | (44 )    | (44 )     |
| Share-based compensation:             |        |       |        |           |          |          |          |           |
| Stock options                         | —      | —     | —      | 548       | —        | —        | —        | 548       |
| Common stock:                         |        |       |        |           |          |          |          |           |
| Options exercised                     | 28     | —     | 1      | 141       | —        | —        | —        | 142       |
| Repurchase of common stock            | —      | —     | —      | —         | (5,015 ) | —        | —        | (5,015 )  |
| Cancellation of treasury stock        | (855 ) | —     | (43 )  | (4,972 )  | 5,015    | —        | —        | —         |
| Other                                 | —      | —     | —      | —         | —        | (4 )     | —        | (4 )      |
| Dividends paid to:                    |        |       |        |           |          |          |          |           |
| Common (\$0.24 per share)             | —      | —     | —      | —         | —        | (2,615 ) | —        | (2,615 )  |
| Class B (\$0.22 per share)            | —      | —     | —      | —         | —        | (464 )   | —        | (464 )    |
| Balance May 28, 2016:                 | 10,703 | 2,141 | \$ 642 | \$ 58,969 | \$—      | \$79,292 | \$ 2,772 | \$141,675 |

## Notes to Consolidated Financial Statements

*(in thousands, except per share amounts)*

### 1. DESCRIPTION OF THE COMPANY

Richardson Electronics, Ltd. is a leading global provider of engineered solutions, power grid and microwave tubes and related consumables; power conversion and RF and microwave components; high value displays, flat panel detector solutions and replacement parts for diagnostic imaging equipment; and customized display solutions. We serve customers in the alternative energy, healthcare, aviation, broadcast, communications, industrial, marine, medical, military, scientific and semiconductor markets. The Company's strategy is to provide specialized technical expertise and "engineered solutions" based on our core engineering and manufacturing capabilities. The Company provides solutions and adds value through design-in support, systems integration, prototype design and manufacturing, testing, logistics, and aftermarket technical service and repair through its global infrastructure.

Our products include electron tubes and related components, microwave generators, subsystems used in semiconductor manufacturing, and visual technology solutions. These products are used to control, switch or amplify electrical power signals, or are used as display devices in a variety of industrial, commercial, medical, and communication applications.

During the first quarter of fiscal 2015, we created a new strategic business unit called Richardson Healthcare ("Healthcare"). Healthcare was previously included in our Canvys business unit. As hospitals remain under pressure to reduce costs while serving a much larger customer base, there is a growing demand for independent sources of high-value replacement parts for diagnostic imaging. Having access to parts that are tested and in stock enables hospitals to terminate expensive service contracts with the Original Equipment Manufacturers ("OEM") and instead use third party service providers or in-house technicians. With our global infrastructure, technical sales team, and experience servicing the healthcare market, we are well positioned to take advantage of this market opportunity. Over time, our plan is to expand our position from being the leader in power grid tubes to a key player in the high-growth, high-profile healthcare industry.

We have three operating and reportable segments, which we define as follows:

Electron Device Group ("EDG"), renamed Power and Microwave Technologies Group ("PMT") in July 2015, provides engineered solutions and distributes electronic components to customers in alternative energy, aviation, broadcast, communications, industrial, marine, medical, military, scientific, and semiconductor markets. PMT focuses on various applications including broadcast transmission, CO2 laser cutting, diagnostic imaging, dielectric and induction heating,

high energy transfer, high voltage switching, plasma, power conversion, radar, and radiation oncology. PMT also offers its customers technical services for both microwave and industrial equipment.

Canvys provides customized display solutions serving the corporate enterprise, financial, industrial, and OEM markets.

Healthcare manufactures, distributes and services high value replacement parts for the healthcare market including hospitals, medical centers, independent service organizations, and multi-vendor service providers. Products include power grid tubes, hydrogen thyratrons, klystrons, magnetrons; Image Systems medical displays and workstations for picture archiving and communication systems (“PACS”); visual solutions for operating rooms/surgical environments; digital radiography solutions including replacement flat panel detectors and upgrades; and additional replacement components currently under development for the diagnostic imaging service market. Through a combination of newly developed products and partnerships, service offerings, and training programs, we believe we can help our customers improve efficiency and deliver better clinical outcomes while lowering the cost of healthcare delivery.

We currently have operations in the following major geographic regions: North America, Asia/Pacific, Europe, and Latin America.

**Customer Concentration:** One customer represented \$3.8 million, or 15%, of our total accounts receivable balance, as of May 28, 2016. This receivable was collected in the first month of our fiscal year 2017. For the fiscal year ended May 30, 2015, the Company did not have any specific customer receivable balance that exceeded 10% of our total accounts receivable.

**Supplier Concentration:** One of our suppliers represented 11% of our total sales volume as of May 28, 2016, and 17% as of May 30, 2015. The amount owed to this supplier was approximately \$2.2 million as of May 28, 2016, and \$1.2 million as of May 30, 2015.

## 2. BASIS OF PRESENTATION

The accompanying consolidated financial statements have been prepared in accordance with U.S. GAAP for all fiscal years presented.

The consolidated financial statements include our wholly owned subsidiaries. All intercompany transactions and account balances have been eliminated in consolidation.

Our fiscal year 2016 began on May 31, 2015, and ended on May 28, 2016. Unless otherwise noted, all references to a particular year in this document shall mean our fiscal year.

## 3. SIGNIFICANT ACCOUNTING POLICIES AND DISCLOSURES

**Use of Estimates:** The preparation of financial statements in conformity with GAAP requires management to make significant estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Management continuously evaluates its critical accounting policies and estimates, including the allowance for doubtful accounts, revenue recognition, inventory obsolescence, goodwill and other intangible assets, loss contingencies, and income taxes. Management bases the estimates on historical experience and on various other assumptions believed to be reasonable under the circumstances, however, actual results could differ from those estimates.

**Fair Values of Financial Instruments:** The fair values of financial instruments are determined based on quoted market prices and market interest rates as of the end of the reporting period. Our financial instruments include investments, accounts receivable, accounts payable, and accrued liabilities. The fair values of these financial instruments approximate carrying values at May 28, 2016, and May 30, 2015.

**Cash and Cash Equivalents:** We consider short-term, highly liquid investments that are readily convertible to known amounts of cash, and so near their maturity that they present insignificant risk of changes in value because of changes in interest rates, and that have a maturity of three months or less, when purchased, to be cash equivalents. The carrying amounts reported in the balance sheet for cash and cash equivalents approximate the fair market value of these assets.



**Allowance for Doubtful Accounts:** Our allowance for doubtful accounts includes estimated losses that result from uncollectible receivables. The estimates are influenced by the following: continuing credit evaluation of customers' financial conditions; aging of receivables, individually and in the aggregate; a large number of customers which are widely dispersed across geographic areas; collectability and delinquency history by geographic area; and the fact that no single customer accounts for more than 10% of net sales. Significant changes in one or more of these considerations may require adjustments affecting net income and net carrying value of accounts receivable. The allowance for doubtful accounts was approximately \$0.4 million as of May 28, 2016, and \$0.3 million as of May 30, 2015.

**Loss Contingencies:** We accrue a liability for loss contingencies when it is probable that a liability has been incurred and the amount can be reasonably estimated. When only a range of possible loss can be established, the most probable amount in the range is accrued. If no amount within this range is a better estimate than any other amount within the range, the minimum amount in the range is accrued. If we determine that there is at least a reasonable possibility that a loss may have been incurred, we will include a disclosure describing the contingency.

**Revenue Recognition:** Our product sales are recognized as revenue upon shipment, when title passes to the customer, when delivery has occurred or services have been rendered, and when collectability is reasonably assured. We also record estimated discounts and returns based on our historical experience. Our products are often manufactured to meet the specific design needs of our customers' applications. Our engineers work closely with customers to ensure that our products will meet their needs. Our customers are under no obligation to compensate us for designing the products we sell.

**Foreign Currency Translation:** Balance sheet items for our foreign entities, included in our consolidated balance sheet are translated into U.S. dollars at end-of-period spot rates. Gains and losses resulting from translation of foreign subsidiary financial statements are credited or charged directly to accumulated other comprehensive income/(loss), a component of stockholders' equity. Revenues and expenses are translated at the current rate on the date of the transaction. Gains and losses resulting from foreign currency transactions are included in income. Foreign currency translation reflected in our consolidated statements of comprehensive income (loss) was a loss of \$0.2 million during fiscal 2016, a gain of \$0.2 million during fiscal 2015, and a loss of \$0.1 million during fiscal 2014.

**Shipping and Handling Fees and Costs:** Shipping and handling costs billed to customers are reported as revenue and the related costs are reported as a component of cost of sales.

**Inventories:** Our worldwide inventories are stated at the lower of cost or market, generally using a weighted-average cost method. Our inventories include approximately \$40.0 million of finished goods, \$4.4 million of raw materials, and \$1.0 million of work-in-progress as of May 28, 2016, as compared to approximately \$33.7 million of finished goods, \$3.2 million of raw materials, and \$1.9 million of work-in-progress as of May 30, 2015. The inventory reserve as of May 28, 2016, was \$3.4 million compared to \$3.0 million as of May 30, 2015.

Provisions for obsolete or slow moving inventories are recorded based upon regular analysis of stock rotation privileges, obsolescence, the exiting of certain markets, and assumptions about future demand and market conditions. If future demand, changes in the industry, or market conditions differ from management's estimates, additional provisions may be necessary.

We recorded provisions to our inventory reserves of \$0.7 million, \$0.2 million, and \$0.8 million during fiscal 2016, 2015, and 2014, respectively, which were included in cost of sales from continuing operations. The provisions were principally for obsolete and slow moving parts. The parts were written down to estimated realizable value.

**Income Taxes:** We recognize deferred tax assets and liabilities based on the differences between financial statement carrying amounts and the tax bases of assets and liabilities. We regularly review our deferred tax assets for recoverability and determine the need for a valuation allowance based on a number of factors, including both positive and negative evidence. These factors include historical taxable income or loss, projected future taxable income or loss, the expected timing of the reversals of existing temporary differences, and the implementation of tax planning strategies. In circumstances where we, or any of our affiliates, have incurred three years of cumulative losses which constitute significant negative evidence, positive evidence of equal or greater significance is needed to overcome the negative evidence before a tax benefit is recognized for deductible temporary differences and loss carryforwards.

**Investments:** As of May 28, 2016, we have invested in time deposits and certificates of deposit (“CD”) in the amount of \$9.5 million. Of this, \$2.3 million mature in less than twelve months and \$7.2 million mature in greater than twelve months. As of May 30, 2015, we had approximately \$34.7 million invested in time deposits and CD’s. Of this, \$23.7 million mature in less than twelve months and \$10.9 million mature in greater than twelve months. The fair value of these investments is the face value of each time deposit and CD.

We also have investments in equity securities, all of which are classified as available-for-sale and are carried at their fair value based on quoted market prices. Our investments, which are included in non-current assets, had a carrying amount of \$0.6 million at May 28, 2016, and \$0.6 million at May 30, 2015. Proceeds from the sale of securities were \$0.3 million during fiscal 2016 and \$0.2 million during fiscal years 2015 and 2014. We reinvested proceeds from the sale of securities, and the cost of the equity securities sold was based on a specific identification method. Gross realized gains and losses on those sales were less than \$0.1 million during fiscal years 2016, 2015, and 2014. Net unrealized holding losses during fiscal years 2016, 2015, and 2014, were less than \$0.1 million and have been included in accumulated comprehensive income (loss) during its respective fiscal year.

**Discontinued Operations:** During fiscal year 2011, we completed the sale of the assets primarily used or held for use in, and certain liabilities of, our RF, Wireless and Power Division (“RFPD”), as well as certain other Company assets, including our information technology assets, to Arrow Electronics, Inc. (“Arrow”) in exchange for \$238.8 million, (“the Transaction”). In accordance with Accounting Standards Codification (“ASC”) 205-20, *Presentation of Financial Statements - Discontinued Operations* (“ASC 205-20”), we reported the financial results of RFPD as a discontinued operation.

**Goodwill and Other Intangible Assets:** We test goodwill for impairment annually and whenever events or circumstances indicates an impairment may have occurred, such as a significant adverse change in the business climate, loss of key personnel or a decision to sell or dispose of a reporting unit.

During the fourth quarter of each fiscal year, our goodwill balances are reviewed for impairment using the third quarter as the measurement date. If after reviewing the totality of events or circumstances as provided in ASU 2011-08 we determine that it is not likely that the fair value of a reporting unit exceeds its carrying amount, then we test for impairment through the application of a fair value based test. We estimate the fair value of each of our reporting units based on projected future operating results, market approach, and discounted cash flows. Projected future operating results and cash flows used for valuation purposes may reflect considerable improvements relative to historical periods with respect to, among other things, revenue growth and operating margins. Although we believe our projected future operating results and cash flows and related estimates regarding fair values are based on reasonable assumptions, historically, projected operating results and cash flows have not always been achieved.

In accordance with ASC 350 “*Intangibles - Goodwill and Other*”, if indicators of impairment are deemed to be present, we would perform an interim impairment test and any resulting impairment loss would be charged to expense in the period identified.

For annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011, Accounting Standards Update (ASU) 2011-08, Testing for Goodwill for Impairment (“ASU 2011-08”) permits an entity to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, an entity determines it is not likely that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary.

Intangible assets are initially recorded at their fair market values determined on quoted market prices in active markets, if available, or recognized valuation models. Intangible assets that have finite useful lives are amortized over their useful lives and are tested when events or changes in circumstances occur that indicate possible impairment.

**Property, Plant and Equipment:** Property, plant and equipment are stated at cost, net of accumulated depreciation. Improvements and replacements are capitalized while expenditures for maintenance and repairs are charged to expense as incurred. Provisions for depreciation are computed using the straight-line method over the estimated useful life of the asset. Depreciation expense was approximately \$2.0 million, \$1.7 million, and \$1.0 million during fiscal years 2016, 2015, and 2014, respectively. Property, plant and equipment consist of the following (*in thousands*):

|                                       | May 28,<br>2016 | May 30,<br>2015 |
|---------------------------------------|-----------------|-----------------|
| Land and improvements                 | \$1,301         | \$1,594         |
| Buildings and improvements            | 19,023          | 18,883          |
| Computer and communications equipment | 6,810           | 6,774           |
| Construction in progress              | 2,721           | 1,218           |
| Machinery and other equipment         | 8,080           | 6,562           |
|                                       | \$37,935        | \$35,031        |
| Accumulated depreciation              | (24,949)        | (24,950)        |
| Property, plant, and equipment, net   | \$12,986        | \$10,081        |

Construction in progress includes \$1.6 million related to our Healthcare growth initiatives, \$0.9 million for our new IT system, and \$0.2 million of other projects. All projects are expected to be completed before the end of fiscal 2017.

Supplemental disclosure information of the estimated useful life of the assets:

|                                       |               |
|---------------------------------------|---------------|
| Land improvements                     | 10 years      |
| Buildings and improvements            | 10 - 30 years |
| Computer and communications equipment | 3 - 10 years  |
| Machinery and other equipment         | 3 - 10 years  |

We review all property, plant, and equipment for impairment when events or changes in circumstances occur which indicate a possible impairment may exist. We have concluded that our property, plant, and equipment as of May 28, 2016, were not impaired.

**Accrued Liabilities:** Accrued liabilities consist of the following (*in thousands*):

|                                | May<br>28,<br>2016 | May<br>30, 2015 |
|--------------------------------|--------------------|-----------------|
| Compensation and payroll taxes | \$4,054            | \$4,303         |
| Income taxes                   | 0                  | 572             |
| Professional fees              | 775                | 885             |
| Deferred revenue               | 1,879              | 1,680           |
| Other accrued expenses         | 2,427              | 2,704           |
| Accrued Liabilities            | \$9,135            | \$10,144        |

**Warranties:** We offer warranties for the limited number of specific products we manufacture. We also provide extended warranties for some products we sell that lengthen the period of coverage specified in the manufacturer's original warranty. Our warranty terms generally range from one to three years.

We estimate the cost to perform under the warranty obligation and recognize this estimated cost at the time of the related product sale. We record expense related to our warranty obligations as cost of sales in our consolidated statements of comprehensive income (loss). Each quarter, we assess actual warranty costs incurred on a product-by-product basis and compare the warranty costs to our estimated warranty obligation. With respect to new products, estimates are based generally on knowledge of the products, the extended warranty period, and warranty experience.

Warranty reserves are established for costs that are expected to be incurred after the sale and delivery of products under warranty. Warranty reserves are included in accrued liabilities on our consolidated balance sheets. The warranty reserves are determined based on known product failures, historical experience, and other available evidence.

Changes in the warranty reserve during fiscal 2016 and 2015 were as follows (*in thousands*):

|                            | Warranty<br>Reserve |
|----------------------------|---------------------|
| Balance at May 31, 2014    | \$ 175              |
| Accruals for products sold | 116                 |
| Utilization                | (103 )              |
| Balance at May 30, 2015    | \$ 188              |
| Accruals for products sold | 108                 |
| Utilization                | (86 )               |
| Balance at May 28, 2016    | \$ 210              |

**Other Non-Current Liabilities:** Other non-current liabilities of \$1.0 million at May 28, 2016, and \$1.2 million at May 30, 2015, primarily represent employee-benefits obligations in various non-US locations.

**Share-Based Compensation:** We measure and recognize compensation cost at fair value for all share-based payments, including stock options. We estimate fair value using the Black-Scholes option-pricing model, which requires assumptions such as expected volatility, risk-free interest rate, expected life, and dividends. Compensation cost is recognized using a graded-vesting schedule over the applicable vesting period. Share-based compensation expense totaled approximately \$0.5 million during fiscal 2016, \$0.7 million during fiscal 2015, and \$0.8 million during fiscal 2014.

Stock options granted generally vest over a period of five years and have contractual terms to exercise of 10 years. A summary of stock option activity is as follows (*in thousands, except option prices and years*):

|  | Number of<br>Options | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Life | Aggregate<br>Intrinsic<br>Value |
|--|----------------------|--|---|---------------------------------|
| <b>Options Outstanding at June 1, 2013</b> | 944                  | \$ 10.13                                 |   |                                 |
| Granted                                    | 224                  | 11.15                                    |   |                                 |
| Exercised                                  | (32 )                | 5.84                                     |   |                                 |
| Forfeited                                  | (54 )                | 11.73                                    |   |                                 |
| Cancelled                                  | (17 )                | 11.52                                    |   |                                 |
| <b>Options Outstanding at May 31, 2014</b> | 1,065                | \$ 10.37                                 |   |                                 |
| Granted                                    | 225                  | 9.92                                     |   |                                 |
| Exercised                                  | (47 )                | 6.53                                     |   |                                 |
| Forfeited                                  | (34 )                | 11.42                                    |   |                                 |
| Cancelled                                  | (72 )                | 11.19                                    |   |                                 |
| <b>Options Outstanding at May 30, 2015</b> | 1,137                | \$ 10.35                                 |   |                                 |
| Granted                                    | 122                  | 5.88                                     |   |                                 |
| Exercised                                  | (28 )                | 5.18                                     |   |                                 |
| Forfeited                                  | (105 )               | 10.98                                    |   |                                 |
| Cancelled                                  | (107 )               | 9.97                                     |   |                                 |
| <b>Options Outstanding at May 28, 2016</b> | 1,019                | \$ 9.93                                  | 6.0   | \$4                             |
| <b>Options Vested at May 28, 2016</b>      | 602                  | \$ 10.34                                 | 4.6   | \$4                             |

There were 28,000 stock options exercised during fiscal 2016, with cash received of \$0.1 million. The total intrinsic value of options exercised totaled less than \$0.1 million during fiscal 2016 and \$0.2 million during fiscal 2015 and fiscal 2014. The weighted average fair value of stock option grants was \$1.21 during fiscal 2016, \$3.71 during fiscal 2015, and \$4.53 during fiscal 2014. As of May 28, 2016, total unrecognized compensation costs related to unvested stock options was approximately \$1.2 million which is expected to be recognized over the remaining weighted average period of approximately three to four years. The total grant date fair value of stock options vested during fiscal 2016 was \$0.6 million.

The fair value of stock options is estimated using the Black-Scholes option-pricing model with the following weighted average assumptions:

| Fiscal Year Ended |                 |                 |
|-------------------|-----------------|-----------------|
| May 28,<br>2016   | May 30,<br>2015 | May 31,<br>2014 |



|                         |         |         |         |
|-------------------------|---------|---------|---------|
| Expected volatility     | 32.21 % | 46.12 % | 49.31 % |
| Risk-free interest rate | 1.78 %  | 2.12 %  | 2.03 %  |
| Expected lives (years)  | 6.50    | 6.47    | 6.47    |
| Annual cash dividend    | \$0.24  | \$0.24  | \$0.24  |

The expected volatility assumptions are based on historical experience commensurate with the expected term. The risk-free interest rate is based on the yield of a treasury note with a remaining term equal to the expected life of the stock option.

The expected stock option life assumption is based on the Securities and Exchange Commission's ("SEC") guidance in Staff Accounting Bulletin ("SAB") No. 107 ("SAB No. 107"). On December 21, 2007, the SEC issued SAB No. 110 stating that they will continue to accept SAB No. 107, past the original expiration date of December 31, 2007. For stock options granted during fiscal years 2016, 2015, and 2014, we believe that our historical stock option experience does not provide a reasonable basis upon which to estimate expected term. We utilized the Safe Harbor option, or Simplified Method, to determine the expected term of these options in accordance with SAB No. 107 for options granted. We intend to continue to utilize the Simplified Method for future grants in accordance with SAB No. 110 until such time that we believe that our historical stock option experience will provide a reasonable basis to estimate an expected term.

The following table summarizes information about stock options outstanding at May 28, 2016 (*in thousands, except option prices and years*):

| Exercise Price Range | Outstanding  |                                 |                       |                           | Vested     |                                 |                       |                           |
|----------------------|--------------|---------------------------------|-----------------------|---------------------------|------------|---------------------------------|-----------------------|---------------------------|
|                      | Shares       | Weighted Average Exercise Price | Weighted Average Life | Aggregate Intrinsic Value | Shares     | Weighted Average Exercise Price | Weighted Average Life | Aggregate Intrinsic Value |
| \$5.03 to \$8.58     | 285          | \$ 6.01                         | 5.4                   | \$ 4                      | 169        | \$ 6.10                         | 2.6                   | \$ 4                      |
| \$9.48 to \$11.14    | 382          | \$ 10.49                        | 7.6                   | \$ —                      | 133        | \$ 10.65                        | 6.9                   | \$ —                      |
| \$11.50 to \$13.76   | 352          | \$ 12.51                        | 4.9                   | \$ —                      | 300        | \$ 12.59                        | 4.6                   | \$ —                      |
| <b>Total</b>         | <b>1,019</b> | <b>\$ 9.93</b>                  | <b>6.0</b>            | <b>\$ 4</b>               | <b>602</b> | <b>\$ 10.34</b>                 | <b>4.6</b>            | <b>\$ 4</b>               |

As of May 28, 2016, we did not have any unvested restricted shares.

Compensation effects arising from issuing stock awards have been charged against income and recorded as additional paid-in-capital in the consolidated statements of stockholder's equity during fiscal 2016, 2015, and 2014.

The Employees' 2011 Long-Term Incentive Compensation Plan authorizes the issuance of up to 1,500,000 shares as incentive stock options, non-qualified stock options, or stock awards. Under this plan, 950,000 shares are reserved for future issuance. The Plan authorizes the granting of stock options at the fair market value at the date of grant. Generally, these options become exercisable over five years and expire up to 10 years from the date of grant.

**Earnings per Share:** We have authorized 17,000,000 shares of common stock, and 3,000,000 shares of Class B common stock. The Class B common stock has 10 votes per share and has transferability restrictions; however, Class B common stock may be converted into common stock on a share-for-share basis at any time. With respect to dividends and distributions, shares of common stock and Class B common stock rank equally and have the same rights, except that Class B common stock cash dividends are limited to 90% of the amount of Class A common stock cash dividends.

In accordance with ASC 260-10, *Earnings Per Share* ("ASC 260"), our Class B common stock is considered a participating security requiring the use of the two-class method for the computation of basic and diluted earnings per share. The two-class computation method for each period reflects the cash dividends paid per share for each class of stock, plus the amount of allocated undistributed earnings per share computed using the participation percentage which reflects the dividend rights of each class of stock. Basic and diluted earnings per share were computed using the two-class method as prescribed in ASC 260. The shares of Class B common stock are considered to be participating

convertible securities since the shares of Class B common stock are convertible on a share-for-share basis into shares of common stock and may participate in dividends with common stock according to a predetermined formula which is 90% of the amount of Class A common stock cash dividends.

The per share amounts presented in the consolidated statements of comprehensive income (loss) are based on the following (*amounts in thousands, except per share amounts*):

|  | For the Fiscal Year Ended |            |              |            |              |            |
|--|---------------------------|------------|--------------|------------|--------------|------------|
|  | May 28, 2016              |            | May 30, 2015 |            | May 31, 2014 |            |
|  | Basic                     | Diluted    | Basic        | Diluted    | Basic        | Diluted    |
| Numerator for Basic and Diluted EPS:   |                           |            |              |            |              |            |
| Loss from continuing operations  | \$(6,766 )                | \$(6,766 ) | \$(5,528 )   | \$(5,528 ) | \$(345 )     | \$(345 )   |
| Less dividends:  |                           |            |              |            |              |            |
| Common stock   | 2,615                     | 2,615      | 2,794        | 2,794      | 2,853        | 2,853      |
| Class B common stock   | 464                       | 464        | 466          | 466        | 488          | 488        |
| Undistributed losses   | \$(9,845 )                | \$(9,845 ) | \$(8,788 )   | \$(8,788 ) | \$(3,686 )   | \$(3,686 ) |
| Common stock undistributed losses  | \$(8,367 )                | \$(8,367 ) | \$(7,539 )   | \$(7,539 ) | \$(3,151 )   | \$(3,151 ) |
| Class B common stock undistributed losses  | (1,478 )                  | (1,478 )   | (1,249 )     | (1,249 )   | (535 )       | (535 )     |
| Total undistributed losses   | \$(9,845 )                | \$(9,845 ) | \$(8,788 )   | \$(8,788 ) | \$(3,686 )   | \$(3,686 ) |
| Loss from discontinued operations  | \$—                       | \$—        | \$(31 )      | \$(31 )    | \$(170 )     | \$(170 )   |
| Less dividends:  |                           |            |              |            |              |            |
| Common stock   | 2,615                     | 2,615      | 2,794        | 2,794      | 2,853        | 2,853      |
| Class B common stock   | 464                       | 464        | 466          | 466        | 488          | 488        |
| Undistributed losses   | \$(3,079 )                | \$(3,079 ) | \$(3,291 )   | \$(3,291 ) | \$(3,511 )   | \$(3,511 ) |
| Common stock undistributed losses  | \$(2,615 )                | \$(2,615 ) | \$(2,823 )   | \$(2,823 ) | \$(3,001 )   | \$(3,001 ) |
| Class B common stock undistributed losses  | (464 )                    | (464 )     | (468 )       | (468 )     | (510 )       | (510 )     |
| Total undistributed losses   | \$(3,079 )                | \$(3,079 ) | \$(3,291 )   | \$(3,291 ) | \$(3,511 )   | \$(3,511 ) |
| Net loss   | \$(6,766 )                | \$(6,766 ) | \$(5,559 )   | \$(5,559 ) | \$(515 )     | \$(515 )   |
| Less dividends:  |                           |            |              |            |              |            |
| Common stock   | 2,615                     | 2,615      | 2,794        | 2,794      | 2,853        | 2,853      |
| Class B common stock   | 464                       | 464        | 466          | 466        | 488          | 488        |
| Undistributed losses   | \$(9,845 )                | \$(9,845 ) | \$(8,819 )   | \$(8,819 ) | \$(3,856 )   | \$(3,856 ) |
| Common stock undistributed losses  | \$(8,367 )                | \$(8,367 ) | \$(7,565 )   | \$(7,565 ) | \$(3,296 )   | \$(3,296 ) |
| Class B common stock undistributed losses  | (1,478 )                  | (1,478 )   | (1,254 )     | (1,254 )   | (560 )       | (560 )     |
| Total undistributed losses   | \$(9,845 )                | \$(9,845 ) | \$(8,819 )   | \$(8,819 ) | \$(3,856 )   | \$(3,856 ) |
| Denominator for Basic and Diluted EPS:   |                           |            |              |            |              |            |
| Common stock weighted average shares   | 10,908                    | 10,908     | 11,682       | 11,682     | 11,915       | 11,915     |
| Class B common stock weighted average shares, and shares under if-converted method for diluted EPS | 2,141                     | 2,141      | 2,151        | 2,151      | 2,250        | 2,250      |
| Effect of dilutive stock options   |                           | —          |              | —          |              | —          |
| Denominator for diluted EPS adjusted for weighted average shares and assumed conversions           |                           | 13,049     |              | 13,833     |              | 14,165     |
| Loss from continuing operations per share:   |                           |            |              |            |              |            |
| Common stock   | \$(0.53 )                 | \$(0.53 )  | \$(0.41 )    | \$(0.41 )  | \$(0.03 )    | \$(0.03 )  |
| Class B common stock   | \$(0.47 )                 | \$(0.47 )  | \$(0.36 )    | \$(0.36 )  | \$(0.02 )    | \$(0.02 )  |
| Income from discontinued operations per share:   |                           |            |              |            |              |            |
| Common stock   | \$—                       | \$—        | \$—          | \$—        | \$(0.01 )    | \$(0.01 )  |
| Class B common stock   | \$—                       | \$—        | \$—          | \$—        | \$(0.01 )    | \$(0.01 )  |
| Net loss per share:  |                           |            |              |            |              |            |

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|                      |            |            |            |            |            |            |
|----------------------|------------|------------|------------|------------|------------|------------|
| Common stock         | \$ (0.53 ) | \$ (0.53 ) | \$ (0.41 ) | \$ (0.41 ) | \$ (0.04 ) | \$ (0.04 ) |
| Class B common stock | \$ (0.47 ) | \$ (0.47 ) | \$ (0.36 ) | \$ (0.36 ) | \$ (0.03 ) | \$ (0.03 ) |

*Note: Common stock options that were anti-dilutive and not included in diluted earnings per common share for fiscal 2016, fiscal 2015, and fiscal 2014 were 890; 881; and 489 respectively.*

### *New Accounting Pronouncements*

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606). ASU 2014-09 is principles based guidance that can be applied to all contracts with customers, enhancing comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets. The core principle of the guidance is that entities should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The guidance details the steps entities should apply to achieve the core principle. For public entities, ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period; early adoption is not permitted. We are currently evaluating the impact that the adoption of ASU 2014-09 will have on our financial condition, results of operations and disclosures.

In February 2016, the FASB issued ASU 2016-02, “Leases.” ASU 2016-02 establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Company is currently evaluating the potential impact of the adoption of ASU 2016-02 on the Company’s consolidated financial statements.

In July 2015, the FASB issued ASU 2015-11, “Simplifying the Measurement of Inventory.” ASU 2015-11 requires inventory within the scope of the ASU (e.g., first-in, first-out (“FIFO”) or average cost) to be measured using the lower of cost and net realizable value. Inventory excluded from the scope of the ASU (i.e., last-in, first-out (“LIFO”) or the retail inventory method) will continue to be measured at the lower of cost or market. The ASU also amends some of the other guidance in Topic 330, “Inventory,” to more clearly articulate the requirements for the measurement and disclosure of inventory. However, those amendments are not intended to result in any changes to current practice. ASU 2015-11 is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The adoption of this standard is not expected to have a significant impact on the Company’s consolidated financial statements.

In November 2015, the FASB issued ASU No. 2015-17, *Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes*, eliminating the current requirement for companies to present deferred tax assets and liabilities as current and noncurrent. Instead, companies will be required to classify all deferred tax assets and liabilities as noncurrent. This ASU is effective for annual periods beginning on or after December 15, 2016, including interim periods within those annual periods. The adoption of this guidance will result in a balance sheet reclassification and require related disclosure revisions in the Company’s consolidated financial statements.

In March 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-09, “Compensation—Stock Compensation: Improvements to Employee Share-Based Payment Accounting.” ASU 2016-09 introduces targeted amendments intended to simplify the accounting for stock compensation. Specifically, the ASU requires all excess tax benefits and tax deficiencies (including tax benefits of dividends on share-based payment awards) to be recognized as income tax expense or benefit in the income statement. The tax effects of exercised or vested awards should be treated as discrete items in the reporting period in which they occur. An entity also should recognize excess tax benefits, and assess the need for a valuation allowance, regardless of whether the benefit reduces

taxes payable in the current period. That is, off balance sheet accounting for net operating losses stemming from excess tax benefits would no longer be required and instead such net operating losses would be recognized when they arise. Existing net operating losses that are currently tracked off balance sheet would be recognized, net of a valuation allowance if required, through an adjustment to opening retained earnings in the period of adoption. Entities will no longer need to maintain and track an “APIC pool.” The ASU also requires excess tax benefits to be classified along with other income tax cash flows as an operating activity in the statement of cash flows.

In addition, ASU 2016-09 elevates the statutory tax withholding threshold to qualify for equity classification up to the maximum statutory tax rates in the applicable jurisdiction(s). The ASU also clarifies that cash paid by an employer when directly withholding shares for tax withholding purposes should be classified as a financing activity.

ASU 2016-09 provides an optional accounting policy election (with limited exceptions), to be applied on an entity-wide basis, to either estimate the number of awards that are expected to vest (consistent with existing U.S. GAAP) or account for forfeitures when they occur. ASU 2016-09 is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The Company is currently evaluating the potential impact of the adoption of this standard on the Company’s consolidated financial statements.

#### 4. ACQUISITION

On June 15, 2015, Richardson Electronics, Ltd (“the Company”), acquired certain assets of International Medical Equipment and Services, Inc. (“IMES”), for a purchase price of \$12.2 million. This includes the purchase of inventory, receivables, fixed assets, and certain other assets of the Company. The Company did not acquire any liabilities of IMES. The total consideration paid excludes transaction costs.

IMES, based in South Carolina, provides reliable, cost-saving solutions worldwide for major brands of CT and MRI equipment. This acquisition positions Richardson Healthcare to provide cost effective diagnostic imaging replacement parts and training to hospitals, diagnostic imaging centers, medical institutions, and independent service organizations. IMES offers an extensive selection of replacement parts, as well as an interactive training center, on-site test bays and experienced technicians who provide 24/7 customer support. Replacement parts are readily available and triple tested to provide peace of mind when uptime is critical. IMES core operations will remain in South Carolina. Richardson Healthcare plans to expand IMES’ replacement parts and training offerings geographically to leverage the Company’s global infrastructure. During the fourth quarter of fiscal 2016, IMES opened up their first foreign location in Amsterdam.

The consideration paid by the Company to IMES at closing was \$12.2 million in cash. The following table summarizes the fair values of the assets acquired at the date of the closing of the acquisition (*in thousands*):

|                               |          |
|-------------------------------|----------|
| Accounts receivable           | \$737    |
| Inventories                   | 1,420    |
| Property, plant and equipment | 230      |
| Goodwill                      | 6,332    |
| Other intangibles             | 3,490    |
| Net assets acquired           | \$12,209 |

Intangible assets include trade names with an estimated life of 3 years for \$0.6 million, customer relationships with an estimated life of 20 years for \$2.5 million, non-compete agreements with an estimated life of 5 years for \$0.2 million, and technology with an estimated life of 10 years for \$0.2 million.

Goodwill recognized represents value the Company expects to be created by combining the operations of IMES with the Company’s operations, including the expansion into markets within existing business segments and geographic regions, access to new customers and potential cost savings and synergies.



Goodwill related to the acquisition is deductible for tax purposes.

In connection with the acquisition of IMES, the Company also entered into an Employment, Non-Disclosure, and Non-Compete Agreement (“Employment Agreement”) with Lee A. McIntyre III as the Company’s Executive Vice President, IMES. During the term of his employment, Mr. McIntyre will earn an annual base salary of \$300,000. In addition to his base salary, he will be entitled to an annual bonus equal to 20% of the EBITDA of IMES provided that the EBITDA of the business is at least \$2.0 million inclusive of the bonus payment. The annual bonus payment will terminate after five years. For fiscal year 2016, Lee McIntyre did not receive a bonus as the minimum EBITDA needed was not achieved.

The following unaudited pro forma information represents the Company's results of operations as if the acquisitions had occurred as of June 1, 2014:

| \$ in thousands, except per share amounts | <b>For the<br/>year<br/>ended<br/>May 30,<br/>2015</b> |
|---|--|
| Net sales                                 | \$ 145,136   |
| Net loss                                  | \$(3,666 )   |
| Earnings per share:                       |  |
| Common shares - Basic                     | \$(0.27 )  |
| Class B common shares - Basic             | \$(0.24 )  |
| Common shares - Diluted                   | \$(0.27 )  |
| Class B common shares - Diluted           | \$(0.24 )  |

The pro forma results have been prepared for informational purposes only and include adjustments to amortize acquired intangible assets with finite life and reflect foregone interest income on cash paid for the acquisitions. These pro forma results do not purport to be indicative of the results of operations that would have occurred had the purchases been made as of the beginning of the periods presented or of the results of operations that may occur in the future. The financial results for the fiscal year ended May 28, 2016, includes the financial results for IMES from June 15, 2015, through May 28, 2016. The financial transactions for IMES from May 31, 2015, through June 14, 2015, were deemed immaterial for illustrating pro forma financial statements. IMES net sales for fiscal 2016 were \$7.6 million. The gross profit was \$4.4 million, or 57.9% of net sales during fiscal 2016.

## 5. DISCONTINUED OPERATIONS

### Financial Summary - Discontinued Operations

Summary financial results for fiscal 2016, 2015, and 2014 are presented in the following table (*in thousands*):

|  | <b>Fiscal<br/>2016</b> | <b>Fiscal<br/>2015</b> | <b>Fiscal<br/>2014</b> |
|--|------------------------|------------------------|------------------------|
| Net sales  | \$ —                   | \$ —                   | \$ 402                 |
| Gross loss <sup>(1)</sup>                                    | —                      | —                      | (330)                  |
| Selling, general, and administrative expenses <sup>(2)</sup> | —                      | —                      | 215                    |
| Income tax provision (benefit) <sup>(3)</sup>                | —                      | 31                     | (375)                  |

Loss from discontinued operations, net of tax — (31) (170)

*Notes:*

- (1) *Gross loss for fiscal year 2014 includes unabsorbed manufacturing labor and overhead expenses related to the Manufacturing Agreement with RFPD which ended March 1, 2014.*
- (2) *Selling, General and Administrative expenses in fiscal year 2014 related primarily to professional fees for tax audits resulting from the Transaction.*
- (3) *The income tax provision for fiscal year 2015 was due to an income tax audit as a result of the Transaction. The income tax benefits in fiscal year 2014 relates to the reversal of tax reserves.*

## **6. RELATED PARTY TRANSACTION**

On June 15, 2015, the Company entered into a lease agreement for the IMES facility with LDL, LLC. The Executive Vice President of IMES, Lee A. McIntyre III (former owner of IMES), has an ownership interest in LDL, LLC. The lease agreement provides for monthly payments over five years with total future minimum lease payments of \$0.6 million. Rental expense related to this lease amounted to \$0.1 million for the fiscal year ended May 28, 2016. The Company shall be entitled to extend the term of the lease for a period of an additional five years by notifying the landlord in writing of its intention to do so within nine months of the expiration of the initial term.

On October 16, 2014, the Company repurchased 50,000 Class B shares from the Richardson Wildlife Foundation, an Illinois not-for-profit corporation, at a negotiated price of \$9.91 per share. Edward Richardson, Chairman and CEO of the Company, also serves as President of the Richardson Wildlife Foundation. These shares were repurchased pursuant to the Company's share repurchase authorization approved by its Board of Directors. Mr. Richardson filed a Form 4 to record the gifting of his Class B shares.

On August 9, 2013, the Company repurchased 300,000 Class B shares from Mr. Richardson at a negotiated price of \$11.50 per share. On May 15, 2013, the Company repurchased 48,925 Class B shares from the Richardson Wildlife Foundation and an additional 200,000 Class B shares from Mr. Richardson at a negotiated price of \$11.70 per share. These shares were repurchased pursuant to the Company's share repurchase authorization approved by its Board of Directors. Mr. Richardson filed a Form 4 to record the gifting or sale of his Class B shares.

## 7. **GOODWILL AND INTANGIBLE ASSETS**

### *Goodwill*

Changes in the carrying value of goodwill are as follows (*in thousands*):

|                                   | Goodwill |
|-----------------------------------|----------|
| Balance at May 30, 2015           | \$ —     |
| Premium paid for IMES acquisition | 6,332    |
| Balance at May 28, 2016           | \$ 6,332 |

Goodwill is initially recorded based on the premium paid for acquisitions and is subsequently tested for impairment, using the first day of our fourth quarter as the measurement date. We test goodwill for impairment annually and whenever events or circumstances indicates an impairment may have occurred, such as a significant adverse change in the business climate, loss of key personnel or a decision to sell or dispose of a reporting unit. The goodwill balance in its entirety relates to our IMES reporting unit which is included in the Healthcare segment.

In accordance with ASC 350 "*Intangibles - Goodwill and Other*", if indicators of impairment are deemed to be present, we would perform an interim impairment test and any resulting impairment loss would be charged to expense in the period identified.

For annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011, Accounting Standards Update (ASU) 2011-08, *Testing for Goodwill for Impairment* ("ASU 2011-08") permits an entity to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, an entity determines it is not likely that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary.

We had \$6.3 million of goodwill on our balance sheet as of May 28, 2016. In accordance with ASU 2011-08, the results of our goodwill impairment test as of February 28, 2016, indicated that the value of goodwill attributed to our IMES reporting unit, which is included in the Healthcare segment, was not impaired.

Projected future operating results and cash flows used for valuation purposes may, in testing for impairment, reflect considerable improvements relative to historical periods with respect to, among other things, revenue growth and operating margins. Although we believe our projected future operating results and cash flows and related estimates regarding fair values are based on reasonable assumptions, historically, projected operating results and cash flows have not always been achieved.

### *Intangible Assets*

Intangible assets are initially recorded at their fair market values determined on quoted market prices in active markets, if available, or recognized valuation models. Intangible assets that have finite useful lives are amortized over their useful lives and are tested for impairment when events or changes in circumstances occur that indicate possible impairment.

Our intangible assets represent the fair value for trade name, customer relationships, non-compete agreements, and technology acquired in connection with our acquisitions. Intangible assets subject to amortization as well as amortization expense are as follows (*in thousands*):

|                                | Intangible Assets Subject<br>to<br>Amortization as of |                 |
|--------------------------------|---|-----------------|
|                                | May 28,<br>2016                                       | May 30,<br>2015 |
| Gross Amounts:                 |   |                 |
| Trade Name                     | \$ 659  | \$ 29           |
| Customer Relationships         | 3,434   | 948             |
| Non-compete Agreements         | 177   | 47              |
| Technology                     | 230   | —               |
| Total Gross Amounts            | \$ 4,500  | \$ 1,024        |
| Accumulated Amortization:      |   |                 |
| Trade Name                     | \$ 231  | \$ 29           |
| Customer Relationships         | 374   | 221             |
| Non-compete Agreements         | 55  | 31              |
| Technology                     | 22  | —               |
| Total Accumulated Amortization | \$ 682  | \$ 281          |
| Net Intangibles                | \$ 3,818  | \$ 743          |

We determined that intangible assets were not impaired as of May 28, 2016 on the basis that no adverse events or changes in circumstances were identified that could indicate that the carrying amounts of such assets may not be recoverable.

The amortization expense associated with the intangible assets subject to amortization for the next five years is presented in the following table (*in thousands*):

| <u>Fiscal Year</u> | <u>Amortization<br/>Expense</u> |
|--------------------|---------------------------------|
| 2017               | \$ 362                          |
| 2018               | 434                             |
| 2019               | 246                             |
| 2020               | 258                             |
| 2021               | 246                             |
| Thereafter         | 2,272                           |

**Total amortization expense \$ 3,818**

The amortization expense associated with the intangible assets totaled approximately \$0.4 million during fiscal 2016 and \$0.1 million during both fiscal 2015 and fiscal 2014. The weighted average number of years of amortization expense remaining is 15.8 years.

**8. LEASE OBLIGATIONS, OTHER COMMITMENTS, AND CONTINGENCIES**

We lease certain warehouse and office facilities and office equipment under non-cancelable operating leases. Rent expense from continuing operations for fiscal 2016, 2015, and 2014 was \$2.0 million, \$1.8 million, and \$1.5 million, respectively. Our future lease commitments for minimum rentals, including common area maintenance charges and property taxes during the next five years are as follows (*in thousands*):

| Fiscal Year | Payments |
|-------------|----------|
| 2017        | \$ 1,599 |
| 2018        | 1,332    |
| 2019        | 1,282    |
| 2020        | 1,123    |
| 2021        | 645      |
| Thereafter  | 327      |

**9. INCOME TAXES**

Loss from continuing operations before income taxes includes the following components (*in thousands*):

|                          | Fiscal Year Ended |                 |                 |
|--------------------------|-------------------|-----------------|-----------------|
|                          | May 28,<br>2016   | May 30,<br>2015 | May 31,<br>2014 |
| United States            | \$(7,274)         | \$(9,287)       | \$(1,399)       |
| Foreign                  | 1,054             | 2,293           | 747             |
| Loss before income taxes | \$(6,220)         | \$(6,994)       | \$(652 )        |

The provision (benefit) for income taxes for fiscal 2016, 2015, and 2014 consists of the following (*in thousands*):

|               | Fiscal Year Ended  |                 |                 |
|---------------|--------------------|-----------------|-----------------|
|               | May<br>28,<br>2016 | May 30,<br>2015 | May 31,<br>2014 |
| Current:      |                    |                 |                 |
| Federal       | \$0                | \$(326 )        | \$214           |
| State         | 17                 | 14              | 1               |
| Foreign       | 441                | 191             | 601             |
| Total current | \$458              | \$(121 )        | \$816           |



|                                |       |           |           |
|--------------------------------|-------|-----------|-----------|
| Deferred:                      |       |           |           |
| Federal                        | \$0   | \$(1,964) | \$(585 )  |
| State                          | 0     | 530       | (169 )    |
| Foreign                        | 88    | 89        | (369 )    |
| Total deferred                 | \$88  | \$(1,345) | \$(1,123) |
| Income tax provision (benefit) | \$546 | \$(1,466) | \$(307 )  |

The differences between income taxes at the U.S. federal statutory income tax rate of 34% and the reported income tax provision (benefit) for fiscal 2016, 2015, and 2014 are summarized as follows:

|   | Fiscal Year Ended |   |              |   |              |   |
|---|-------------------|---|--------------|---|--------------|---|
|   | May 28, 2016      |   | May 30, 2015 |   | May 31, 2014 |   |
|   | 34                | % | 34           | % | 34           | % |
| Federal statutory rate                                      | 34                | % | 34           | % | 34           | % |
| Effect of:  |                   |   |              |   |              |   |
| State income taxes, net of federal tax benefit              | 4.2               |   | 5.3          |   | 14.1         |   |
| Foreign income inclusion                                    | (0.4 )            |   | (1.6 )       |   | (10.2)       |   |
| Foreign taxes at other rates                                | 0.6               |   | 4.4          |   | (4.4 )       |   |
| Permanent tax differences                                   | (0.8 )            |   | (0.5 )       |   | (3.9 )       |   |
| Intercompany items  | —                 |   | 2.2          |   | (11.0)       |   |
| Compensation items  | —                 |   | —            |   | (12.7)       |   |
| Tax reserves  | (6.0 )            |   | 0.8          |   | (7.2 )       |   |
| Additional U.S. tax on undistributed foreign earnings       | (32.7)            |   | (0.5 )       |   | 37.6         |   |
| Net increase in valuation allowance for deferred tax assets | (11.4)            |   | (27.3)       |   | (3.4 )       |   |
| Return to provision adjustments                             | 3.9               |   | 4.0          |   | 15.3         |   |
| Other   | (0.2 )            |   | 0.1          |   | (1.2 )       |   |
| Effective tax rate  | (8.8) %           |   | 20.9 %       |   | 47.0 %       |   |

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 amounts used for income tax purposes. Our deferred tax assets and liabilities reflect continuing operations as of May 28, 2016 and May 30, 2015. Significant components are as follows (*in thousands*):

|   | Fiscal Year Ended |                 |
|---|-------------------|-----------------|
|   | May 28,<br>2016   | May 30,<br>2015 |
| Deferred tax assets:                              |                   |                 |
| NOL carryforwards - foreign and domestic          | \$9,089           | \$5,960         |
| Inventory valuations                              | 1,141             | 1,060           |
| Goodwill  | 798               | 1,031           |
| Foreign tax credits                               | 304               | 322             |
| Severance reserve                                 | 34                | —               |
| Foreign capital loss                              | 1,079             | 1,073           |
| Other   | 2,167             | 1,983           |
| Subtotal  | \$14,612          | \$11,429        |
| Valuation allowance - foreign and domestic        | (5,871 )          | (5,158 )        |
| Net deferred tax assets after valuation allowance | \$8,741           | \$6,271         |
| Deferred tax liabilities:                         |                   |                 |
| Accelerated depreciation                          | \$(973 )          | \$(218 )        |
| Tax on undistributed foreign earnings             | (6,702 )          | (4,813 )        |
| Other   | (175 )            | (202 )          |
| Subtotal  | \$(7,850 )        | \$(5,233 )      |
| Net deferred tax assets                           | \$891             | \$1,038         |
| Supplemental disclosure of deferred tax assets :  |                   |                 |
| Domestic  | \$4,190           | \$3,477         |
| Foreign   | \$2,549           | \$2,710         |
| Total   | \$6,739           | \$6,187         |

As of May 28, 2016, we had approximately \$5.7 million of net deferred tax assets for federal net operating loss ("NOL") carryforwards, compared to \$3.0 million as of May 30, 2015. Net deferred tax assets for domestic state NOL carryforwards amounted to approximately \$2.7 million, compared to \$2.4 million during fiscal year 2015. Net deferred tax assets related to foreign NOL carryforwards totaled approximately \$0.6 million with various or indefinite expiration dates. The amount of net deferred tax assets related to foreign NOL carryforwards was the same as the fiscal year 2015. We also have a net deferred tax asset of \$0.3 million related to foreign tax credit carryforwards as of May 28, 2016 and May 30, 2015. The changes in balances from prior year for the federal NOL carryforwards is driven by current year forecast taxable losses. We do not have any alternative minimum tax credit carryforward as of May 28, 2016.

We have historically determined that certain undistributed earnings of our foreign subsidiaries, to the extent of cash available, will be repatriated to the U.S. Accordingly, we have provided a deferred tax liability totaling \$6.7 million

and \$4.8 million as of May 28, 2016 and May 30, 2015, respectively, on foreign earnings of \$48.7 million and \$38.2 million, respectively. The increase year over year relates to the change in management's assertion for RELL China. As of the fourth quarter of fiscal year 2016, we changed our assertion to no longer be permanently reinvested in China. In addition, as of May 28, 2016, \$5.7 million of cumulative positive earnings of some of our foreign subsidiaries are still considered permanently reinvested pursuant to ASC 740-30, Income Taxes - Other Considerations or Special Areas ("ASC 740-30"). Due to various tax attributes that are continuously changing, it is not practicable to determine what, if any, tax liability might exist if such earnings were to be repatriated.

Management assesses the available positive and negative evidence to estimate if sufficient future taxable income will be generated to use the existing deferred tax assets. A significant component of objective evidence evaluated was the cumulative income or loss incurred in each jurisdiction over the three-year period ended May 28, 2016. Such objective evidence limits the ability to consider subjective evidence such as future income projections. We considered other positive evidence in determining the need for a valuation allowance in the U.S. including the repatriation of foreign earnings which we do not consider permanently reinvested in certain of our foreign subsidiaries. The weight of this positive evidence is not sufficient to outweigh other negative evidence in evaluating our need for a valuation allowance in the U.S. jurisdiction.

As of May 28, 2016, a valuation allowance of \$5.9 million has been established to record only the portion of the deferred tax asset that will more likely than not be realized. There has been an increase in the valuation allowance from May 30, 2015 in the amount of \$0.7 million. The valuation allowance on deferred tax assets in foreign jurisdictions relates to jurisdictions where historical taxable losses have been incurred. We also recorded a valuation allowance for all domestic federal and state net deferred tax assets considering the significant cumulative losses in the U.S. jurisdiction, the reversal of the deferred tax liability for foreign earnings, and no forecast of additional U.S. income. The amount of the deferred tax asset considered realizable, however, could be adjusted if estimates of future taxable income during the carryforward period are increased, or if objective negative evidence in the form of cumulative losses is no longer present and additional weight may be given to subjective evidence such as our projections for growth.

Income taxes paid, including foreign estimated tax payments, were \$0.7 million, \$0.5 million, and \$2.1 million, during fiscal 2016, 2015, and 2014, respectively.

In the normal course of business, we are subject to examination by taxing authorities throughout the world. Generally, years prior to fiscal 2006 are closed for examination under the statute of limitation for U.S. federal, U.S. state and local, or non-U.S. tax jurisdictions. We are under examination in the state of Illinois for fiscal years 2012 and 2013. We are currently under examination in Thailand for fiscal years 2008 through 2011 and France for fiscal years 2013 and 2015. Our primary foreign tax jurisdictions are Germany and the Netherlands. After the closure of the Germany tax audit for fiscal years 2009 through 2011, we have tax years open in Germany beginning in fiscal 2012 and the Netherlands beginning in fiscal 2010.

The uncertain tax positions from continuing operations as of May 28, 2016 and May 30, 2015, totaled \$0.1 million. We record penalties and interest relating to uncertain tax positions in the income tax expense line item within the unaudited consolidated statements of income and comprehensive income. It is not expected that there will be a change in the unrecognized tax benefits within the next 12 months. The following table summarizes the activity related to the unrecognized tax benefits (*in thousands*):

|  | Fiscal Year |         |
|--|-------------|---------|
|  | Ended       |         |
|  | May         | May     |
|  | 28,         | 30,     |
|  | 2016        | 2015    |
| Unrecognized tax benefits, beginning of period | \$2,000     | \$161   |
| Increase in positions taken in prior period    | 299         | 2,000   |
| Decrease in positions due to settlements       | (299 )      | (161 )  |
| Unrecognized tax benefits, end of period       | \$2,000     | \$2,000 |

Unrecognized tax benefits for continuing and discontinued operations are as follows *(in thousands)*:

|  | Fiscal Year<br>Ended        |                             |
|--|-----------------------------|-----------------------------|
|  | <b>May<br/>28,<br/>2016</b> | <b>May<br/>30,<br/>2015</b> |
| Continuing operations                  | \$117                       | \$117                       |
| Discontinued operations <sup>(1)</sup> | 1,883                       | 1,883                       |
|  | \$2,000                     | \$2,000                     |

*(1) Relates to an amended state income tax return*

We record penalties and interest relating to uncertain tax positions in the income tax expense line item within the Consolidated Statements of Comprehensive Income (Loss). Accrued interest and penalties are included within the related tax liability line in the Consolidated Balance Sheets. We have not recorded a liability for interest and penalties as of May 28, 2016, and none were recorded during May 30, 2015.

It is not expected that there will be a change in the unrecognized tax benefits due to the expiration of various statutes of limitations within the next 12 months.

## 10.EMPLOYEE BENEFIT PLANS

*Employee Profit Sharing Plan:* The employee profit sharing plan is a defined contribution profit sharing plan for employees. The profit sharing plan has a 401(k) provision whereby we match 50% of employee contributions up to 4.0% of pay. Charges to expense for matching contributions to this plan were \$0.4 million, \$0.3 million, and \$0.3 million, during fiscal years 2016, 2015, and 2014, respectively.

## 11.SEGMENT AND GEOGRAPHIC INFORMATION

During the first quarter of fiscal 2015, we created a new strategic business unit called Healthcare. As hospitals remain under pressure to reduce costs while serving a much larger customer base, there is a growing demand for independent sources of high value replacement parts for diagnostic imaging. Having access to parts that are tested and in stock enables hospitals to terminate expensive service contracts with OEM and instead use third party service providers or in-house technicians. With our global infrastructure, technical sales team, and experience servicing the healthcare market, we are well positioned to take advantage of this market opportunity. Over time, our plan is to expand our position from being the leader in power grid tubes to a key player in the high-growth, high-profile Healthcare industry.

In accordance with ASC 280-10, *Segment Reporting*, we have identified three reportable segments: PMT and Canvys, and Healthcare.

Electron Device Group (“EDG”), renamed Power and Microwave Technologies Group (“PMT”) in July 2015, provides engineered solutions and distributes electronic components to customers in alternative energy, aviation, broadcast, communications, industrial, marine, medical, military, scientific, and semiconductor markets. PMT focuses on various applications including broadcast transmission, CO2 laser cutting, diagnostic imaging, dielectric and induction heating, high energy transfer, high voltage switching, plasma, power conversion, radar, and radiation oncology. PMT also offers its customers technical services for both microwave and industrial equipment.

Canvys provides customized display solutions serving the corporate enterprise, financial, industrial, and OEM markets.

Healthcare manufactures, distributes and services high value replacement parts for the healthcare market including hospitals, medical centers, independent service organizations, and multi-vendor service providers. Products include power grid tubes, hydrogen thyratrons, klystrons, magnetrons; Image Systems medical displays and workstations for picture archiving and communication systems (“PACS”); visual solutions for operating rooms/surgical environments; digital radiography solutions including replacement flat panel detectors and upgrades; and additional replacement components currently under development for the diagnostic imaging service market. Through a combination of newly developed products and partnerships, service offerings, and training programs, we believe we can help our customers improve efficiency and deliver better clinical outcomes while lowering the cost of healthcare delivery.

The CEO evaluates performance and allocates resources primarily based on the gross profit of each segment.



Operating results by segment are summarized in the following table (*in thousands*):

|               | Fiscal Year Ended |                 |                 |
|---------------|-------------------|-----------------|-----------------|
|               | May 28,<br>2016   | May 30,<br>2015 | May 31,<br>2014 |
| <u>PMT</u>    |                   |                 |                 |
| Net Sales     | \$105,554         | \$105,748       | \$103,274       |
| Gross Profit  | 33,088            | 33,098          | 31,610          |
| <u>Canvys</u> |                   |                 |                 |
| Net Sales     | \$23,453          | \$24,645        | \$27,857        |
| Gross Profit  | 6,017             | 6,457           | 7,588           |
| Healthcare    |                   |                 |                 |
| Net Sales     | \$13,009          | \$6,564         | \$6,829         |
| Gross Profit  | 5,730             | 1,583           | 1,816           |

A reconciliation of assets to the relevant consolidated amount is as follows (*in thousands*):

|  | May 28,<br>2016 | May 30,<br>2015 |
|--|-----------------|-----------------|
| Segment assets                                   | \$80,210        | \$60,200        |
| Cash and cash equivalents                        | 60,454          | 74,535          |
| Investments - current                            | 2,268           | 23,692          |
| Other current assets <sup>(1)</sup>              | 3,143           | 3,494           |
| Net property                                     | 12,986          | 10,081          |
| Investments - non-current                        | 7,799           | 11,549          |
| Other assets - non-current deferred income taxes | 1,270           | 1,443           |
| Total assets                                     | \$168,130       | \$184,994       |

(1) Other current assets include miscellaneous receivables, prepaid expenses, and current deferred income taxes.

Assets are not disclosed by reportable segment as the Company does not track assets by reportable segment and certain assets are not specific to any reportable segment.

Capital expenditures for our Healthcare segment during fiscal 2016 were approximately \$2.9 million. In addition, we also had capital expenditures during fiscal year 2016 and fiscal year 2015 related to the Company's new ERP system that are not specific to any particular reportable segment.

Geographic net sales information is primarily grouped by customer destination into five areas: North America; Asia/Pacific; Europe; Latin America; and Other.

Net sales and gross profit by geographic region are summarized in the following table (*in thousands*):

|                     | Fiscal Year Ended |                 |                 |
|---------------------|-------------------|-----------------|-----------------|
|                     | May 28,<br>2016   | May 30,<br>2015 | May 31,<br>2014 |
| <u>Net Sales</u>    |                   |                 |                 |
| North America       | \$66,365          | \$59,742        | \$57,137        |
| Asia/Pacific        | 24,564            | 24,605          | 24,069          |
| Europe              | 44,634            | 44,425          | 47,610          |
| Latin America       | 6,347             | 8,275           | 8,936           |
| Other (1)           | 106               | (90 )           | 208             |
| Total               | \$142,016         | \$136,957       | \$137,960       |
| <u>Gross Profit</u> |                   |                 |                 |
| North America       | \$23,506          | \$20,352        | \$18,905        |
| Asia/Pacific        | 8,212             | 7,967           | 7,849           |
| Europe              | 13,541            | 14,051          | 15,506          |
| Latin America       | 2,397             | 3,082           | 3,231           |
| Other (1)           | (2,821 )          | (4,314 )        | (4,477 )        |
| Total               | \$44,835          | \$41,138        | \$41,014        |

(1) *Other primarily includes net sales not allocated to a specific geographical region, unabsorbed value-add costs, and other unallocated expenses.*

We sell our products to customers in diversified industries and perform periodic credit evaluations of our customers' financial condition. Terms are generally on open account, payable net 30 days in North America, and vary throughout Asia/Pacific, Europe, and Latin America. Estimates of credit losses are recorded in the financial statements based on monthly reviews of outstanding accounts.

Net assets by geographic region are summarized in the following table (in thousands):

|                   | Fiscal Year Ended |                 |                 |
|-------------------|-------------------|-----------------|-----------------|
|                   | May 28,<br>2016   | May 30,<br>2015 | May 31,<br>2014 |
| <u>Net Assets</u> |                   |                 |                 |
| North America     | \$65,832          | \$76,153        | \$88,902        |
| Asia/Pacific      | 42,547            | 44,602          | 45,334          |
| Europe            | 31,495            | 34,127          | 38,407          |
| Latin America     | 1,801             | 1,770           | 2,202           |
| Total             | \$141,675         | \$156,652       | \$174,845       |

The Company has long-lived assets of \$16.8 million as of May 28, 2016. The long-lived assets, which include our fixed assets and intangibles, are primarily in the US. There are approximately \$1.3 million of long-lived assets that belong to our foreign affiliates.

The Company had depreciation and amortization expense of \$2.4 million as of May 28, 2016. The depreciation and amortization, which includes our fixed assets and intangibles, are primarily in the US. There was approximately \$0.3 million of depreciation and amortization expense that belong to our foreign affiliates.

## 12. LITIGATION

We are involved in several pending judicial proceedings concerning matters arising in the ordinary course of business. While the outcome of litigation is subject to uncertainties, based on information available at the time the financial statements were issued, we determined disclosure of contingencies relating to any of our pending judicial proceedings was not necessary because there was less than a reasonable possibility that a material loss had been incurred.

During fiscal 2014, we received settlements in the amount of \$2.5 million related to an antitrust class action lawsuit settlement. The settlement was recorded as proceeds from legal settlement within the Other Income section of our Consolidated Statements of Comprehensive Income (Loss).

### **13. FAIR VALUE MEASUREMENTS**

ASC 820, *Fair Value Measurements and Disclosures* (“ASC 820”), defines fair value, establishes a framework for measuring fair value in accordance with accounting principles generally accepted in the United States, and expands disclosures about fair value measurements.

ASC 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists; therefore requiring an entity to develop its own assumptions.

As of May 28, 2016, we held investments that are required to be measured at fair value on a recurring basis. Our investments consist of time deposits and CDs, where face value is equal to fair value, and equity securities of publicly traded companies for which market prices are readily available.

Investments measured at fair value on a recurring basis subject to the disclosure requirements of ASC 820 as of May 28, 2016 and May 30, 2015, were as follows (*in thousands*):

|                     | Level 1  | Level 2 | Level 3 |
|---------------------|----------|---------|---------|
| <u>May 28, 2016</u> |          |         |         |
| Time deposits/CDs   | \$9,517  | \$ —    | \$ —    |
| Equity securities   | 550      | —       | —       |
| Total               | \$10,067 | \$ —    | \$ —    |
| May 30, 2015        |          |         |         |
| Time deposits/CDs   | \$34,665 | \$ —    | \$ —    |
| Equity securities   | 576      | —       | —       |
| Total               | \$35,241 | \$ —    | \$ —    |

#### 14. VALUATION AND QUALIFYING ACCOUNTS

The following table presents the valuation and qualifying account activity for fiscal year ended May 28, 2016, May 30, 2015, and May 31, 2014, (*in thousands*):

| Description                     | Balance at beginning of period | Charged to expense | Deductions  | Balance at end of period |
|---------------------------------|--------------------------------|--------------------|-------------|--------------------------|
| <u>Year ended May 28, 2016</u>  |                                |                    |             |                          |
| Allowance for doubtful accounts | \$ 283                         | \$ 228 (1)         | \$(147) (2) | \$ 364                   |
| Inventory provisions            | 2,991                          | 690 (3)            | 301 (4)     | 3,380                    |
| Year ended May 30, 2015         |                                |                    |             |                          |
| Allowance for doubtful accounts | \$ 581                         | \$(221) (1)        | \$ 77 (2)   | \$ 283                   |
| Inventory provisions            | 3,141                          | 228 (3)            | 378 (4)     | 2,991                    |
| Year ended May 31, 2014         |                                |                    |             |                          |
| Allowance for doubtful accounts | \$ 1,092                       | \$ 114 (1)         | \$ 625 (2)  | \$ 581                   |
| Inventory provisions            | 2,715                          | 751 (3)            | 325 (4)     | 3,141                    |

Notes:

(1) Charges to bad debt expense, net of bad debt recoveries.

(2) Uncollectible amounts written off, net of recoveries and foreign currency translation.

(3) Charges to cost of sales. Included in fiscal 2016 are inventory write-downs of \$0.3 million for PMT and \$0.3 million for Canvys, and less than \$0.1 million for Healthcare.

(4) Inventory disposed of or sold, net of foreign currency translation.



**15. SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)**

| Description                                | First<br>Quarter | Second<br>Quarter | Third<br>Quarter | Fourth<br>Quarter |
|--|------------------|-------------------|------------------|-------------------|
| <b>Fiscal 2016</b>                         |                  |                   |                  |                   |
| Net sales                                  | \$37,071         | \$34,086          | \$31,291         | \$39,568          |
| Gross profit                               | 11,262           | 10,435            | 9,750            | 13,388            |
| Loss from continuing operations            | (1,399 )         | (2,286 )          | (2,926 )         | (155 )            |
| Income (loss) from discontinued operations | —                | —                 | —                | —                 |
| Net loss                                   | (1,399 )         | (2,286 )          | (2,926 )         | (155 )            |
| Loss from continuing operations            |                  |                   |                  |                   |
| Common stock - basic                       | \$(0.10 )        | \$(0.18 )         | \$(0.23 )        | \$(0.01 )         |
| Class B common stock - basic               | \$(0.10 )        | \$(0.16 )         | \$(0.21 )        | \$(0.01 )         |
| Common stock - diluted                     | \$(0.10 )        | \$(0.18 )         | \$(0.23 )        | \$(0.01 )         |
| Class B common stock - diluted             | \$(0.10 )        | \$(0.16 )         | \$(0.21 )        | \$(0.01 )         |
| Net loss                                   |                  |                   |                  |                   |
| Common stock - basic                       | \$(0.10 )        | \$(0.18 )         | \$(0.23 )        | \$(0.01 )         |
| Class B common stock - basic               | \$(0.10 )        | \$(0.16 )         | \$(0.21 )        | \$(0.01 )         |
| Common stock - diluted                     | \$(0.10 )        | \$(0.18 )         | \$(0.23 )        | \$(0.01 )         |
| Class B common stock - diluted             | \$(0.10 )        | \$(0.16 )         | \$(0.21 )        | \$(0.01 )         |
| <b>Fiscal 2015</b>                         |                  |                   |                  |                   |
| Net sales                                  | \$34,699         | \$33,841          | \$33,471         | \$34,946          |
| Gross profit                               | 10,658           | 10,462            | 9,800            | 10,218            |
| Loss from continuing operations            | (83 )            | (1,144 )          | (2,198 )         | (2,103 )          |
| Income (loss) from discontinued operations | —                | 87                | —                | (118 )            |
| Net loss                                   | (83 )            | (1,057 )          | (2,198 )         | (2,221 )          |
| Loss from continuing operations            |                  |                   |                  |                   |
| Common stock - basic                       | \$(0.01 )        | \$(0.08 )         | \$(0.16 )        | \$(0.16 )         |
| Class B common stock - basic               | \$(0.01 )        | \$(0.07 )         | \$(0.15 )        | \$(0.13 )         |
| Common stock - diluted                     | \$(0.01 )        | \$(0.08 )         | \$(0.16 )        | \$(0.16 )         |
| Class B common stock - diluted             | \$(0.01 )        | \$(0.07 )         | \$(0.15 )        | \$(0.13 )         |
| Income (loss) from discontinued operations |                  |                   |                  |                   |
| Common stock - basic                       | \$—              | \$0.01            | \$—              | \$(0.01 )         |
| Class B common stock - basic               | \$—              | \$0.01            | \$—              | \$(0.01 )         |
| Common stock - diluted                     | \$—              | \$0.01            | \$—              | \$(0.01 )         |
| Class B common stock - diluted             | \$—              | \$0.01            | \$—              | \$(0.01 )         |
| Net loss                                   |                  |                   |                  |                   |
| Common stock - basic                       | \$(0.01 )        | \$(0.07 )         | \$(0.16 )        | \$(0.17 )         |
| Class B common stock - basic               | \$(0.01 )        | \$(0.06 )         | \$(0.15 )        | \$(0.14 )         |
| Common stock - diluted                     | \$(0.01 )        | \$(0.07 )         | \$(0.16 )        | \$(0.17 )         |
| Class B common stock - diluted             | \$(0.01 )        | \$(0.06 )         | \$(0.15 )        | \$(0.14 )         |

**Report of Independent Registered Public Accounting Firm**

Board of Directors and Stockholders

Richardson Electronics, Ltd.

LaFox, Illinois

We have audited the accompanying consolidated balance sheets of Richardson Electronics, Ltd. as of May 28, 2016 and May 30, 2015 and the related consolidated statements of comprehensive income (loss), stockholders' equity, and cash flows for each of the two years in the period ended May 28, 2016. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with 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 financial statements are free of material misstatement. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Richardson Electronics, Ltd. at May 28, 2016 and May 30, 2015, and the results of its operations and its cash flows for each of the two years in the period ended May 28, 2016, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Richardson Electronics, Ltd.'s internal control over financial reporting as of May 28, 2016, based on criteria established in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated July 29, 2016, expressed an unqualified opinion thereon.

/s/ BDO USA, LLP



Chicago, Illinois

July 29, 2016

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**Report of Independent Registered Public Accounting Firm**

Board of Directors and Stockholders

Richardson Electronics, Ltd.

LaFox, Illinois

We have audited the accompanying consolidated balance sheet of Richardson Electronics, Ltd. as of May 31, 2014, and the related consolidated statements of comprehensive income (loss), stockholders' equity, and cash flows for each of the two years in the period ended May 31, 2014. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with 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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Richardson Electronics, Ltd. at May 31, 2014, and the consolidated results of its operations and its cash flows for each of the two years in the period ended May 31, 2014, in conformity with U.S. generally accepted accounting principles.

/s/ Ernst & Young LLP

Chicago, Illinois

July 25, 2014 except for note 6 and note 11, as to which the date is July 27, 2015

## Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders

Richardson Electronics, Ltd.

LaFox, Illinois

We have audited Richardson Electronics, Ltd.'s internal control over financial reporting as of May 28, 2016, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Richardson Electronics, Ltd.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying "Item 9A, Management's Report on Internal Control Over Financial Reporting". Our responsibility is to express an opinion on the company's internal control over financial reporting 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 effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, 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 the policies or procedures may deteriorate.

In our opinion, Richardson Electronics, Ltd. maintained, in all material respects, effective internal control over financial reporting as of May 28, 2016, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Richardson Electronics, Ltd. as of May 28, 2016 and May 30, 2015 and the related consolidated statements of comprehensive income (loss), stockholders' equity, and cash flows for each of the two years in the period ended May 28, 2016 and our report dated July 29, 2016 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP

Chicago, Illinois

July 29, 2016

## ITEM 9A. CONTROLS AND PROCEDURES

### (a) Evaluation of Disclosure Controls and Procedures

Management of the Company, with the participation of the Chief Executive Officer and the Chief Financial Officer, evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") as of May 28, 2016. Disclosure controls and procedures are intended to provide reasonable assurance that information required to be disclosed in the Company's Exchange Act reports is recorded, processed, summarized, and reported within the time periods specified by the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to management, including the Company's Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as of May 28, 2016.

### (a) Management's Report on Internal Control over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Exchange Act Rules 13a-15(f) and 15d-15(f). Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness of future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a deficiency in internal control over financial reporting that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected.

Under the supervision of the Chief Executive Officer and Chief Financial Officer, management conducted an assessment of the effectiveness of our internal control over financial reporting as of May 28, 2016, based on the framework in the *Internal Control-Integrated Framework (2013)* published by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based on that assessment, management has concluded that the Company's internal control over financial reporting was effective as of May 28, 2016.

Management's assessment of the effectiveness of our internal control over financial reporting as of May 28, 2016, has been audited by BDO USA, LLP, an independent registered public accounting firm, as stated in their report which is included herein.

(a) Changes in Internal Control over Financial Reporting

There have been no changes in the Company's internal control over financial reporting during the most recent fiscal year that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**ITEM 9B. OTHER INFORMATION**

None

**Results of Operation and Financial Condition and Declaration of Dividend**

On July 20, 2016, we issued a press release reporting results for our fourth quarter and fiscal year ended May 28, 2016, and the declaration of a quarterly cash dividend. A copy of the press release is furnished as Exhibit 99.1 to this Form 10-K and incorporated by reference herein.

## **PART III**

### **ITEM 10. Directors, Executive Officers and Corporate Governance**

Information concerning directors and executive officers of the registrant will be contained in our Proxy Statement to be issued in connection with our Annual Meeting of Stockholders scheduled to be held on October 4, 2016, and is incorporated herein by reference.

### **ITEM 11. Executive Compensation**

Information concerning executive compensation will be contained in our Proxy Statement to be issued in connection with our Annual Meeting of Stockholders scheduled to be held on October 4, 2016, and is incorporated herein by reference.

### **ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

Information concerning security ownership of certain beneficial owners and management will be contained in our Proxy Statement to be issued in connection with our Annual Meeting of Stockholders scheduled to be held on October 4, 2016, and is incorporated herein by reference.

#### ***Equity Compensation Plan Information***

The following table sets forth information as of May 28, 2016, with respect to compensation plans under which equity securities are authorized for issuance:

| Plan Category | Number of Securities to be Issued | Weighted Average Per Share Exercise | Number of Securities Remaining |
|---------------|-----------------------------------|-------------------------------------|--------------------------------|
|---------------|-----------------------------------|-------------------------------------|--------------------------------|



|   | Upon Exercise<br>of Outstanding<br>Options,<br>Warrants and<br>Rights | Price of<br>Outstanding<br>Options,<br>Warrants<br>and Rights | Available for<br>Future Issuance<br>Under Equity<br>Compensation<br>Plans<br>(Excluding<br>Securities<br>Reflected in the<br>First Column) |
|---|---|---|--|
| Equity Compensation Plans Approved by<br>Security Holders     | 995,375   | \$9.86  | 949,542  |
| Equity Compensation Plans Not Approved by<br>Security Holders | 23,564  | (1) \$12.95   | (1) —  |
| Total   | 1,018,939   | \$9.93  | 949,542  |

(1) *Options issued in 1987 pursuant to an employment contract with a former officer and director of Richardson Electronics, Ltd.*

### **ITEM 13. Certain Relationships and Related Transactions, and Director Independence**

Information concerning certain relationships and related transactions will be contained in our Proxy Statement to be issued in connection with our Annual Meeting of Stockholders scheduled to be held on October 4, 2016, and is incorporated herein by reference.

### **ITEM 14. Principal Accountant Fees and Services**

Information concerning accountant fees and services will be contained in our Proxy Statement to be issued in connection with our Annual Meeting of Stockholders scheduled to be held on October 4, 2016, and is incorporated herein by reference.

**PART IV**

**ITEM 15. Exhibits and Financial Statement Schedules**

(a) Exhibit

See Exhibit Index.

(b) Financial Statements and Financial Statement Schedules.

Our consolidated financial statements being filed as part of this Form 10-K are filed on Item 8 of this Form 10-K. All other schedules for which provision is made in the applicable accounting regulations of the Securities and Exchange Commission are not required under the related instructions or are inapplicable, and therefore have been omitted.

**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.

| Signature  | Title  | Date          |
|--|--|---------------|
| By: /s/ Edward J. Richardson<br>Edward J. Richardson | Chairman of the Board, Chief Executive Officer<br>(Principal Executive Officer), President, and Director | July 29, 2016 |

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.

| Signature  | Title  | Date             |
|--|--|------------------|
| /s/ Edward J. Richardson<br>Edward J. Richardson | Chairman of the Board, Chief Executive Officer (Principal Executive Officer),<br>President, and Director | July 29,<br>2016 |
| /s/ Robert J. Ben<br>Robert J. Ben               | Chief Financial Officer (Principal Financial Officer)  | July 29,<br>2016 |
| /s/ James M. Dudek Jr.<br>James M. Dudek Jr.     | Corporate Controller and Chief Accounting Officer (Principal Accounting<br>Officer)                      | July 29,<br>2016 |
| /s/ Paul J. Plante<br>Paul J. Plante             | Director   | July 29,<br>2016 |
| /s/ Jacques Belin<br>Jacques Belin               | Director   | July 29,<br>2016 |
| /s/ James Benham<br>James Benham                 | Director   | July 29,<br>2016 |

/s/ Kenneth  
Halverson  
Kenneth Halverson

Director

July 29,  
2016

**PART IV**

**ITEM 15. Exhibits and Financial Statement Schedules**

*(a) List of Documents Filed as a Part of This Report:*

*(1) Index to Consolidated Financial Statements:*

Consolidated Balance Sheets as of May 28, 2016, and May 30, 2015.

Consolidated Statements of Comprehensive Income (Loss) for each of the three years ended May 28, 2016, May 30, 2015, and May 31, 2014.

Consolidated Statements of Cash Flows for each of the three years ended May 28, 2016, May 30, 2015, and May 31, 2014.

Consolidated Statements of Stockholders' Equity for each of the three years ended May 28, 2016, May 30, 2015, and May 31, 2014.

Notes to Consolidated Financial Statements.

Report of BDO USA, LLP, Independent Registered Public Accounting Firm.

Report of Ernst & Young LLP, Independent Registered Public Accounting Firm.

*(2) Index to Financial Statement Schedules:*

All schedules have been omitted because the required information is included in the consolidated financial statements or the notes thereto, or is not applicable or required.

| Exhibit Number | Description  |
|----------------|--|
| 2(a)           | Purchase Agreement between the Company and International Medical Equipment & Services, Inc. dated June 15, 2015 (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K filed with the SEC on June 17, 2015).  |
| 3(a)           | Restated Certificate of Incorporation of the Company, (incorporated by reference to the Company's Registration Statement on Form S-4, Registration No. 33-8696, dated November 13, 1986).  |
| 3(b)           | Amended and Restated By-Laws of the Company (incorporated by reference to Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended December 3, 2011).   |
| 3(c)           | Amended and Restated By-Laws of the Company (incorporated by reference to Exhibit 3.2 to the Company's Current Report on Form 8-K filed with the SEC on October 15, 2012).   |
| 3(d)           | Amended and Restated Certificate of Incorporation of the Company, incorporated by reference to Annex III of the Proxy Statement filed August 22, 2014  |
| 10(a) †        | Richardson Electronics, Ltd. 2011 Long-Term Incentive Plan (incorporated by reference to Annex A to the Company's Proxy Statement on Schedule 14A, filed with the Securities and Exchange Commission on August 23, 2011).  |
|                | Amendment to the Richardson Electronics, Ltd. 2011 Long-Term Incentive Plan (incorporated by reference to Annex II to the Company's Proxy Statement on Schedule 14A, filed with the Securities and Exchange Commission on August 28, 2014).  |
| 10(e) †        | Edward J. Richardson Incentive Compensation Plan (incorporated by reference to Appendix F to the Company's Proxy Statement on Schedule 14A, filed with the Securities and Exchange Commission on September 14, 2007).  |
| 10(e)(i) †     | Amended and Restated Edward J. Richardson Incentive Plan (incorporated by reference to Appendix A to the Company's Proxy Statement on Schedule 14A, filed with the SEC on August 30, 2012).  |
| 10(f) †        | Richardson Electronics, Ltd. 2006 Stock Option Plan for Non-Employee Directors (incorporated by reference to Exhibit A to the Company's Proxy Statement on Schedule 14A, filed with the Securities and Exchange Commission on September 12, 2005).   |
| 10(g) †        | Employment, Nondisclosure and Non-Compete Agreement, dated June 1, 2004, by and between the Company and Wendy Diddell (incorporated by reference to Exhibit 10.47 to the Company's Amendment No. 4 to the Registration Statement on Form S-1, Registration No. 333-113568, filed June 14, 2004).     |
| 10(g)(i) †     | First Amendment to Employment, Nondisclosure and Non-Compete Agreement, dated May 31, 2007, by and between the Company and Wendy Diddell (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K, filed with the Securities and Exchange Commission on June 6, 2007). |

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- 10(h) † Employment, Nondisclosure and Non-Compete Agreement, dated October 24, 2007, by and between the Company and Kathleen Dvorak (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K, filed with the Securities and Exchange Commission on October 25, 2007).
- 10(j) † Employment, Nondisclosure and Non-Compete Agreement dated June 26, 2014, by and between the Company and Gregory J. Peloquin (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed with the SEC on June 27, 2014).
- 10(k) † Form of Non-Qualified Stock Option Agreement issued under the Richardson Electronics, Ltd. Employees' 2001 Incentive Compensation Plan (incorporated by reference to Exhibit 10(o) to the Company's Annual Report on Form 10-K for the fiscal year ended May 31, 2008).
- 10(n) Acquisition Agreement, dated October 1, 2010, among Richardson Electronics, Ltd., certain subsidiaries of Richardson Electronics, Ltd. and Arrow Electronics, Inc. (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K, filed with the Securities and Exchange Commission on October 1, 2010).

| Exhibit Number | Description  |
|----------------|--|
| 10(o)(i)       | Amendment No. 1 to Acquisition Agreement, dated February 28, 2011, between Richardson Electronics, Ltd., and Arrow Electronics, Inc. (incorporated by reference to Exhibit 10(q)(i) to the Company's Annual Report on Form 10-K for the fiscal year ended May 28, 2011).   |
| 10(p) †        | Employment, Nondisclosure and Non-compete Agreement between the Company and Lee A. McIntyre III dated June 15, 2015 (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the SEC on June 17, 2015).   |
| 10(q) †        | Employment, Nondisclosure and Non-Compete Agreement between the Company and Robert J. Ben dated as of August 4, 2015 (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the SEC on August 7, 2015).   |
| 14             | Corporate Code of Conduct (incorporated by reference to and Form 8-K filed on June 4, 2012).   |
| 21             | <u>Subsidiaries of the Company.</u>  |
| 23.1           | <u>Consent of Independent Registered Public Accounting Firm - BDO USA, LLP.</u>  |
| 23.1 (a)       | <u>Consent of Independent Registered Public Accounting Firm - Ernst &amp; Young LLP.</u>   |
| 31.1           | <u>Certification of Edward J. Richardson pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed pursuant to Part I).</u>   |
| 31.2           | <u>Certification of Robert J. Ben pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed pursuant to Part I).</u>  |
| 32             | <u>Certifications pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed pursuant to Part I).</u>  |
| 99.1           | <u>Press release, dated July 20, 2016.</u>   |
| 101            | The following financial information from our Annual Report on Form 10-K for the fourth quarter and fiscal year ended May 28, 2016, filed with the SEC on July 29, 2016, formatted in Extensible Business Reporting Language (XBRL): (i) the Audited Consolidated Balance Sheet as of May 28, 2016, (ii) the Audited Consolidated Statements of Income and Comprehensive Income (Loss) for the three months and 12 months ended May 28, 2016, (iii) the Audited Consolidated Statements of Cash Flows for the three and 12 months ended May 28, 2016, (iv) the Audited Consolidated Statement of Stockholder's Equity as of May 28, 2016, and (v) Notes to Audited Consolidated Financial Statements. |

† Executive Compensation Plan or Agreement



