SEVCON, INC.
Form 10-Q
August 12, 2016

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

FORM 10-Q

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

For the quarterly period ended July 2, 2016

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

For the transition period from ________________________________ to ________________________________

Commission File Number 1-9789

SEVCON, INC.
(Exact name of registrant as specified in its charter)

Delaware	04-2985631
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

155 Northboro Road, Southborough, Massachusetts 01772
(Address of principal executive offices and zip code)

(508) 281-5510
(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer	Accelerated filer	Non-accelerated filer (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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at August 12, 2016
Common stock, par value $.10	5,343,257

SEVCON, INC.
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PART I. FINANCIAL INFORMATION
Item 1 Financial Statements
CONSOLIDATED BALANCE SHEETS
Sevcon, Inc. and Subsidiaries
(in thousands of dollars except share and per share data)

	July 2, 2016 (unaudited)	September 30, 2015 (derived from audited statements)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 4,273	$ 8,048
Trade receivables, net of allowances for doubtful accounts of $200 at July 2, 2016 and $37 at September 30, 2015	10,995	8,995
Other receivables	1,230	467
Inventories	14,148	6,790
Deferred taxes	459	1,244
Prepaid expenses and other current assets	3,010	2,337
Total current assets	34,115	$ 27,881
Property, plant and equipment, at cost:		
Land and improvements	19	21
Buildings and improvements	613	693
Equipment	12,032	11,485
	12,664	12,199
Less: accumulated depreciation	(9,713)	(9,574)
Net property, plant and equipment	2,951	2,625
Long-term deferred tax assets	3,683	3,232
Intangible assets, net	10,372	-
Goodwill	8,604	1,435
Other long-term assets	497	443
Total assets	$ 60,222	$ 35,616
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Bank overdraft	$ 109	$ -
Accounts payable	8,699	6,184
Accrued expenses	3,689	1,973
Accrued and deferred taxes on income	65	-
Dividends payable	-	200
Debt to related parties	971	-
Total current liabilities	13,533	8,357
Long-term bank debt, net	15,216	-
Liability for pension benefits	10,527	10,963
Long-term deferred tax liabilities	1,794	500
Long-term debt to related parties	1,507	-
Total liabilities	$ 42,577	$ 19,820

Commitments and Contingencies (Note 16)

Stockholders' equity:		
Preferred stock, par value $.10 per share - authorized - 1,000,000 shares; Outstanding, 449,011 shares at July 2, 2016 and 452,124 at September 30, 2015	45	45
Common stock, par value $.10 per share - authorized 20,000,000; outstanding, 4,218,339 shares at July 2, 2016 and 3,694,872 at September 30, 2015	422	369
Premium paid in on common stock	11,711	6,637
Premium paid in on preferred stock	8,995	9,058
Retained earnings	7,480	10,607
Accumulated other comprehensive loss	(10,961)	(11,004)
Total Sevcon, Inc. and subsidiaries stockholders' equity	17,692	15,712
Non-controlling interest	(47)	84
Total stockholders' equity	17,645	15,796
Total liabilities and stockholders' equity	$ 60,222	$ 35,616

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

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CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
Sevcon, Inc. and Subsidiaries

	(in thousands of dollars except per share data)			
	Three months ended		Nine months ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Net sales	$ 13,913	$ 10,346	$ 36,209	$ 30,619
Cost of sales	(9,161)	(6,490)	(23,219)	(18,976)
Gross profit	4,752	3,856	12,990	11,643
Selling, general and administrative expenses	(4,463)	(2,551)	(10,568)	(7,630)
Research and development expenses	(1,212)	(1,044)	(3,419)	(2,796)
Acquisition costs	(8)	-	(1,425)	-
Operating (loss) income	(931)	261	(2,422)	1,217
Interest expense	(140)	(14)	(271)	(54)
Interest income	4	4	16	20
Foreign currency (loss) gain	(522)	(21)	(487)	258
Change in fair value of foreign exchange contracts	-	132	-	(68)
(Loss) income before income tax	(1,589)	362	(3,164)	1,373
Income tax benefit (provision)	60	(83)	139	(188)
Net (loss) income	(1,529)	279	(3,025)	1,185
Net loss attributable to non-controlling interests	84	2	131	31
Net (loss) income attributable to Sevcon, Inc. and subsidiaries	(1,445)	281	(2,894)	1,216
Preferred share dividends	(93)	(110)	(327)	(335)
Net (loss) income attributable to common stockholders	$ (1,538)	$ 171	$ (3,221)	$ 881
Net income per ordinary share – basic	$ (0.38)	$ 0.04	$ (0.84)	$ 0.25
Net income per ordinary share – diluted	$ (0.38)	$ 0.04	$ (0.84)	$ 0.25
Weighted average shares used in computation of earnings per share:				
Basic	4,070	3,486	3,828	3,459
Diluted	4,070	3,577	3,828	4,913

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(Unaudited)
Sevcon, Inc. and Subsidiaries

	(in thousands of dollars)			
	Three months ended		Nine months ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Net (loss) income attributable to Sevcon, Inc. and subsidiaries	$ (1,445)	$ 281	$ (2,894)	$ 1,216
Other comprehensive income (loss)				
Foreign currency translation adjustment	(71)	174	(160)	(262)
Defined benefit pension plans:				
Pension benefit plans adjustments during the period	128	66	277	198
Tax expense	(39)	(16)	(74)	(47)
Comprehensive (loss) income	$ (1,427)	$ 505	$ (2,851)	$ 1,105

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

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CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
Sevcon, Inc. and Subsidiaries

	(in thousands of dollars) Nine months ended	
	July 2, 2016	July 4, 2015
Cash flow from operating activities:		
Net (loss) income	$ (3,025)	$ 1,185
Adjustments to reconcile net (loss) income to net cash (used by) generated from operating activities:		
Depreciation	557	470
Amortization of intangible assets	732	-
Amortization of fair value uplift to assets arising on acquisition of subsidiary	257	-
Increase in bad debt provision	55	-
Unrealized loss on change in value of foreign exchange contracts	-	68
Stock-based compensation	527	406
Pension contributions greater than pension expense	(114)	(308)
Deferred tax provision	(139)	188
Increase (decrease) in cash resulting from changes in operating assets and liabilities:		
Trade receivables	912	(1,712)
Other receivables	(90)	(285)
Inventories	(4,141)	(517)
Prepaid expenses and other current assets	(1,930)	(321)
Accounts payable	(424)	836
Accrued expenses	(1,744)	159
Accrued and deferred taxes on income	926	(99)
Bank overdraft	109	-
Net cash (used by) generated from operating activities	(7,532)	70
Cash flow used by investing activities:		
Acquisition of property, plant and equipment	(1,043)	(1,088)
Acquisition of subsidiary, net of cash acquired	(9,255)	-
Net cash used by investing activities	(10,298)	(1,088)
Cash flow used by financing activities:		
Proceeds of long-term debt	15,448	500
Debt issuance costs	(232)	-
Repayments of long-term debt	(500)	(1,728)
Dividends paid	(434)	(263)
Purchase and retirement of common stock	(222)	(98)
Net cash generated from (used by) financing activities	14,060	(1,589)
Effect of exchange rate changes on cash	(5)	(83)
Net decrease in cash	(3,775)	(2,690)
Beginning balance - cash and cash equivalents	8,048	11,238
Ending balance - cash and cash equivalents	$ 4,273	$ 8,548
Supplemental disclosure of cash flow information:		
Cash paid for income taxes, net of refunds	197	86
Cash paid for interest	245	54
Conversion of preferred stock to common stock	$ 62	$ 169

Investment in subsidiary, net of cash acquired:

Cash consideration	10,832	-
Cash acquired	(1,577)	$ -
Net cash investment in subsidiary	$ 9,255	$ -
Issuance of common stock on acquisition of subsidiary	$ 4,760	$ -

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

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SEVCON, INC.

Notes to Consolidated Financial Statements – July 2, 2016

(Unaudited)

(1) Basis of presentation

Sevcon, Inc. (or the "Company") is a Delaware corporation organized on December 22, 1987 to carry on the electronic controls business previously performed by Tech/Ops, Inc. (Tech/Ops). Through wholly-owned subsidiaries located in the United States, England, France, South Korea and Japan and a 50% owned joint venture located in China, and through an international dealer network, the Company designs and sells, under the Sevcon name, motor controllers for zero emission electric and hybrid vehicles (EVs). The controls are used to vary the speed and movement of vehicles, to integrate specialized functions and to optimize the energy consumption of the vehicle's power source. Through a wholly-owned subsidiary in Italy acquired in January 2016, the Company also designs, manufactures and sells battery chargers for electric vehicles and power management and uninterrupted power source systems for industrial, medical and telecom applications, as well as electronic instrumentation for battery laboratories. Sevcon's customers are manufacturers of on and off-road vehicles, including cars, trucks, buses, motorcycles, fork lift trucks, aerial lifts, mining vehicles, airport tractors, sweepers and other electrically powered vehicles. Through another subsidiary located in the United Kingdom, Sevcon, Inc. manufactures special metalized film capacitors that are used as components in the power electronics, signaling and audio equipment markets.

Accounting for wholly-owned subsidiaries

The accompanying consolidated financial statements include the accounts of the Company's wholly-owned subsidiaries; Sevcon USA, Inc., Sevcon Ltd, Industrial Capacitors (Wrexham) Ltd., Sevcon Asia Limited, Sevcon Japan KK, Sevcon Security Corp., Sevcon S.r.l. and Bassi S.r.l., in accordance with the provisions required by the Consolidation Topic 810 of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC"). All material intercompany transactions have been eliminated.

Accounting for joint-venture subsidiary

For the Company's less than wholly owned joint venture subsidiary, Sevcon New Energy Technology (Hubei) Company Limited, the Company first analyzes whether this joint venture is a variable interest entity (a "VIE") in accordance with ASC 810 and if so, whether the Company is the primary beneficiary requiring consolidation. A VIE is an entity that has (i) insufficient equity to permit it to finance its activities without additional subordinated financial support or (ii) equity holders that lack the characteristics of a controlling financial interest. VIEs are consolidated by the primary beneficiary, which is the entity that has both the power to direct the activities that most significantly impact the entity's economic performance and the obligation to absorb losses or the right to receive benefits from the entity that potentially could be significant to the entity. Variable interests in a VIE are contractual, ownership, or other financial interests in a VIE that change with changes in the fair value of the VIE's net assets. The Company continuously re-assesses (i) whether the joint venture is a VIE, and (ii) if the Company is the primary beneficiary of the VIE. If it is determined that the joint venture qualifies as a VIE and the Company is the primary beneficiary, it is consolidated.

Based on the Company's analysis for this joint venture, the Company has determined that it is a VIE and that the Company is the primary beneficiary. While the Company owns 50% of the equity interest in the joint venture, the other 50% is owned by a local unrelated third party, and the joint venture agreement with that third party provides the Company with greater voting rights. Accordingly, the Company consolidates its joint venture under the VIE rules and reflects the third party's 50% interest in the consolidated financial statements as a non-controlling interest. The

Company records this non-controlling interest at its initial fair value, adjusting the basis prospectively for the third party's share of the respective consolidated investments' net income or loss or equity contributions and distributions. This non-controlling interest is not redeemable by the equity holders and is presented as part of permanent equity. Income and losses are allocated to the non-controlling interest holder based on its economic ownership percentage.

In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments (consisting of only normally recurring accruals) necessary to present fairly the financial position of Sevcon, Inc. as of July 2, 2016 and the results of operations and cash flows for the three and nine month periods ended July 2, 2016. These unaudited interim financial statements should be read in conjunction with the 2015 annual consolidated financial statements and related notes included in the 2015 Sevcon, Inc. Annual Report filed on Form 10-K (the "2015 consolidated financial statements and related notes included in the 2015 Sevcon, Inc. Annual Report filed on Form 10-K (the "2015 10-K"). Unless otherwise indicated, each reference to a year means the Company's fiscal year, which ends on September 30.

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The results of operations for the three and nine month periods ended July 2, 2016 are not necessarily indicative of the results to be expected for the full year.

(2) Summary of significant accounting policies

There have been no changes since the end of 2015 to the significant accounting policies followed by Sevcon, Inc.

(3) Acquisitions

Bassi Unipersonale S.r.l ("Bassi")

On January 26, 2016, the Company, and its wholly-owned indirect subsidiary, Sevcon S.r.l., ("Sevcon Italy") entered into a Quota Sale and Purchase Agreement with Bassi Holding S.r.l., ("Bassi Holding") an Italian limited liability company, and the quota owners of Bassi Holding, to acquire all the outstanding quotas of Bassi, a limited liability company located in Lugo, Italy. Bassi designs, manufactures and sells battery chargers for electric vehicles and power management and uninterrupted power source systems for industrial, medical and telecom applications, as well as electronic instrumentation for battery laboratories. The principal reasons for the acquisition were to enable the Company to expand its addressable share of the high-growth electrification market and enhance earnings by adding an immediately accretive business.

In order to fund the cash element of the acquisition price, on January 27, 2016, the Company also entered into a Term Loan Agreement providing for a credit facility with Banca Monte dei Paschi di Siena S.p.A. The acquisition was closed on January 29, 2016.

Purchase Price

The total purchase price was approximately $19.1 million and included (1) cash consideration of €10.0 million ($10.8 million) and (2) 500,000 shares of the Company's common stock ($4.8 million at the Company's Closing Date stock price of $9.52) and (3) the fair value of assumed dividends payable to the former owner of Bassi, Bassi Holding of €3.23 million ($3.5 million).

Sevcon Italy is required to distribute to the former owner of Bassi, Bassi Holding, outstanding dividends at fair value aggregating €3.23 million (approximately $3.5 million) in increments over a three-year period, post-closing.

During the nine months ended July 2, 2016, the Company incurred $1.4 million in costs and expenses related to the Company's acquisition of Bassi that are included in the consolidated statement of operations.

The Company accounted for the transaction using the acquisition method and, accordingly, the consideration has been allocated to the tangible and intangible assets acquired and liabilities assumed on the basis of their respective estimated fair values on the acquisition date. Goodwill resulting from this acquisition is largely attributable to the experienced workforce of Bassi and synergies expected to arise after the integration of Bassi's products and operations into those of the Company. Goodwill resulting from this acquisition is not deductible for tax purposes. Identifiable intangible assets acquired as part of the acquisition included definite-lived intangible assets for developed technologies, customer relationships, order backlog and trade names, which are being amortized using the straight-line method over their estimated useful lives, as well as goodwill.

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The fair value of the total consideration has been allocated based on the estimated fair values of assets acquired and liabilities assumed as follows (in thousands)

	(in thousands of dollars) January 29, 2016	
Consideration		
Cash		$ 10,832
Common stock (500,000 shares of Sevcon, Inc.)		4,760
Fair value of pre-acquisition dividends payable to Bassi Holding		3,503
Fair value of total consideration		$ 19,095
Recognized amounts of identifiable assets acquired and liabilities assumed:		
Cash	$ 1,577	
Accounts receivable	3,318	
Inventory	4,183	
Property and equipment	923	
Other assets	715	
Accounts payable	(3,513)	
Accrued and other current liabilities	(2,020)	
Deferred tax liabilities	(1,947)	
Other long-term liabilities	$ (1,360)	$ 1,876
Estimated fair value of identifiable intangible assets acquired:		
Developed technologies	325	
Customer relationships	8,774	
Trade name	758	
Order backlog	325	10,182
Fair value of total consideration, excluding goodwill		12,058
Goodwill		7,037
Fair value of total consideration		$ 19,095

The above fair value allocation is considered preliminary and is subject to revision during the measurement period. Management is in the process of completing its evaluation of acquired intangible assets. Additionally, the Company is continuing to validate the fair values of working capital including inventory and property and equipment.

The preliminary fair value of the assets acquired includes accounts receivable of $3,318,000. The gross amount due under contracts is $3,428,000 of which $110,000 is expected to be uncollectible.

Valuation of Intangible Assets Acquired

The following table sets forth the components of intangible assets acquired in connection with the Bassi acquisition (dollars in thousands):

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	Amount Assigned	Amortization Period (in years)
Definite-lived intangible assets:		
Developed technologies	$ 325	7.0
Customer relationships	8,774	10.0
Trade name	758	10.0
Order backlog	325	1.0
Total intangible assets acquired	$ 10,182	

Actual Results of Bassi Acquisition

Bassi's net revenues and operating income following the acquisition included in the Company's operating results for the nine months ended July 2, 2016 were $9.0 million and nil, respectively.

Pro Forma Summary

The unaudited consolidated pro forma results for the nine month periods ended July 2, 2016 and July 4, 2015 are set out in the table below. The pro forma consolidated results combine the results of operations of the Company and Bassi as though Bassi had been acquired on October 1, 2014 and include amortization charges for the acquired intangibles and interest expense related to the Company's borrowings to finance the acquisition. The 2016 pro forma results were adjusted to exclude $1,425,000 of acquisition costs to date related to Bassi and $257,000 of non-recurring expense relating to the fair value adjustments to acquisition date inventory and property and equipment. The pro forma financial information is presented for informational purposes only and is not necessarily indicative of the results of operations that would have been achieved if the acquisition had taken place on October 1, 2014.

	(in thousands of dollars) Nine months ended July 2, 2016	Nine months ended July 4, 2015
Revenue	$ 41,857	$ 42,228
Net income (loss)	$ (1,397)	$ 368

(4) Stock-based compensation plans

Under the Company's 1996 Equity Incentive Plan (the "Plan") there were 336,990 shares reserved and available for grant at July 2, 2016. There were 139,578 shares reserved and available for grant at September 30, 2015.

The Plan, which is shareholder-approved, permits the grant of Restricted Stock, Restricted Stock Units, Options and Stock Appreciation Rights ("SARs"). SARs may be awarded either separately, or in relation to options granted, and for the grant of bonus shares. The Company believes that such awards better align the interests of the employees with those of its shareholders. Options granted are exercisable at a price not less than fair market value on the date of grant. Recipients of grants of options must execute a standard form of non-competition agreement.

Share options

The Company estimated the fair values of its stock options using the Black-Scholes-Merton option-pricing model, which was developed for use in estimating the fair values of stock options. Option valuation models, including the

Black-Scholes-Merton option-pricing model, require the input of assumptions, including stock price volatility. Changes in the input assumptions can materially affect the fair value estimates and ultimately how much the Company recognizes as stock-based compensation expense. The fair values of the Company's stock options were estimated at the grant dates. The weighted average input assumptions used and resulting fair values of stock options were as follows for fiscal 2016:

Expected life (in years)	4.0
Risk-free interest rate	1.55 %
Volatility	61.43 %
Dividend yield	0.00 %
Weighted-average fair value per share	$4.81

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Expected Life

The expected term represents the period of time that options are expected to be outstanding. As the Company does not have sufficient historical evidence for determining the expected term of the stock option awards granted, the expected life assumption has been determined using the simplified method, which is an average of the contractual term of the option and its ordinary vesting period.

Risk-free Interest Rate

The Company bases the risk-free interest rate assumption on zero-coupon U.S. treasury instruments appropriate for the expected term of the stock option grants.

Expected Volatility

The expected stock price volatility for the Company's common stock is estimated based on the historic volatility of the Company's common stock for a period equivalent to the expected term of the stock option grants.

Expected Dividend Yield

The Company bases the expected dividend yield assumption on the fact that there is no present intention to pay cash dividends. Therefore an expected dividend yield of zero has been used.

Performance based awards

Stock options:

In December 2015, the Compensation Committee awarded performance-based equity compensation to nine executives and managers, including the principal executive officer and principal financial officer, consisting of 38,460 shares in the form of stock options. The performance options have an exercise price of $9.94 per share, representing the average of the highest intraday bid and ask quotes for the Company's common stock on the date of grant, December 16, 2015, and the preceding four trading days. The performance options will vest subject to the Company meeting an earnings per share target applicable to fiscal year 2018 set by the Compensation Committee so long as the employee is then employed by the Company. The estimated fair value of the stock on the date of the grant was $185,000 based on the fair market value of stock on the date of issue. The unvested compensation is being charged to income over three years. The charge to income for this employee stock option grant will be approximately $14,000 on a quarterly basis.

A summary of option activity under the employee share option plan as of July 2, 2016, and changes during the nine months then ended is presented below:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding as of September 30, 2015	-	$ -	-	$ -
Granted	38,460	$ 9.94	5.00	$ 11,153
Exercised	-	-	-	-
Forfeited or Expired	-	-	-	-
Outstanding at July 2, 2016	38,460	$ 9.94	4.46	$ nil
Exercisable	-	-	-	-
Vested and expected to vest	34,737	$ 9.94	4.46	$ nil

Restricted stock:

In December 2015, the Company granted 11,540 shares of restricted stock to four employees which will vest subject to the Company meeting the same earnings per share target applicable to fiscal year 2018, so long as the employee is then employed by the Company. The estimated fair value of the stock on the date of the grant was $116,000 based on the fair market value of stock on the date of issue. The unvested compensation is being charged to income over three years. The charge to income for this employee stock option grant was $8,000 and $18,000 for the three and nine months ended July 2, 2016 and will be approximately $8,000 on a quarterly basis.

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Management has assessed the performance criteria relating to these grants and concluded that they are likely to be met. Accordingly the relevant portion of the charge has been taken to income in the three and nine months ended July 2, 2016.

Time-based awards

Restricted stock:

In February 2016, the Company granted 29,700 shares of restricted stock to nine non-employee directors, which will vest on the day before the 2017 annual general meeting providing that the grantee remains a director of the Company, or as otherwise determined by the Compensation Committee. The aggregate fair value of the stock measured on the date of the grant was $292,000 based on the closing sale price of the stock on the date of grant. Subsequent to this, 3,300 of these granted shares of restricted stock were cancelled and returned to the Plan following the resignation of a director. Compensation expense is being charged to income on a straight line basis over the twelve month period during which the forfeiture conditions lapse. The charge to income for these restricted stock grants in the nine months to July 2, 2016 was $65,000 and the subsequent charge will be approximately $65,000 on a quarterly basis.

In February 2015, the Company granted 30,600 shares of restricted stock to nine non-employee directors, which vested on the day before the 2016 annual meeting. The aggregate fair value of the stock measured on the date of grant was $225,000, based on the closing sale price of the stock on the date of grant. Compensation expense was charged to income on a straight line basis over the twelve month requisite service period during which the forfeiture conditions lapsed. The charge to income for these restricted stock grants in 2015 was $131,000 and the charge in the nine months to July 2, 2016 was $94,000.

For the purposes of calculating average issued shares for basic earnings per share these shares are only considered to be outstanding when the forfeiture conditions lapse and the shares vest.

A summary of restricted stock and stock option activity, including both performance based awards and time-based awards, for the nine months ended July 2, 2016 is as follows:

	Number of shares of Restricted Stock	Weighted Average Grant-Date Fair Value
Non-vested balance as of September 30, 2014	168,600	$ 5.27
Granted	92,600	$ 7.49
Vested	(64,600)	$ 6.32
Non-vested balance as of September 30, 2015	196,600	$ 5.97
Granted	41,240	$ 9.89
Cancelled	(3,300)	$ 9.82
Vested	(91,600)	$ 6.72
Non-vested balance as of July 2, 2016	142,940	$ 6.53

	Number of shares of Stock Options	Weighted Average Grant-Date Fair Value
Non-vested balance as of September 30, 2015	-	$ -
Granted	38,460	$ 4.81
Vested	-	$ -
Non-vested balance as of July 2, 2016	38,460	$ 4.81

Stock-based compensation expense was $169,000 and $527,000 for the three and nine month periods ended July 2, 2016 and $147,000 and $406,000 for the three and nine months ended July 4, 2015 respectively. At July 2, 2016, there was $679,000 of unrecognized compensation expense related to restricted stock and stock options granted under the Plan. The Company expects to recognize that cost over a weighted average period of 1.9 years.

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(5) Cash dividends

Common stock dividends

The Company is not paying a dividend at the present time and the Board of Directors will consider whether to pay a common stock dividend in the future.

Preferred Stock dividends

At July 2, 2016 there were 449,011 shares of Series A Convertible Preferred Stock issued and outstanding. The preferred stock, which has a stated value of $24 per share, pays a 4% cumulative annual dividend semi-annually on October 15 and April 15 each year. A semi-annual dividend of $216,816 was paid on April 15, 2016. The next semi-annual dividend will be paid on October 15, 2016.

(6) Calculation of earnings per share and weighted average shares outstanding

Basic earnings per share is computed by dividing the net income or loss for the period by the weighted average number of shares of common stock outstanding during the period. The computation of diluted earnings per share is similar to the computation of basic earnings per share, except that the denominator is increased for the assumed exercise of dilutive options and other potentially dilutive securities, including convertible preferred stock, using the treasury stock method, unless the effect is anti-dilutive.

Basic and diluted net income per common share for the three and nine month periods ended July 2, 2016 and July 4, 2015 were calculated as follows:

	(in thousands of dollars except per share data)			
	Three months ended		Nine months ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Numerator:				
Net income (loss) attributable to common stockholders for computing net income (loss) per ordinary share – basic	$ (1,538)	$ 171	$ (3,221)	$ 881
Dividend eliminated upon assumed conversion of convertible preferred stock	-	-	-	335
Net income (loss) attributable to common stockholders for computing net income (loss) per ordinary share – diluted	$ (1,538)	$ 171	$ (3,221)	$ 1,216
Denominator:				
Weighted average shares used in calculating net income (loss) per ordinary share – basic	4,070	3,486	3,828	3,459
Adjustment for assumed conversion of convertible preferred stock	-	-	-	1,374
Adjustment for shares issuable upon vesting of restricted stock	-	91	-	80
Weighted average shares used in calculating net income (loss) per ordinary share – diluted	4,070	3,577	3,828	4,913
Net income (loss) per ordinary share – basic	$ (0.38)	$ 0.04	$ (0.84)	$ 0.25
Net income (loss) per ordinary share – diluted	$ (0.38)	$ 0.04	$ (0.84)	$ 0.25
No. of shares of convertible preferred stock that are anti-dilutive excluded from calculation of common stock equivalents	1,347	1,357	1,353	-

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(7) Segment information

The Company has three reportable segments: electronic controls, capacitors and battery chargers. The electronic controls segment produces microprocessor based control systems for zero emission and hybrid electric vehicles. The capacitor segment produces special-metalized film capacitors for sale to electronic equipment manufacturers. The battery chargers segment designs and manufactures battery chargers for electric vehicles. Each segment has its own management team and sales force and the capacitor and battery charger segments have their own manufacturing facilities.

The significant accounting policies of the segments are the same as those described above and in Note 1 to the Notes to Consolidated Financial Statements in the 2015 10-K. Inter-segment revenues are accounted for at current market prices. The Company evaluates the performance of each segment principally based on operating income. The Company does not allocate income taxes, interest income and expense or foreign currency translation gains and losses to segments. Information concerning operations of these businesses is as follows:

(in thousands of dollars)

	Three months ended July 2, 2016				
	Controls	Capacitors	Chargers	Corporate	Total
Sales to external customers	8,462	405	5,046	-	13,913
Inter-segment revenues	-	-	-	-	-
Operating income (loss)	(511)	(5)	(257)	(158)	(931)
Identifiable assets, excluding goodwill	38,149	901	8,715	3,853	51,618
Goodwill	1,435	-	7,169	-	8,604

	Three months ended July 4, 2015				
	Controls	Capacitors	Chargers	Corporate	Total
Sales to external customers	9,820	526	-	-	10,346
Inter-segment revenues	-	-	-	-	-
Operating income	342	5	-	(86)	261
Identifiable assets, excluding goodwill	24,033	1,248	-	7,150	32,431
Goodwill	1,435	-	-	-	1,435

	Nine months ended July 2, 2016				
	Controls	Capacitors	Chargers	Corporate	Total
Sales to external customers	25,968	1,215	9,026	-	36,209
Inter-segment revenues	-	-	-	-	-
Operating income (loss)	(449)	(61)	9	(1,921)	(2,422)
Identifiable assets, excluding goodwill	38,149	901	8,715	3,853	51,618
Goodwill	1,435	-	7,169	-	8,604

	Nine months ended July 4, 2015				
	Controls	Capacitors	Chargers	Corporate	Total
Sales to external customers	29,000	1,619	-	-	30,619
Inter-segment revenues	-	3	-	-	3
Operating income	1,064	121	-	32	1,217
Identifiable assets, excluding goodwill	24,033	1,248	-	7,150	32,431
Goodwill	1,435	-	-	-	1,435

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In the electronic controls segment, revenues derive from the following products and services:

(in thousands of dollars)

	Three Months ended		Nine Months ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Electronic controls for zero emission and hybrid electric vehicles	$ 5,638	$ 7,445	$ 17,876	$ 19,746
Accessory and aftermarket products and services	2,824	2,375	8,092	9,254
Total controls segment revenues	$ 8,462	$ 9,820	$ 25,968	$ 29,000

(8) Research and development

The cost of research and development programs is charged against income as incurred and was as follows:

In recent years the Company has received several awards of research and development grants by public bodies established by the U.K. government to stimulate technology-enabled innovation.

In 2011, the Company was awarded a research and development grant by the Technology Strategy Board to lead a collaborative project with Cummins Generator Technologies and Newcastle University in the U.K. to develop an innovative electric drive system for electric vehicles using advanced switched reluctance motor technology. The Company recorded grant income from this Technology Strategy Board project of $Nil in the nine month period ended July 2, 2016, associated with research and development expense of $7,000 in the period. The Company recorded grant income of $56,000 in the nine month period ended July 4, 2015, associated with research and development expense of $245,000 in the same period.

In 2015 the Company was awarded a grant of approximately $625,000 by the U.K. Regional Growth Fund, a U.K. government body. The grant is to develop an innovative range of low voltage motor controls which are designed to serve the emerging needs for on-road, automotive electrification. The grant includes a commitment to create or safeguard a total of twenty jobs at the Company's U.K. facility over the period of the project. The Company recorded grant income from this project of $115,000 in the nine month period ended July 2, 2016 associated with research and development expense of $392,000 in the period. The Company recorded grant income of $27,000 in the nine month period ended July 4, 2015, associated with research and development expense of $149,000 in the same period.

The grant income in the first nine months of 2016 and 2015 was recorded as a reduction of research and development expense.

In the three and nine month periods ended July 2, 2016, the Company recorded refundable tax credits of $315,000 related to certain research and development incentives in the U.K. These amounts have been recorded in operating income, as they are refunded without regard to actual tax liability.

(9) Income Taxes

The Company's effective tax rate of 4% is significantly lower than the U.S. statutory rate of 34%, primarily due to the fact that certain current year operating losses in the U.K. have been foregone in exchange for a cash refund. As mentioned in Note 8, this benefit is recorded in operating income, as such amounts are refundable without regard to actual tax liability.

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(10) Employee benefit plans

Sevcon, Inc. has defined contribution plans covering the majority of its U.S. and U.K. employees in the controls business. There is also a small defined contribution plan covering senior managers in the capacitor business.

The Company’s French subsidiary, Sevcon S.A.S., has a liability to pay its employees a service and salary based award when they reach retirement age and leave the Company’s employment. This liability, which is unfunded, is recognized in accrued expenses and was $161,000 and $152,000 at July 2, 2016 and July 4, 2015, respectively. The obligation to pay this award is a French legal requirement and is only payable if the employee is employed by the Company when they retire; if they leave the Company prior to that time the award is no longer payable.

The Company’s Italian subsidiary, Bassi S.r.l., has a liability to pay its employees a severance indemnity, ‘Trattamento di fine Rapporto’ (“TFR”) when they leave the Company’s employment. TFR, which is mandatory for Italian companies, is deferred compensation and is based on the employees’ years of service and the compensation earned by the employee during the service period. TFR is considered a “Defined Benefit Plan” and the related liability is recognized in the consolidated balance sheet within “Liability for pension benefits”. This liability, which is unfunded, was $1,245,000 at July 2, 2016.

The Company has frozen the U.K. and U.S. defined benefit plans for which no future benefits are being earned by employees. The Company uses a September 30 measurement date for its defined benefit pension plans.

	(in thousands of dollars)			
	Three Months ended		Nine Months ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Interest cost	$304	$308	$ 885	$ 928
Service cost	49	-	82	-
Expected return on plan assets	(281)	(311)	(846)	(937)
Amortization of net loss	128	66	278	198
Net periodic benefit cost	200	63	399	189
Net cost of defined contribution plans	$105	$87	$ 388	$ 359
Net cost of all employee benefit plans	$305	$150	$ 787	$ 548

The following table sets forth the movement in the liability for pension benefits in the nine month periods ended July 2, 2016 and July 4, 2015, respectively:

	(in thousands of dollars)	
	Nine Months ended	
	July 2, 2016	July 4, 2015
Liability for pension benefits at beginning of period	10,963	9,529
Liability assumed on acquisition of subsidiary	1,167	-
Interest cost	885	928
Service cost	82	-
Expected return on plan assets	(846)	(937)
Plan withdrawals	(36)	-
Plan contributions	(477)	(497)
Effect of exchange rate changes	(1,211)	(349)

Balance at end of period	10,527	8,674

Amounts recognized in the balance sheet consist of:

	(in thousands of dollars)	
	July 2, 2016	July 4, 2015
Non-current liabilities	$ 10,527	$ 8,674

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Amounts recognized in accumulated other comprehensive loss consist of:

	(in thousands of dollars)			
	Three Months ended		Nine Months ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Actuarial loss, net of $39 and $74 tax benefit for the three and nine month periods, respectively, (2015: net of $16 and $47 tax benefit for the three and nine month periods, respectively)	$ 89	$ 50	$ 203	$ 151

Sevcon, Inc. contributed $150,000 to its frozen U.S. defined benefit plan in the nine months ended July 2, 2016; it presently anticipates contributing a further $50,000 to fund its U.S. plan in the remainder of fiscal 2016. In addition, employer contributions to the frozen U.K. defined benefit plan were $327,000 in the first nine months and are estimated to total $426,000 in 2016.

The table below presents information about the Company's pension plan assets measured and recorded at fair value as of July 2, 2016 and indicates the fair value hierarchy of the inputs utilized by the Company to determine the fair values.

	(in thousands of dollars)		
July 2, 2016	Level 1* (Quoted prices in active markets)	Level 2** (Significant observable inputs)	Level 3*** (Unobservable inputs)
Adept Strategy 9 Fund (a sub-fund of Adept Investment Management plc)	-	12,011	-
Schroder Matching Plus Nominal and Index Linked Liability Driven Investment Swap Funds (funds managed by Schroder Investment Management Limited)	-	4,869	-
U.S. Mutual Funds and Fixed Income Funds	1,176	-	-
U.S. Equity Funds	1,970	-	-
Other Types of Investments			
Cash	1,159	-	-
Total	4,305	16,880	-

	(in thousands of dollars)		
September 30, 2015	Level 1* (Quoted prices in active markets)	Level 2** (Significant observable inputs)	Level 3*** (Unobservable inputs)
Adept Strategy 9 Fund (a sub-fund of Adept Investment Management plc)	-	13,044	-
	-	3,845	-

Schroder Matching Plus Nominal and Index Linked Liability Driven Investment Swap Funds (funds managed by Schroder Investment Management Limited)			
U.S. Mutual Funds and Fixed Income Funds	2,557	-	-
U.S. Equity Funds	350	-	-
Other Types of Investments			
Cash	331	-	-
Total	3,238	16,889	-

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* Level 1 investments represent mutual funds for which a quoted market price is available on an active market. These investments primarily hold stocks or bonds, or a combination of stocks and bonds.

** Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. The Company's pension plan financial assets held in the Adept Strategy 9 Fund and the Schroder investments are Level 2 assets. The Company uses the Net Asset Value to determine the fair value of underlying investments which (a) do not have readily determinable fair value; and (b) prepare their financial statements consistent with the measurement principles of an investment company. The Funds are not exchange traded. The Funds are not subject to any redemption notice periods or restrictions and can be redeemed on a daily basis. No gates or holdbacks or dealing suspensions are being applied to the Funds. The Funds are of perpetual duration.

*** The Company currently does not have any Level 3 pension plan financial assets.

The following estimated benefit payments have been, or are expected, to be paid:

	(in thousands of dollars)
2016	$ 426