ANNUAL REPORT

FOR THE FISCAL YEAR ENDED
DECEMBER 31, 2015

PARAGON TECHNOLOGIES, INC.

101 Larry Holmes Drive, Suite 500
Easton, PA 18042
Telephone: 610-252-3205
Fax: 610-252-3102

I.R.S. Employer Identification No.	CUSIP No.
22-1643428	69912T108

ISSUER'S EQUITY SECURITIES

COMMON STOCK

$1.00 Par Value

20,000,000 Common Shares Authorized

1,684,745 Shares Issued and Outstanding
as of the Filing of this Annual Report

1) Name of the Issuer and its predecessors (if any):

The name of the issuer is Paragon Technologies, Inc. The issuer was formerly known as SI Handling Systems, Inc. until April 5, 2000.

2) Address of the Issuer's principal executive offices:

Company Headquarters
Paragon Technologies, Inc.
101 Larry Holmes Drive, Suite 500
Easton, PA 18042
Phone: (610) 252-3205
E-Mail: info@pgntgroup.com
Website(s): www.pgntgroup.com

IR Contact
Paragon Technologies, Inc.
101 Larry Holmes Drive, Suite 500
Easton, PA 18042
Phone: (706) 549-7141
E-Mail: ir@pgntgroup.com
Website(s): www.pgntgroup.com

3) Security Information:

Trading Symbol: PGNT
Exact title and class of securities outstanding: Common Stock
CUSIP: 69912T108
Par Value: $1.00 per share
Total shares authorized: 20,000,000
Total shares outstanding: 1,684,745

Transfer Agent
American Stock Transfer & Trust Company
6201 15th Avenue
Brooklyn, NY 11219
Phone: (718) 921-8206
Is the Transfer Agent registered under the Exchange Act: Yes: ☑ No: ☐

List any restrictions on the transfer of security:
None

Describe any trading suspension orders issued by the SEC in the past 12 months:
None

List any stock split, stock dividend, recapitalization, merger, acquisition, spin-off, or reorganization either currently anticipated or that occurred within the past 12 months.
None

4) Issuance History:

Not Applicable.

5) Financial Statements:

The financial statements for the fiscal year ended December 31, 2015 are incorporated by reference and can be found at the end of this Annual Report. The financial statements as of and for the fiscal year ended December 31, 2015 include: (1) consolidated balance sheets, (2) consolidated statements of operations, (3) consolidated statements of comprehensive income (loss), (4) consolidated statements of stockholders' equity, (5) consolidated statements of cash flows, (6) notes to consolidated financial statements, and (7) the independent auditors report.

6) Describe the Issuer's Business, Products, and Services:

Describe the issuer's business so a potential investor can clearly understand the company. In answering this item, please include the following:

A. Description of the issuer's business operations:

Business

Paragon Technologies, Inc. ("Paragon" or the "Company"), based out of Easton, Pennsylvania, provides a variety of material handling solutions, including systems, technologies, products, and services for material flow applications through its wholly owned subsidiary, SI Systems, LLC ("SI Systems"). SI Systems' capabilities include horizontal conveyance and transportation, rapid dispensing for order fulfillment, a full suite of high performance Warehouse Execution Systems (WES), Warehouse Management Systems (WMS) and Warehouse Control Systems (WCS) software systems and aftermarket services.

SI Systems' automated material handling systems are used by manufacturing, assembly, order fulfillment, and distribution operations customers located primarily in North America, including the U.S. government. SI Systems' branded products are utilized to automate the movement or selection of products and are often integrated with other automated equipment such as pick to light devices, conveyors and robots. SI Systems is brought to market as two individual brands, SI Systems' Order Fulfillment Systems (hereafter referred to as "SI Systems OFS") and SI Systems' Production & Assembly Systems (hereafter referred to as "SI Systems PAS").

The OFS business focuses on providing order fulfillment systems to distribution operations, including Dispen-SI-matic®, Mobile-matic® (a patented product) and our full suite of Warehouse Execution Systems, Warehouse Management Systems and Warehouse Control Systems software solutions with our VWare™ product. These systems are sold primarily through a nationwide network of authorized material handling integrators, dealers and direct to major OEM accounts.

The PAS business focuses on providing automated material handling systems to manufacturing, assembly and distribution operations via our Lo-Tow® horizontal conveyance and transportation technologies. These systems are sold primarily to end users.

6) Describe the Issuer's Business, Products, and Services: *(Continued)*

<u>Business</u> *(Continued)*

SI Systems' automated material handling systems are marketed, designed, sold, installed, and serviced by its own staff or subcontractors as labor-saving devices to improve productivity, quality, and reduce costs. SI Systems' integrated material handling solutions involve both standard and specially designed components and include integration of non-proprietary automated handling technologies to provide turnkey solutions for its customers' unique material handling needs. SI Systems' engineering staff develops and designs computer control programs required for the efficient operation of the systems and for optimizing manufacturing, assembly, and fulfillment operations.

SI Systems' business is largely dependent upon a limited number of large contracts with a limited number of customers. This dependence can cause unexpected fluctuations in sales volume. Various external factors affect the customers' decision-making process on expanding or upgrading their current production or distribution sites. Customer's timing and placement of new orders is often affected by factors such as the current economy, current interest rates, and future expectations. SI Systems believes that its business is not subject to seasonality, although the rate of new orders can vary substantially from month to month. Since the Company recognizes sales on a percentage of completion basis for its systems contracts, fluctuations in SI Systems' sales and earnings occur with increases or decreases in major installations.

Paragon also invests in businesses and securities under the Investment Management Policy. The Investment Management Policy sets forth the parameters under which a portion of Paragon's cash balance may be invested in marketable securities, including U.S. Treasuries, equities of publicly traded companies, bonds, money market instruments and other securities. Investment decisions under the Investment Management Policy are made by Hesham Gad, Chairman and Chief Executive Officer. The Investment Management Policy sets forth restrictions on the investment of Paragon's funds, including an aggregate limit on Paragon's cash balance that is made available for investment, limits on the amount that may be invested in any single equity or fixed income position or certain categories of securities, prohibition of short-selling, margin trading and the use of leverage, requirements for the management of the investment account, and other Board-approval requirements.

B. Date and State (or Jurisdiction) of Incorporation:

The Company was originally incorporated in Pennsylvania on June 18, 1958 as SI Handling Systems, Inc.

On April 5, 2000, SI Handling Systems, Inc. changed its name to Paragon Technologies, Inc.

The Company changed its state of incorporation from Pennsylvania to Delaware on November 21, 2001.

C. The issuer's primary and secondary SIC Codes:

Primary SIC Code:	3530
Secondary SIC Code:	N/A

D. The issuer's fiscal year end date:

The Company's fiscal year end is December 31.

6) Describe the Issuer's Business, Products, and Services: *(Continued)*

E. Principal products or services, and their markets:

SI Systems' Branded Products

SI Systems' branded products encompass the horizontal conveyance and transport and order fulfillment families of products.

Horizontal Conveyance and Transport

Lo-Tow®. Lo-Tow® is an in-floor towline conveyor system. These conveyor systems are utilized in the automation of manufacturing, assembly and unit load handling in distribution environments. Industries served include the automotive, recreational and utility vehicle, distribution centers, radiation chambers, engine assembly, truck assembly, construction vehicles, newspaper facilities, farm machinery, and the U.S. government, primarily the United States Postal Service and the Defense Logistics Agency. This simple, yet reliable component design allows for a variety of configurations well suited for numerous applications. It provides reliable and efficient transportation for unit loads of all types in progressive assembly or distribution applications. Because SI Systems' Lo-Tow® tow chain used with the system operates at a minimal depth, systems can be installed in existing one-story and multi-story buildings as well as newly constructed facilities. Controls sophistication varies depending upon the application. More complex systems include programmable logic controllers ("PLCs"), personal computers for data collection and operator interface, radio frequency identification and communication, bar code identification, and customer host computer communication interface. The Company believes that SI Systems is the largest supplier of in-floor towline systems in the United States.

Order Fulfillment Systems

Dispen-SI-matic®, Mobile-matic™, Doc-U-spense™, VWare™
Dispen-SI-matic® and VWare™ offer ideal solutions for increasing efficiencies, labor-intensive processes, and long-time deliveries where a high volume of orders must be fulfilled in a time sensitive nature. Industries served include e-commerce and omni-channel retailers, pharmaceutical, entertainment, vision, nutritional supplements, electronics, health and beauty aids, cosmetics, jewelry and an assortment of other various industries.

SI Systems' branded products include a variety of Dispen-SI-matic® models for automated order fulfillment where volume, speed, accuracy, and efficiency are of the essence. The Pick-to-Belt, Pick-to-Tote and Pick-to-Bucket are solutions that provide ultra-high throughput for split case order fulfillment. Additionally, the Dispen-SI-matic® monitors the dispensing of packages into totes or cartons thus achieving a high degree of accuracy and efficiency in order fulfillment.

Mobile-Matic™ was introduced to the market in the fourth quarter of 2010 to target a wider base of potential customers. Mobile-Matic™, a mobile version of the Dispen-SI-matic® with fewer channels, is scalable and automatically dispenses product directly into cartons or totes being transported on an adjacent conveyor or directly onto an adjacent conveyor to feed downstream operations.

Doc-U-spense™ is a new product introduced in 2016 based on Mobile-Matic technology. The Doc-U-spense system is a very economical and intelligent document inserter system. Designed primarily for distribution centers, the automated system allows order fulfillment operations to place a large number of flyers, coupons, instructions and other documents into open orders without the labor and associate costs.

6) Describe the Issuer's Business, Products, and Services: *(Continued)*

Order Fulfillment Systems *(Continued)*

Our Warehouse suite of software (**VWare**™) is founded on industry standard Microsoft technologies. The modular architecture utilizes the latest object-oriented design techniques and methodologies to ensure the best possible reliability and maintainability. Our scalable product line deploys on a Windows based system utilizing client-server technology capable of enterprise-level inventory control and order fulfillment applications. We have designed our runtime environment around the most popular platform utilized today for scalable information systems. Microsoft Windows workstations utilize Open Database Connectivity (ODBC) to interact with a Microsoft SQL Server database. The baseline system is hosted on a Windows server. The VWare™ family of warehouse control applications work in concert on client workstations to collectively create a scalable distributed processing system capable of managing a wide variety of concurrent tasks. Selective tasks have been designed to take advantage of Microsoft Windows native connectivity capabilities to import order fulfillment and warehouse maintenance demands, while interfacing and exporting vital data to external systems.

Aftermarket Spare Parts, Equipment and Support Service

SI Systems provides spare and replacement parts and equipment for all of its products, along with support contract services for its order fulfillment systems.

7) Describe the Issuer's Facilities:

Paragon Technologies, Inc.
101 Larry Holmes Drive, Suite 500
Easton, PA 18042

On December 30, 2013, the Company entered into a lease agreement for the address noted above for an initial term of two years, followed by an option to renew for two consecutive /additional terms of two years each. The lease commenced on April 15, 2014. Based on prior agreement with the new lessor, the Company started occupying the new space effective February 17, 2014. The area of the new lease is 9,648 square feet in Easton, Pennsylvania. The leasing agreement requires fixed monthly payments of $12,750.

On September 3, 2015, the lease was renewed to extend the term of the lease for a period of two years beginning February 17, 2016. The leasing agreement requires fixed monthly payments of $13,000 in year one and $13,500 in year two.

The Company believes that its Easton, Pennsylvania facility is adequate for its current operations. The Company's operations experience fluctuations in workload due to the timing and receipt of new orders and customer job completion requirements. Currently, the Company's facility is adequate to handle these fluctuations. In the event of an unusual demand in workload, the Company supplements its internal operations with outside subcontractors that perform services for the Company in order to complete contractual requirements for its customers. The Company will continue to utilize internal personnel and its own facility and, when necessary and/or cost effective, outside subcontractors to complete contracts in a timely fashion in order to address the needs of its customers.

8) Officers, Directors, and Control Persons:

A. <u>Names of Officers, Directors, and Control Persons</u>.

Information concerning The Company's directors is as follows:

Name, Other Positions or Offices With the Company and Principal Occupation for Past Five Years	Director Since	Age
Hesham M. Gad..	2010	38

Hesham M. Gad has been Chief Executive Officer of the Company since June 2014, Chairman of the Company's Board of Directors since March 2012 and a director of the Company since October 2010. Mr. Gad is also the Chairman and CEO of SED International Holdings, Inc. (OTC: SEDN). Paragon is the largest shareholder in SED.

Mr. Gad is also the author of the internationally published book, "The Business of Value Investing." Mr. Gad holds a B.A. in finance and an MBA in finance from the University of Georgia.

Jack H. Jacobs	2012	70

Jack H. Jacobs has been a principal of The Fitzroy Group, Ltd., a firm that specializes in the development of residential real estate in London and invests both for its own account and in joint ventures with other institutions, for the past six years. He has held the McDermott Chair of Politics at West Point since 2005 and has served as an NBC military analyst since 2002. Mr. Jacobs was a co-founder and Chief Operating Officer of AutoFinance Group Inc., one of the firms to pioneer the securitization of debt instruments, from 1988 to 1989; the firm was subsequently sold to KeyBank. He was a Managing Director of Bankers Trust Corporation, a diversified financial institution and investment bank, where he ran foreign exchange options worldwide and was a partner in the institutional hedge fund business.

Mr. Jacobs' military career included two tours of duty in Vietnam where he was among the most highly decorated soldiers, earning three Bronze Stars, two Silver Stars and the Medal of Honor, the nation's highest combat decoration. He retired from active military duty as a Colonel in 1987. From 2007 to 2012, Mr. Jacobs served as a member of the Board of Directors of Xedar Corporation, a public company; from June 2006 to 2009, he was a director of Visual Management Systems, a private company; and he was a director of BioNeutral Group, Inc., a public company, until 2009. Mr. Jacobs was previously a director of Premier Exhibitions, Inc. (NASDAQ: PRXI), a public company. Mr. Jacobs is Vice Chairman of the Medal of Honor Foundation and a member of the Board of Trustees of the USO of New York. Mr. Jacobs is the author of the book "If Not Now, When?: Duty and Sacrifice in America's Time of Need." Mr. Jacobs received a Bachelor of Arts and a Master's degree from Rutgers University

Name, Other Positions or Offices With the Company and Principal Occupation for Past Five Years	Director Since	Age
Samuel S. Weiser	2012	56

Samuel S. Weiser is currently the President and Chief Executive Officer of Foxdale Management LLC. From August 2009 until April 2015, he was a member of the Board of Directors and from August 2014 until March 2015 was Executive Chairman of Premier Exhibitions, Inc. (NASDAQ: PRXI), a provider of museum quality touring exhibitions. In addition, Mr. Weiser served as President and Chief Executive Officer of Premier Exhibitions from November 2011 until June 2014. Mr. Weiser was a member of SED International's Board of Directors from October of 2013 until October 2014. Previously, Mr. Weiser served as a member and Chief Operating Officer of Sellers Capital LLC, an investment management firm, from 2007 to 2010. From 2005 to 2007, he was a Managing Director responsible for the Hedge Fund Consulting Group within Citigroup Inc.'s Global Prime Brokerage Division. From 2002 to April 2005, he was the President and Chief Executive Officer of Foxdale Management, LLC, a consulting firm founded by Mr. Weiser that provided operational consulting to hedge funds and litigation support services in hedge fund related securities disputes. Mr. Weiser also served as Chairman of the Managed Funds Association, a lobbying organization for the hedge fund industry, from 2001 to 2003 and was formerly a partner in Ernst and Young. He received his B.A. in Economics from Colby College and a M.A. in Accounting from George Washington University.

The directors of the Company hold their positions as directors until the next Annual Meeting of Stockholders.

The names, ages, and offices with the Company of its executive officers are as follows:

Name	Age	Office
Hesham M. Gad	38	Chief Executive Officer, Paragon Technologies
Deborah R. Mertz	59	Chief Financial Officer, Paragon Technologies/ SI Systems, LLC.
John C. Molloy	64	President and Chief Executive Officer, SI Systems, LLC.

John C. Molloy has over 30 years of financial and executive management experience, including acquisitions, divestitures, reorganizations, strategic planning, software systems and change management. From 2010 to 2014, John was the Founder and CEO of Sapient Automation, an established material handling company that focuses on carousel and vertical lift market applications. From 2002 to 2009, Mr. Molloy was White Systems' President/COO and CFO from 1997 to 2002. In 2005, he led a management buyout of White Systems from F.K.I. (the second largest material handling company worldwide) along with a private equity group and from 2005 to 2009, Mr. Molloy was part owner of White Systems. From 1991 to 1996, Mr. Molloy served as VP/Corporate Controller of Lab-Volt Systems, Inc., a global leader in the design and manufacture of hands-on training laboratories for public education, industry and the military. John is a graduate of Fairleigh Dickinson University with a B.S. in Accounting. He also completed graduate work at Fordham University with a concentration in Finance and a three month Executive Management program at Stanford University.

Deborah R. Mertz, is an accounting professional with over 30 years experience in both publicly held and privately held companies. From 2006 to 2013, Ms. Mertz held the position of Assistant Controller of ASSA ABLOY Inc. Americas Division. ASSA ABLOY is the largest global supplier of intelligent lock and security solutions. From 1999 to 2006, Ms. Mertz was the Controller/CFO of Sargent Manufacturing Company. Sargent Manufacturing Company is a wholly owned subsidiary of ASSA ABLOY Inc. and manufactures architectural hardware used primarily in commercial construction. Ms. Mertz has held various other senior accounting positions. Ms. Mertz is a CPA and has an MBA from Rider University and a B.S. in Accounting from King's College.

B. Legal/Disciplinary History. Please identify whether any of the foregoing persons have, in the last five years, been the subject of:

1. A conviction in a criminal proceeding or named as a defendant in a pending criminal proceeding (excluding traffic violations and other minor offenses).

   Except as set forth below, the executive officers and directors of the Company have not, in the last five years, been the subject of a conviction in a criminal proceeding or named as a defendant in a pending criminal proceeding (excluding traffic violations and other minor offenses).

   On June 9, 2011, Mr. Gad was charged in the Superior Court of Athens-Clarke County, Georgia with making a false statement relating to the allegation that Mr. Gad checked the incorrect box on his driver's license application completed on March 27, 2007 as to whether Mr. Gad is a U.S. citizen. On October 19, 2011, Mr. Gad pled not guilty to this charge. This charge is subject to an Order Permitting Pretrial Diversion, pursuant to which the charge will be dismissed upon Mr. Gad's successful completion of the requirements under a Pretrial Diversion Agreement in effect between April 1, 2014 and March 31, 2016.

2. The entry of an order, judgment, or decree, not subsequently reversed, suspended or vacated, by a court of competent jurisdiction that permanently or temporarily enjoined, barred, suspended, or otherwise limited such person's involvement in any type of business, securities, commodities, or banking activities.

   The executive officers and directors of the Company have not, in the last five years, been the subject of the entry of an order, judgment, or decree, not subsequently reversed, suspended or vacated, by a court of competent jurisdiction that permanently or temporarily enjoined, barred, suspended or otherwise limited such person's involvement in any type of business, securities, commodities, or banking activities.

3. A finding or judgment by a court of competent jurisdiction (in a civil action), the Securities and Exchange Commission, the Commodity Futures Trading Commission, or a state securities regulator of a violation of federal or state securities or commodities law, which finding or judgment has not been reversed, suspended, or vacated.

   The executive officers and directors of the Company have not, in the last five years, been the subject of a finding or judgment by a court of competent jurisdiction (in a civil action), the Securities and Exchange Commission, the Commodity Futures Trading Commission, or a state securities regulator of a violation of federal or state securities or commodities law, which finding or judgment has not been reversed, suspended, or vacated.

4. The entry of an order by a self-regulatory organization that permanently or temporarily barred, suspended or otherwise limited such person's involvement in any type of business or securities activities.

   The executive officers and directors of the Company have not, in the last five years, been the subject of the entry of an order by a self-regulatory organization that permanently or temporarily barred, suspended or otherwise limited such person's involvement in any type of business or securities activities.

C. <u>Beneficial Shareholders</u>. Provide a list of the name, address and shareholdings or the percentage of shares owned by all persons beneficially owning more than ten percent (10%) of any class of the issuer's equity securities. If any of the beneficial shareholders are corporate shareholders, provide the name and address of the person(s) owning or controlling such corporate shareholders and the resident agents of the corporate shareholders.

<u>Security Ownership of Certain Beneficial Owners and Management</u>

To the best of the Company's knowledge, the following table sets forth certain information as of December 31, 2015 (unless otherwise noted) regarding the ownership of common stock by each person known by the Company to be the beneficial owner of more than ten percent (10%) of the outstanding common stock. Unless otherwise stated, the beneficial owners exercise sole voting and/or investment power over their shares.

Title of Class	Name and Address of Beneficial Owner (1)	Amount and Nature of Beneficial Ownership	Right to Acquire Under Options Exercisable Within 60 Days	Percent of Class (2)
Common Stock, Par Value $1.00 Per Share	Hesham M. Gad (3)	477,953	-	28.4%

(1) The address for the stockholder listed on the table is c/o Paragon Technologies, Inc., 101 Larry Holmes Drive, Suite 500, Easton, Pennsylvania 18042.
(2) The percentage for each individual, entity or group is based on the aggregate number of shares outstanding as of 12/31/2015.
(3) Mr. Gad holds 273,422 shares directly and beneficially owns 204,531 shares held by Gad Capital.

9) Third Party Providers:

Please provide the name, address, telephone number, and e-mail address of each of the following outside providers that advise your company on matters relating to operations, business development, and disclosure:

<u>Legal Counsel</u>:

Thompson Hine LLP
Attention: Derek D. Bork
3900 Key Center
127 Public Square
Cleveland, Ohio 44114-1291
Telephone number: (216) 566-5500
E-mail address: Derek.Bork@thompsonhine.com

Auditor:

RSM US LLP
Attention: Susan Roeder
751 Arbor Way, Suite 200
Blue Bell, PA 19422
Telephone number: (215) 641-8600
E-mail address: Susan.Roeder@rsmus.com

Investor Relations Consultant:

None.

Other Advisor:

None.

10) Issuer Certification:

The issuer shall include certifications by the chief executive officer and chief financial officer of the issuer (or any other persons with different titles, but having the same responsibilities).

I, Hesham M. Gad, President and Chief Executive Officer, certify that:

1. I have reviewed this annual disclosure statement of Paragon Technologies, Inc.;

2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and

3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations, and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

March 31, 2016

/s/ Hesham M. Gad
Hesham M. Gad
President and Chief Executive Officer

The issuer shall include certifications by the chief executive officer and chief financial officer of the issuer (or any other persons with different titles, but having the same responsibilities).

I, Deborah R. Mertz, Chief Financial Officer, certify that:

1. I have reviewed this annual disclosure statement of Paragon Technologies, Inc.;

2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and

3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations, and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

March 31, 2016

/s/ Deborah R. Mertz
Deborah R. Mertz
Chief Financial Officer

PARAGON TECHNOLOGIES, INC.
and Subsidiaries

ANNUAL REPORT

2015 YEAR-END CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED FINANCIAL STATEMENTS

I N D E X

Independent Auditor's Report

To the Board of Directors
Paragon Technologies, Inc.
Easton, Pennsylvania

Report on the Financial Statements
We have audited the accompanying consolidated financial statements of Paragon Technologies, Inc. and its subsidiary which comprise the consolidated balance sheets as of December 31, 2015 and 2014, and the related consolidated statements of operations, comprehensive income (loss), stockholders' equity and cash flows for each of the three years in the period ended December 31, 2015 and the related notes to the consolidated financial statements, (collectively, financial statements).

Management's Responsibility for the Financial Statements
Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility
Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Paragon Technologies, Inc. and its subsidiary as of December 31, 2015 and 2014, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2015 in accordance with accounting principles generally accepted in the United States of America.

RSM US LLP

Blue Bell, Pennsylvania
March 31, 2016

PARAGON TECHNOLOGIES, INC.
Consolidated Balance Sheets
December 31, 2015 and 2014
(In Thousands, Except Share and Per Share Data)

	December 31, 2015	December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	$ 1,841	$ 1,803
Trade accounts receivables	1,454	1,594
Costs and estimated earnings in excess of billings	155	31
Inventories:		
Raw materials	100	78
Work-in-process	3	38
Finished goods	255	157
Total inventories	358	273
Prepaid expenses and other current assets	32	41
Total current assets	3,840	3,742
Marketable securities	680	686
Machinery, equipment, and software, at cost:		
Machinery and equipment	547	565
Software	906	771
Less: accumulated depreciation	976	837
Net machinery, equipment, and software	477	499
Other assets - intangible assets, net	774	834
Total assets	$ 5,771	$ 5,761

See accompanying notes to consolidated financial statements.

(Continued)

PARAGON TECHNOLOGIES, INC.
Consolidated Balance Sheets *(Continued)*
December 31, 2015 and 2014
(In Thousands, Except Share and Per Share Data)

	December 31, 2015	December 31, 2014
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 740	$ 697
Billings in excess of costs and estimated earnings	396	1,410
Accrued salaries, wages, and commissions	287	104
Accrued product warranties	142	121
Unearned support contract revenue	232	192
Income taxes payable	110	26
Accrued other liabilities	263	359
Total current liabilities	2,170	2,909
Commitments and contingencies (Notes 8 and 9)		
Stockholders' equity:		
Common stock, $1 par value; authorized 20,000,000 shares; issued and outstanding 1,684,745 shares as of December 31, 2015 and 2014	1,685	1,685
Additional paid-in capital	3,499	3,499
Accumulated deficit	(1,552)	(2,400)
Accumulated other comprehensive income (loss)	(31)	68
Total stockholders' equity	3,601	2,852
Total liabilities and stockholders' equity	$ 5,771	$ 5,761

See accompanying notes to consolidated financial statements.

PARAGON TECHNOLOGIES, INC.
Consolidated Statements of Operations
For the Years Ended December 31, 2015, 2014, and 2013
(In Thousands, Except Share and Per Share Data)

	December 31, 2015	December 31, 2014	December 31, 2013
Net sales	$ 11,582	$ 6,680	$ 11,643
Cost of sales	7,772	4,886	8,098
Gross profit on sales	3,810	1,794	3,545
Operating expenses:			
Selling, general and administrative expenses	2,667	2,197	2,519
Product development costs	115	64	125
Total operating expenses	2,782	2,261	2,644
Operating income (loss)	1,028	(467)	901
Other income (expense):			
Interest expense	(1)	(11)	(1)
Interest income	20	17	12
Loss on investment, equity method	-	-	(2,997)
Gain on investment, marketable securities	17	13	37
Total other income (expense), net	36	19	(2,949)
Income (loss) before income taxes	1,064	(448)	(2,048)
Income tax (expense) benefit	(216)	17	272
Net income (loss)	$ 848	$ (431)	$ (1,776)
Basic and diluted income (loss) per share	$ .50	$ (.26)	$ (1.11)
Weighted average shares outstanding	1,684,745	1,684,745	1,605,672
Dilutive effect of stock options	-	-	189,000
Weighted average shares outstanding assuming dilution	1,684,745	1,684,745	1,794,672

See accompanying notes to consolidated financial statements.

PARAGON TECHNOLOGIES, INC.
Consolidated Statements of Comprehensive Income (Loss)
For the Years Ended December 31, 2015, 2014, and 2013
(In Thousands)

	December 31, 2015	December 31, 2014	December 31, 2013
Net income (loss)..	$ 848	$ (431)	$ (1,776)
Other comprehensive income (loss):			
Unrealized gain (loss) on marketable securities, net of tax of $65 in 2015, ($33) in 2014 and ($3) in 2013	(99)	50	6
Comprehensive income (loss)	$ 749	$ (381)	$ (1,770)

See accompanying notes to consolidated financial statements

PARAGON TECHNOLOGIES, INC.
Consolidated Statements of Stockholders' Equity
For the Years Ended December 31, 2015, 2014 and 2013
(In Thousands, Except Share and Per Share Data)

	Common Stock		Additional Paid-In Capital	Accumulated Deficit	Unamortized Restricted Stock	Accumulated Other Comprehensive Income	Total Stockholders' Equity
	Shares	Amount					
Balance at January 1, 2013	1,656,854	$ 1,657	$ 3,441	$ (193)	$ 5	$ 12	$ 4,922
Net loss	-	-	-	(1,776)	-	-	(1,776)
Net change in unrealized gain on marketable securities, net of tax	-	-	-	-	-	6	6
Issue of common stock in lieu of directors' fees under directors' stock plan	21,268	21	34	-	-	-	55
Restricted stock grant to employee	6,623	7	10	-	(5)	-	12
Stock option grants to officers and employee –	-	-	13	-	-	-	13
Balance at December 31, 2013	1,684,745	1,685	3,498	(1,969)	-	18	3,232
Net income	-	-	-	(431)	-	-	(431)
Net change in unrealized gain on marketable securities, net of tax	-	-	-	-	-	50	50
Stock option grants to officers and employee	-	-	1	-	-	-	1
Balance at December 31, 2014	1,684,745	$ 1,685	$ 3,499	$ (2,400)	$ -	$ 68	$ 2,852
Net income	-	-	-	848	-	-	848
Net change in unrealized loss on marketable securities, net of tax	-	-	-	-	-	(99)	(99)
Balance at December 31, 2015	1,684,745	$ 1,685	$ 3,499	$ (1,552)	$ -	$ (31)	$ 3,601

See accompanying notes to consolidated financial statements.

PARAGON TECHNOLOGIES, INC.
Consolidated Statements of Cash Flows
For the Years Ended December 31, 2015, 2014 and 2013
(In Thousands)

	December 31, 2015	December 31, 2014	December 31, 2013
Cash flows from operating activities:			
Net income (loss)………………………………..	$ 848	$ (431)	$ (1,776)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation of machinery, equipment and software	203	80	32
Amortization of intangible assets	60	48	39
Loss on disposition of machinery and equipment...	5	3	-
Investment loss – equity method of valuation	-	-	2,997
Realized gains on investments...........................	(17)	(18)	(37)
Issue of common stock in lieu of Directors' fees………………………………	-	-	55
Stock-based compensation	-	1	25
Deferred taxes……………………………………	65	(33)	(361)
Change in operating assets and liabilities:			
Receivables	140	(894)	1,140
Costs and estimated earnings in excess of billings………………………………………….	(124)	168	(181)
Inventories	(85)	131	191
Prepaid expenses and other current assets	9	39	(35)
Accounts payable	43	55	(237)
Billings in excess of costs and estimated earnings	(1,014)	1,173	(1,182)
Accrued salaries, wages and commissions	183	(193)	202
Income taxes payable	84	(27)	58
Accrued product warranties	21	(38)	27
Unearned support contract revenue	40	(73)	(124)
Accrued other liabilities	9	(23)	14
Net cash provided by (used in) operating activities	470	(32)	847

(Continued)

PARAGON TECHNOLOGIES, INC.
Consolidated Statements of Cash Flows (Continued)
For the Years Ended December 31, 2015, 2014 and 2013
(In Thousands)

	December 31, 2015	December 31, 2014	December 31, 2013
Cash flows from investing activities:			
Purchases of machinery, equipment and software…………………………………………….	(186)	(311)	(225)
Purchases of investments ………………………..	(613)	(498)	(2,810)
Proceeds from sale of investments………………	472	238	512
Acquisition, net of cash required ………………..	-	-	(212)
Net cash used in investing activities …………………………………………..	(327)	(571)	(2,735)
Cash flows from financing activities:			
Repayments of amounts due to seller	(105)	(140)	(70)
Net cash used in financing activities…………………………………………..	(105)	(140)	(70)
Increase (decrease) in cash and cash equivalents	38	(743)	(1,958)
Cash and cash equivalents, beginning of year………………………………….	1,803	2,546	4,504
Cash and cash equivalents, end of year…………	$ 1,841	$ 1,803	$ 2,546
Supplemental disclosures of cash flow Information:			
Cash paid during the period for:			
Interest expense………………………………	$ 1	$ 10	$ 1
Income taxes ………………………………….	$ 69	$ 61	$ 57
Supplemental disclosures of noncash Investing activities:			
Mark to market on available for sale securities, gross …………………………..	$ (164)	$ 83	$ 9

See accompanying notes to consolidated financial statements.

(1) Description of Business and Summary of Significant Accounting Policies

Description of Business and Concentrations of Credit Risk

Paragon Technologies, Inc. (“Paragon” or the “Company”), based out of Easton, Pennsylvania, provides a variety of material handling solutions, including systems, technologies, products, and services for material flow applications through its wholly owned subsidiary, SI Systems, LLC (“SI Systems”). SI Systems’ capabilities include horizontal conveyance and transportation, rapid dispensing for order fulfillment, a full suite of high performance Warehouse Execution Systems (WES), Warehouse Management Systems (WMS) and Warehouse Control Systems (WCS) software systems and aftermarket services.

SI Systems’ automated material handling systems are used by manufacturing, assembly, order fulfillment, and distribution operations customers located primarily in North America, including the U.S. government. SI Systems’ branded products are utilized to automate the movement or selection of products and are often integrated with other automated equipment such as pick to light devices, conveyors and robots. SI Systems is brought to market as two individual brands, SI Systems’ Order Fulfillment Systems (hereafter referred to as “SI Systems OFS”) and SI Systems’ Production & Assembly Systems (hereafter referred to as “SI Systems PAS”).

The OFS business focuses on providing order fulfillment systems to distribution operations, including Dispen-SI-matic®, Doc-U-spense™ and Mobile-Matic™ (a patented product) and our full suite of Warehouse Execution Systems, Warehouse Management Systems and Warehouse Control Systems software solutions with our VWare™ product. These systems are sold primarily through a nationwide network of authorized material handling integrators, dealers and direct to major OEM accounts.

The PAS business focuses on providing automated material handling systems to manufacturing, assembly and distribution operations via our Lo-Tow® horizontal conveyance and transportation technologies. These systems are sold primarily to end users.

SI Systems’ automated material handling systems are marketed, designed, sold, installed, and serviced by its own staff or subcontractors as labor-saving devices to improve productivity, quality, and reduce costs. SI Systems’ integrated material handling solutions involve both standard and specially designed components and include integration of non-proprietary automated handling technologies to provide turnkey solutions for its customers' unique material handling needs. SI Systems’ engineering staff develops and designs computer control programs required for the efficient operation of the systems and for optimizing manufacturing, assembly, and fulfillment operations.

Paragon also invests in businesses and securities under the Investment Management Policy. The Investment Management Policy sets forth the parameters under which a portion of Paragon’s cash balance may be invested in marketable securities, including U.S. Treasuries, equities of publicly traded companies, bonds, money market instruments and other securities. Investment decisions under the Investment Management Policy are made by Sham Gad, CEO and Chairman of the Board. The Investment Management Policy sets forth restrictions on the investment of Paragon’s funds, including an aggregate limit on Paragon’s cash balance that is made available for investment, limits on the amount that may be invested in any single equity or fixed income position or certain categories of securities, prohibition of short-selling, margin trading and the use of leverage, requirements for the management of the investment account, and other Board-approval requirements.

(1) <u>Description of Business and Summary of Significant Accounting Policies</u> *(Continued)*

<u>Description of Business and Concentrations of Credit Risk</u> *(Continued)*

In the year ended December 31, 2015, two customers individually accounted for sales of 24.4% and 11.1.%. In the year ended December 31, 2014, three customers individually accounted for sales of 13.7%, 13.5%, and 12.1.%. In the year ended December 31, 2013, three customers individually accounted for sales of 26.6%, 12.8% and 11.3%. No other customers accounted for over 10% of sales.

As of December 31, 2015, two customers individually owed the Company 45.0% and 28.0% in trade accounts receivable. One of these customers was included in the 2015 sales concentration noted above. As of December 31, 2014 two customers individually owed the Company 31.8% and 22.8% in trade accounts receivables. One of these customers was included in the 2014 sales concentration noted above. No other customers owed SI Systems in excess of 10% of trade accounts receivable at December 31, 2015 and 2014. The Company believes that the concentration of credit risk in its trade accounts receivable is substantially mitigated by SI Systems' ongoing credit evaluation process as well as the general creditworthiness of its customer base.

SI Systems' business is largely dependent upon a limited number of large contracts with a limited number of customers. This dependence can cause unexpected fluctuations in sales volume. Various external factors affect the customers' decision-making process on expanding or upgrading their current production or distribution sites. Customer's timing and placement of new orders is often affected by factors such as the current economy, current interest rates, and future expectations. SI Systems believes that its business is not subject to seasonality, although the rate of new orders can vary substantially from month to month. Since the Company recognizes sales on a percentage of completion basis for its systems contracts, fluctuations in SI Systems' sales and earnings occur with increases or decreases in major installations. SI Systems maintains its cash and cash equivalents in a financial institution located in the United States of America. At times, cash balances may be in excess of F.D.I.C. limits. Investment balances are held in broker accounts and may be in excess of S.I.P.C. limits.

<u>Principles of Consolidation</u>

The consolidated financial statements include the accounts of Paragon Technologies, Inc., SI Systems, LLC., a wholly owned subsidiary, and Innovative Automation, Inc., a wholly owned subsidiary of SI Systems, LLC., after elimination of intercompany balances and transactions.

<u>Use of Estimates</u>

The preparation of the financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The judgments made in assessing the appropriateness of the estimates and assumptions utilized by management in the preparation of the financial statements are based on historical and empirical data and other factors germane to the nature of the risk being analyzed. Materially different results may occur if different assumptions or conditions were to prevail. Estimates and assumptions are mainly utilized to establish the appropriateness of the inventory reserve, warranty reserve, deferred tax valuation allowance and revenue recognition on fixed price contracts.

<u>Innovative Automation, Inc</u>.

On April 18, 2013 the Company acquired Innovative Automation, Inc. (IA), a San Diego based company. The Company purchased all the outstanding capital stock with cash and a note payable due to seller as detailed herein. IA designs, builds and supports warehouse control systems software and has been in business since 1993.

The results of operations for IA have been included in the accompanying consolidated financial statements from the acquisition date forward. Revenue and costs since April 18, 2013 are not significant and therefore not reported separately. The purchase price was $562,500 consisting of cash payments of $150,000, a note payable of $350,000 and payment of certain liabilities of $62,500.

(1) Description of Business and Summary of Significant Accounting Policies *(Continued)*

Innovative Automation, Inc *(Continued)*

As part of the purchase agreement the seller may receive earn-out payments during the five year period following the closing date which will be accounted for as compensation in the period incurred as the earn-out was associated with the seller's employment. The earn-out payments are calculated based upon net booking of all warehouse control and management software. A portion of the earn-out is based upon a percentage of the revenue and the other portion is based upon certain gross margins achieved on sales, as defined in the agreement. During the years ended December 31, 2015 and December 31, 2014 the seller earned approximately $16,000 and $52,000 respectively, which was recorded in accrued other liabilities on the consolidated balance sheet and included in cost of sales on the consolidated statement of operations.

The allocation of the purchase price to the assets acquired and liabilities assumed is based upon the estimated fair values at the date of acquisition.

All acquisition-related costs, including legal, professional and other expenses, were expensed by the Company in the period incurred and not included in the purchase price. Acquisition costs were approximately $37,000 and are included in selling, general, and administrative expenses on the statement of operations for the year ended December 31, 2013.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, cash on deposit, amounts invested on an overnight basis with a bank or broker/dealer and other highly liquid investments purchased with an original maturity of three months or less.

Trade Accounts Receivable and Allowance for Doubtful Accounts

Trade accounts receivable are stated at outstanding balances, less an allowance for doubtful accounts. The Company provides an allowance for doubtful accounts determined by a specific identification of individual accounts. The Company writes off receivables upon determination that no further collections are probable. There was no allowance for doubtful accounts as of December 31, 2015 and 2014.

Inventories

Inventories are valued at the lower of average cost or market. Inventories primarily consist of materials purchased or manufactured for stock.

Marketable Securities

The Company's marketable securities portfolio is designated as available-for-sale. Securities classified as available-for-sale are those securities that the Company intends to hold for an indefinite period of time but not necessarily to maturity. Securities available-for-sale are carried at fair value. Any decision to sell a security classified as available-for-sale would be based on various factors, including significant movement in interest rates, changes in maturity mix of the Company's assets and liabilities, liquidity needs, capital considerations and other similar factors. Unrealized gains and losses are reported as increases or decreases in other comprehensive income (loss). Realized gains or losses, determined on the basis of the cost of the specific securities sold, are included in earnings.

Declines in the fair value of securities below their cost that are deemed to be other-than-temporary impairments (OTTI) are reflected in earnings as realized losses. In estimating OTTI under the rules for accounting for certain debt and equity securities, management considers many factors, including: (1) the length of time and the extent to which the fair value has been less than amortized cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the market decline was affected by macroeconomic conditions, and (4) whether the entity has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery. In instances when a determination is made that an other-than-temporary impairment exists but the investor does not intend to sell the debt security and it is not more likely than not that it will be required to sell the debt security prior to anticipated recovery, the other-than-temporary impairment is separated into (a) the amount of the total other-than-temporary impairment related to a decrease in cash flows expected to be collected from the debt security (the credit loss) and (b) the amount of the total other-than-temporary impairment related to all other

(1) <u>Description of Business and Summary of Significant Accounting Policies</u> *(Continued)*

<u>Marketable Securities</u> *(continued)*
factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings. The amount of the total other-than-temporary impairment related to all other factors is recognized in other comprehensive income.

The Company has not recognized any other-than-temporary impairment losses for the year ended December 31, 2015.

The amortized cost and approximate fair value of marketable securities available-for-sale as of December 31, are summarized as follows *(in thousands)*:

	Equity Securities			
	Amortized Costs	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2015	$ 732	$ 240	$ 292	$ 680
December 31, 2014 ………………..	574	146	34	686

At December 31, 2015, the Company had twelve equity securities in an unrealized loss position for less than seventeen months. The decline in fair value is not due to credit losses. The Company does not intend to sell these securities prior to recovery and it is more likely than not that the Company will not be required to sell these securities prior to recovery and, therefore, no securities are deemed to be other-than-temporarily impaired. Fair value accounting guidance provides a consistent definition of fair value, which focuses on exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value is a reasonable point within the range that is most representative of fair value under current market conditions.

In accordance with this guidance, the Company groups its financial assets and financial liabilities generally measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value.

Level 1 — Valuation is based on quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 1 assets and liabilities generally include debt and equity securities that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 — Valuation is based on inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. The valuation may be based on quoted prices for similar assets or liabilities; quoted prices in markets that are not active or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.

(1) Description of Business and Summary of Significant Accounting Policies *(Continued)*

Marketable Securities *(continued)*

Level 3 — Valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which determination of fair value requires significant management judgment or estimation.

For financial assets measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, are as follows *(in thousands)*:

	Equity Securities			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
As of December 31, 2015	$ 680	$ 680	$ -	$ -
As of December 31, 2014………..	686	661	25	-

Equity Method Investment

As of December 31, 2015 and 2014, the Company had 1,430,860 shares in SED International Holdings, Inc. (SED), representing 27.6% of the outstanding share capital of SED. At December 31, 2012, SED was traded on the NYSE, and the Company accounted for its shares in SED as a marketable equity security. Effective on or about November 26, 2013, SED voluntarily delisted its common stock from the NYSE and began trading on the OTC markets under ticker symbol SEDN, which is not considered an active market as defined by ASC 320, Investments – Debt and Equity Securities. As a result, the Company adopted the equity method of accounting for its investment in SED. Under this method, the Company's equity in the earnings or losses of the investee is reported currently in the Company's earnings. Upon adoption, the investment, results of operations, and retained earnings were adjusted retroactively on a step-by-step basis as if the equity method had been in effect during all previous periods in which the Investment was held. SED's last available published financial statement is for the period ending June 30, 2014. No further quarterly reports are publicly available. The latest closing price of SED as reported by the OTC Markets is $0.01 as of March 4, 2016.

As of December 31, 2015, the carrying value of the SED investment was $0. There was no investment activity for SED in 2015 and 2014.

Fixed Assets

Machinery, equipment and software are recorded at cost and are depreciated on the straight-line method over the estimated useful lives of individual assets. The Company capitalizes costs incurred to develop commercial software products or enhancements to software products where such enhancement extend the life of the products. The ranges of lives used in determining depreciation rates for machinery and equipment and software is generally 3 - 7 years. Maintenance and repairs are charged to operations; betterments and renewals are capitalized. Upon sale or retirement of machinery and equipment, the cost and related accumulated depreciation are removed from the accounts and the resultant gain or loss, if any, is credited or charged to earnings.

Intangible Assets

Intangible assets consist of a trade name and technology, which are being amortized over 6 years. The detail of the intangible assets and the related amortization are shown in Note 4 to the consolidated financial statements.

(1) <u>Description of Business and Summary of Significant Accounting Policies</u> *(Continued)*

<u>Impairment of Long Lived Assets</u>

The Company reviews the recovery of the net book value of long-lived assets whenever events and circumstances indicate that the net book value of an asset may not be recoverable. In cases where undiscounted expected future cash flows are less than the net book value, an impairment loss is recognized equal to an amount by which the net book value exceeds the fair value of assets. There were no impairments noted in 2015 or 2014.

<u>Revenue and Cost Recognition</u>

Revenues on fixed price systems contracts are recorded on the basis of the Company's estimates of the percentage of completion of individual contracts. Revenue and gross profit is recognized on the basis of the ratio of aggregate costs incurred to date to the most recent estimate of total costs. As contracts may extend over one or more years, revisions in cost and profit estimates during the course of the work are reflected in the accounting periods in which the facts requiring revisions become known. At the time a loss on a contract becomes known, the entire amount of the estimated ultimate loss is accrued.

Contract costs include all direct material, subcontract and labor costs, and those indirect costs related to contract performance, including but not limited to costs such as indirect labor, supplies, tools, repairs, and depreciation. Selling, general and administrative costs are charged to expense as incurred. Changes in job performance, job conditions, and estimated profitability may result in revisions to costs and income, which are recognized in the period in which the revisions are determined.

The asset, “Costs and estimated earnings in excess of billings,” represents revenues recognized in excess of amounts billed on uncompleted contracts. The liability, “Billings in excess of costs and estimated earnings,” represents billings in excess of revenues recognized on uncompleted contracts.

Revenues on other sales of parts or equipment are recognized when title transfers pursuant to shipping terms. There are no installation or customer acceptance aspects of these sales.

Revenue on individual support contracts is recognized on a straight-line basis over the one-year term of each individual support contract.

<u>Unearned Support Contract Revenue</u>

The Company offers its Order Fulfillment customers one-year support contracts for an annual service fee. The support contracts cover a customer’s single distribution center or warehouse where the Company’s products are installed. As part of its support contracts, the Company provides analysis, consultation, and technical information to the customer’s personnel on matters relating to the operation of its Order Fulfillment System and related equipment and/or peripherals.

The Company records advance payments for unearned support contracts in the balance sheet as a current liability that are in excess over amounts recognized as revenue at the end of each period. Revenue on individual support contracts is deferred and recognized on a straight-line basis over the one-year term of each individual support contract.

<u>Product Development Costs</u>

The Company expenses product development costs as incurred.

<u>Accrued Product Warranty</u>

The Company’s products are warranted against defects in materials and workmanship for varying periods of time depending on customer requirements and the type of system sold, with a typical warranty period of one year. The Company provides an accrual for estimated future warranty costs and potential product liability claims based upon a percentage of cost of sales, typically one and one-half percent of the cost of the system being sold. A detailed review of the liability needed for products still in the warranty period is performed each quarter.

(1) Description of Business and Summary of Significant Accounting Policies *(Continued)*

Accrued Product Warranty *(continued)*

A roll-forward of warranty activities is as follows *(in thousands)*:

	Beginning Balance January 1	Additions (Reductions) Included in Cost of Sales	Claims	Ending Balance December 31
2015	$ 121	$ 22	$ (1)	$ 142
2014	159	(34)	(4)	121

Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Income tax expense is the tax payable or refundable for the period, plus or minus the change during the period in deferred tax assets and liabilities.

Tax benefits for uncertain tax positions are recognized when it is more likely than not that the position will be sustained upon examination based on its technical merits. The Company classifies interest and penalties related to unrecognized tax benefits as a component of income tax expense. To the extent interest and penalties are not assessed with respect to uncertain tax positions, amounts accrued will be reduced and reflected as a reduction of the overall income tax provision.

The Company is subject to U.S. federal income tax as well as income tax of multiple state jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal, state, and local income tax examinations by tax authorities for years before 2012.

Stock-Based Compensation

The Company has a stock-based compensation plan in place and records the associated stock-based compensation expense over the requisite service period. These stock-based compensation plans and related compensation expense are discussed more fully in Note 5 to the consolidated financial statements.

Restricted stock awards that are service-based are recorded as deferred compensation and amortized into compensation expense on a straight-line basis over the vesting period, which ranges from three to four years in duration. Compensation cost for service-based restricted stock is based on the grant date fair value of the award, which is the closing market price of the Company's common stock on the grant date multiplied by the number of shares awarded.

Earnings Per Share

Basic and diluted earnings per share for the years ended December 31, 2015, 2014 and 2013 are based on the weighted average number of shares outstanding. In addition, diluted earnings per share reflect the effect of dilutive securities which include the shares that would be outstanding assuming the exercise of dilutive stock incentive plan awards. The number of shares that would be issued from the exercise has been reduced by the number of shares that could have been purchased from the proceeds at the average market price of the Company's common stock.

(2) Line of Credit

On May 30, 2013, the Company established a $750,000 line of credit facility with its principal bank to be used primarily for working capital purposes. The line of credit facility contains various non-financial covenants and is secured by all of the Company's trade accounts receivables and inventories. The availability on the line of credit

(2) Line of Credit *(Continued)*
was $750,000 as of December 31, 2015. Interest on the line of credit facility is based on the "Wall Street Journal Prime Rate." There were no borrowings outstanding as of December 31, 2015 or 2014.

On October 24, 2012, the Company established a $3,225,000 line of credit facility with its marketable securities broker to be used primarily for general business purposes. On March 21, 2015, the line of credit facility was reduced to $100,000. On November 2, 2015, the line of credit facility was increased to $945,000. The line of credit facility is secured by the available securities in the account. The availability on the line of credit was approximately $945,000 as of December 31, 2015. Interest on the line of credit facility is based on the one (1) month Libor rate plus 225 bps. There were no borrowings outstanding as of December 31, 2015 or 2014.

(3) Uncompleted Contracts

Costs and estimated earnings and billings on uncompleted contracts are as follows *(in thousands):*

	December 31,2015	December 31, 2014
Costs and estimated earnings on uncompleted contracts	$ 8,191	$ 983
Less: billings to date	(8,432)	(2,362)
	$ (241)	$ (1,379)
Included in accompanying balance sheets under the following captions:		
Costs and estimated earnings in excess of billings	$ 155	$ 31
Billings in excess of costs and estimated earnings	(396)	(1,410)
	$ (241)	$ (1,379)

(4) Intangible Assets

Intangible assets are as follows *(in thousands):*

2015	Gross Carrying Amount	Accumulated Amortization	Net Book Value
VWARE™ software	$ 761	$ 121	$ 640
Trade name	160	26	134
	$ 921	$ 147	$ 774

2014	Gross Carrying Amount	Accumulated Amortization	Net Book Value
VWARE™ software	$ 761	$ 72	$ 689
Trade name	160	15	145
	$ 921	$ 87	$ 834

Aggregate amortization expense for intangible assets is estimated to be as follows: 2016 $107; 2017 $177; 2018 $208; and 2019 $282.

(5) Stock Options and Non-vested Stock

2012 Equity Incentive Plan

On July 27, 2012, the Board of Directors of the Company adopted the Paragon Technologies, Inc. 2012 Equity Incentive Plan (the "Plan"). Under the Plan, the Board may grant restricted stock, stock options, stock appreciation rights and other equity-based awards to employees, directors and consultants of the Company. Initially, there were 200,000 shares of the Company's common stock available for grant under the Plan. The Plan provides that it will be administered by the Board or a committee of the Board that may be designated in the future. The Plan has a term of 10 years. On September 18, 2013, the Board of Directors increased the number of shares of common stock available for grant under the Plan to 350,000 shares.

Under the Plan, officers have been granted options to purchase shares of common stock. Each of these options has an exercise price equal to the average of the closing bid and asked prices for the Company's common stock on the OTC Markets for the thirty trading days immediately preceding the grant date. Stock options vest in four or five equal annual installments beginning on the first anniversary of the date of grant.

Vested stock option awards may be exercised through payment of cash, exchange of mature shares, or through a broker. As of December 31, 2015 and 2014, no stock options were outstanding under the plan.

Stock-based compensation expense recognized during the years ended December 31, 2015 and 2014 for stock-based compensation programs was $0 and $1,200, respectively. All of the stock-based compensation expense recognized was a component of selling, general and administrative expenses.

During 2014, all of the officers that had been granted options to purchase shares of common stock had terminated their employment. Per the stock option award agreement the term of the options shall expire one (1) month after the termination of optionee's employment with the company for any reason (the "Expiration Date"). Upon the Expiration Date, the option will automatically be cancelled and will be of no further force or effect to the extent not exercised prior thereto. As of December 31, 2014 all of the options for shares had been cancelled.

The Company estimates the fair value of stock options on the grant date by applying the Black-Scholes option pricing valuation model. The application of this valuation model involved assumptions that are highly subjective, judgmental, and sensitive in the determination of compensation cost.

There were no options granted during 2015 and 2014.

A summary of stock option activity is presented below:

Options	Shares	Weighted-Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2013	149,000	$ 2.50	9.7	$ -
Granted	40,000	2.88	9.3	-
Outstanding at December 31, 2013	189,000	2.58	8.6	9
Forfeited	(189,000)	2.58	8.1	-
Outstanding at December 31, 2014	-	$ -	-	$ -
Exercisable at December 31, 2015	-	$ -	-	$ -
Exercisable at December 31, 2014	32,050	$ 2.50	8.3	$ 4

(5) Stock Options and Non-vested Stock *(Continued)*

2012 Equity Incentive Plan *(Continued)*

A summary of the status of the Company's non-vested shares as of December 31, 2014 and 2013 is presented below:

Nonvested Shares	Shares	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2013	149,000	$ 0.49
Granted	40,000	0.60
Vested	(32,050)	0.49
Nonvested at December 31,2013	156,950	0.52
Vested	(10,000)	0.60
Forfeited	(146,950)	0.52
Nonvested at December 31, 2014	-	$ -

Directors' Fees Paid

For the first six months of 2013, directors were entitled to the following director compensation:

- Annual retainer of $20,000 per year in cash payable quarterly;
- Fee of $2,500 per director for each in-person Board Meeting;
- The Company will pay travel and hotel lodging for in-person Board Meetings;
- Fee of $500 per director for each Board Teleconference Meeting;
- Fee of $1,000 for the Chair of the Audit Committee for each committee meeting; and
- Fee of $500 per director for each committee meeting.

Effective July 2013, directors were entitled to the following director compensation:

- Annual retainer of $40,000 per year;
- $30,000 in cash payable quarterly; and
- $10,000 in shares of common stock under the Equity Incentive Plan.
- The Company will pay travel and hotel lodging for in person Board Meetings;

For year ended December 31, 2013, the Company issued 3,936 shares to the directors under this Plan, with an expense of $10,000.

For 2014, each director, including Mr. Gad, was paid $30,000 in cash in four equal quarterly installments in advance. The Company paid travel and hotel lodging for in-person board meetings.

For 2015, each director was paid the same fees as stated above for 2014 except for Mr. Gad, who was paid $60,000 for the year. The Company paid travel and hotel lodging for in person board meetings.

For 2016, Mr. Gad will be paid $150,000 in cash and the other directors will be paid $30,000 in cash in four equal quarterly installments in advance.

Chairman's Compensation

For the first six months of 2013, Mr. Gad was paid $25,000 in cash and $30,000 in shares of common stock, paid quarterly, with the common stock being valued based on the average of the closing bid and asked prices for the Company's common stock on the OTC Markets for the 30 trading days immediately preceding stock issuance.

Effective July 2013, the payment of Mr. Gad's compensation was revised to be paid $80,000 in cash and $30,000 in shares of common stock.

(5) Stock Options and Non-vested Stock *(Continued)*

Chairman's Compensation *(Continued)*

For the year ended December 31, 2013, the Company issued 17,332 shares to the Chairman under this Plan, with an expense of $45,000.

As noted previously, for 2014, in lieu of the foregoing Mr. Gad was paid $30,000 in cash in four equal quarterly installments in advance.

For the year ended December 31, 2015, Mr. Gad was paid $22,500 in cash in three equal quarterly installments in advance and $37,500 in advance for the fourth quarter that totaled $60,000.

For 2016, Mr. Gad will be paid $150,000 in cash in four equal quarterly installments.

(6) Employee Benefit Plans

The Company has a defined contribution Retirement Savings Plan for its employees. Employees age 21 and above are eligible to participate in the Plan. Effective March 30, 2009, Company contributions under the Company's Retirement Savings Plan were suspended for an indefinite period of time as part of a cost-reduction initiative. Effective August 14, 2015, Company contributions have been reinstated. The matching contribution for the years ended December 31, 2015, 2014 and 2013 was $19,813, $0 and $0 respectively. The Plan also contains provisions for profit sharing contributions in the form of cash as determined annually by the Company's Board of Directors. The profit sharing contribution for the year ended December 31, 2015, 2014 and 2013 was $0, $30,000 and $0 respectively. Total expense for the Retirement Savings Plan, including Plan expenses, was $20,955, $30,300 and $1,200 for the years ended December 31, 2015, 2014 and 2013, respectively.

(7) Income Taxes

The provision for income tax benefit consists of the following *(in thousands)*:

		For the Year Ended December 31, 2015	For the Year Ended December 1, 2014	For the Year Ended December 31, 2013
Federal:	current	$ 139	$ -	$ 12
	deferred	52	(26)	(304)
		191	(26)	(292)
State:	current	12	16	75
	deferred	13	(7)	(55)
		25	9	20
		$ 216	$ (17)	$ (272)

(7) Income Taxes *(Continued)*

The reconciliation between the U.S. federal statutory rate and the Company's effective income tax rate is *(in thousands):*

	Year Ended December 31, 2015	Year Ended December 31, 2014	Year Ended December 31, 2013
Computed tax expense (benefit) at statutory rate of 34%	$ 362	$ (152)	$ (733)
Increase (reduction) in taxes resulting from:			
State income taxes, net of federal benefit	5	(17)	(101)
Meals and entertainment deduction …..	2	2	3
Valuation allowance	(163)	51	562
Miscellaneous items	10	99	(3)
	$ 216	$ (17)	$ (272)

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities at December 31, 2015 and 2014 are presented below *(in thousands):*

	Year Ended December 31, 2015	Year Ended December 31, 2014
Deferred tax assets:		
Net operating loss carryforward	$ 146	$ 448
Inventory reserve	118	132
Accrued warranty costs	54	45
Unrealized loss on equity method investment	1,182	1,171
Amortization of software development cost ……………...	92	14
Intangibles earn out payments …………………………	28	20
Accruals for other expenses, not yet deductible for tax purposes	110	82
Total gross deferred tax assets	1,730	1,912
Less: valuation allowance	(1,143)	(1,307)
Net deferred tax assets	587	605
Deferred tax liabilities:		
Machinery and equipment, principally due to differences in depreciation	(56)	(42)
Software development cost	(206)	(154)
Unrealized gain/loss on investments	20	(42)
Intangibles ……………………………………………..….	(333)	(352)
Prepaid expenses …………………………………………	(12)	(15)
Total gross deferred tax liabilities	(587)	(605)
Net deferred tax assets	$ -	$ -

The Company has state net operating losses of approximately $2,183 at December 31, 2015, expiring at various times based on individual state limits.

Valuation allowances are provided to reduce the carrying amount of deferred tax assets when it is more likely than not that some portion or all of the deferred tax assets will not be realized. When assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the

(7) <u>Income Taxes</u> *(Continued)*
generation of future taxable income in the appropriate taxing jurisdictions during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, taxable income in carryback years, and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income, management has concluded that the Company's deferred tax assets are more likely than not to expire before the Company can use them and, therefore, the Company's management has concluded that a full valuation allowance for deferred tax assets, net of deferred tax liabilities, was appropriate as of December 31, 2015 and 2014.

A roll forward of valuation allowance activities is as follows *(in thousands):*

	Beginning Balance January 1	Additions Charged to Income Tax Expense	Charge-Offs	Ending Balance December 31
2015………	$ 1,307	$ -	$ (164)	$ 1,143
2014………	1,255	52	-	1,307

The valuation allowance at December 31, 2015 and 2014 was an offset of net deferred tax assets primarily related to inventory, warranty, net operating loss carryforwards, and other temporary differences.

Tax benefits for uncertain tax positions are recognized when it is more likely than not that the position will be sustained upon examination based on its technical merits.

(8) <u>Contingencies</u>

From time to time, the Company is involved in various claims and legal actions arising in the ordinary course of business. Although the amount of any liability that could arise with respect to currently pending actions cannot be accurately predicted, in the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's financial position, results of operations, or liquidity. There are no pending actions as of December 31, 2015.

(9) <u>Commitments</u>

The Company previously leased a facility located at 600 Kuebler Road in Easton, Pennsylvania. The leasing agreement required fixed monthly rental payments of $18,000 and the lease expired on February 20, 2013.

On November 28, 2012, the Company renewed the lease agreement to extend the term of the lease for a period of one year. Commencing on February 21, 2013, the square footage of the lease was reduced to 15,200 square feet and the fixed monthly rental payments were reduced to $12,750 for one year through February 20, 2014.

On December 30, 2013, the Company entered into a new lease agreement for an initial term of two years followed by an option to renew for two consecutive/additional terms of two years each. The lease commenced on April 15, 2014 and expires on February 14, 2016. The Company has renewed the lease for two additional years through February 14, 2018. The area of the new lease is 9,648 square feet in Easton, Pennsylvania. The leasing agreement requires fixed monthly payments of $12,750 through February 14, 2016, $13,000 for the next twelve months and $13,500 for the final twelve months through February 14, 2018.

Total rental expense in the years ended December 31, 2015, 2014, and 2013 approximated $204,500, $167,000 and $171,000, respectively.

(9) Commitments *(Continued)*

Future minimum rental commitments at December 31, 2015 are as follows *(in thousands):*

	Operating Leases
2016	$ 156
2017	161
2018	27
TOTAL	$ 344

(10) Stock Repurchase Program

On May 14, 2015, the Company's board of directors approved a program to repurchase up to $250,000 of its outstanding stock. There were no stock repurchases during the year ended December 31, 2015.

(11) Recently Issued Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), requiring an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The updated standard will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective and permits the use of either a full retrospective or retrospective with cumulative effect transition method. The updated standard will be effective for interim and annual reporting periods beginning after December 15, 2017. In August 2015, the FASB issued ASU 2015-14 which defers the effective date of ASU 2014-09 one year making it effective for annual reporting periods beginning after December 31, 2018. The Company has not yet selected a transition method and is currently evaluating the effect that the updated standard will have on the consolidated financial statements.

In August 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standard Update (ASU) 2014-15, Presentation of Financial Statements – Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. ASU 2014-15 explicitly requires management to evaluate, at each annual reporting period, whether there are conditions or events that exist which raise substantial doubt about an entity's ability to continue as going concern and to provide related disclosures. ASU 2014-15 is effective for annual periods ending after December 15, 2016, with early adoption permitted. The adoption of this accounting guidance is not expected have a material effect on the Company's financial condition or results of operations.

In July 2015, the FASB issued ASU 2015-11, Inventory (Topic 330): Simplifying the Measurement of Inventory. The amendments in the ASU require entities that measure inventory using the first in, first-out or average cost methods to measure inventory at the lower of cost and net realizable value. Net realizable value is defined as estimated selling price in the ordinary course of business less reasonably predictable costs of completion, disposal and transportation. ASU 2015-11 is effective for financial statements issued for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016 on a prospective basis. The Company does not expect the adoption of ASU 2015-11 to have a material effect on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). The guidance in the ASU supersedes the leasing guidance in Topic 840, Leases. Under the new guidance, lessees are required to recognize lease assets and lease liabilities 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. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company is currently evaluating the impact of our pending adoption of the new standard on our consolidated financial statements.

(12) Subsequent Events

Events and transactions for items that should potentially be recognized or disclosed in these financial statements occurring subsequent to the balance sheet date of December 31, 2015 have been evaluated through March 31, 2016 the date which these financial statements were available to be issued.