Microwave Filter Company, Inc.

2020

Financial Statements

To the Shareholders:

FY2020 was a challenging year given the outbreak of the COVID-19 pandemic. MFC received confirmation as an essential business from the state of New York pursuant to the revised New York State Executive Order 202.6. MFC remained open following safety guidelines and taking other appropriate actions as needed.

In FY2020 MFC saw a decrease in sales of $813,000 compared to 2019 resulting in a loss of $293,000. It is unclear how much of the decline in sales is due to the COVID-19 pandemic but MFC believes there was a material impact. MFC did obtain a PPP loan for $298,282, which if forgiven in full or in part, will mitigate or eliminate the fiscal year loss. Primarily because of the PPP loan, the cash position of MFC was up $46,000 compared to FY2019.

The Broadcast TV market saw the largest decline of $457,900 or 56%. This decrease was primarily due to orders from one customer that did not recur in fiscal 2020. MFC believes that the reduction in spending of this key customer was a result of a reduction of government spending as funds were diverted to combat COVID-19 pandemic.

The Cable TV market saw a decline of $181,000 or 40%. This decrease was primarily due to orders from one customer that did not recur in fiscal 2020. MFC believes that the reduction in spending of these key customers was a result of a reduction of government spending as funds were diverted to combat COVID-19 pandemic.

The RF/Microwave market saw a decline of $163,000 or 10%. The Satellite market was steady with a decline of $11,000 or 1%

While the COVID-19 pandemic will continue to affect the economy in the future, MFC continues to be optimistic. The company continues to invest in production engineering, product development and developing OEM partners in key market segments, including 5G, 5G related and other satcom and other RF specialized solutions. We continue to believe that the 5G and satcom segments will lead to our greatest growth opportunities, followed by key broadcast and RF segments.

MFC is in a strong financial position. At this time MFC believes it is reasonable to expect that the PPP loan will be forgiven in full or in part. This cash position is sufficient to provide the resources needed to execute our strategies. The management of MFC is particularly appreciative of our partners and employees during this difficult time.

Sincerely,

Carl F. Fahrenkrug, Jr	Robert R. Andrews
Chief Executive Officer	Chairman of the Board

MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS

Microwave Filter Company, Inc. (MFC) operates primarily in the United States and principally in one industry. The Company extends credit to business customers, including original equipment manufacturers (OEMs), distributors and other end users, based upon ongoing credit evaluations. Microwave Filter Company, Inc. designs, develops, manufactures and sells electronic filters, both for radio and microwave frequencies, to help process signal distribution and to prevent unwanted signals from disrupting transmit or receive operations. Markets served include cable television, television and radio broadcast, satellite broadcast, mobile radio and commercial and defense electronics. NSI's sales consist of spare parts orders.

THE IMPACT OF COVID-19

In March 2020, the coronavirus disease 2019 (“COVID 19”) was declared a pandemic by the World Health Organization and a national emergency by the U.S. Government.

The financial impact of the COVID 19 pandemic cannot be reasonably estimated at this time as its impact depends on future developments, which are highly uncertain and cannot be predicted.

In late March, Microwave Filter Company, Inc. received confirmation from the State of New York that we are designated as an “essential business” pursuant to the revised New York State Executive Order 202.6 with respect to our business function of supply partner for several essential industries.

RESULTS OF OPERATIONS

The following table sets forth the Company's net sales by major product group for each of the fiscal years in the two year period ended September 30, 2020.

Product group	Fiscal 2020	Fiscal 2019
Microwave Filter:		
RF/Microwave	$ 1,471,799	$ 1,634,760
Satellite	1,000,738	1,011,347
Broadcast TV	362,602	820,514
Cable TV	272,338	453,633
Niagara Scientific	133	84
Total	$ 3,107,610	$ 3,920,338
Sales backlog at 9/30	$ 631,764	$ 827,981

Fiscal 2020 compared to fiscal 2019

Consolidated net sales for the fiscal year ended September 30, 2020 equaled $3,107,610, a decrease of $812,728 or 20.7%, when compared to consolidated net sales of $3,920,338 during the fiscal year ended September 30, 2019.

MFC's RF/Microwave product sales decreased $162,961 or 10% to $1,471,799 during the fiscal year ended September 30, 2020 when compared to sales of $1,634,760 during the fiscal year ended September 30, 2019. MFC's RF/Microwave products are sold primarily to Original Equipment Manufacturers (OEM) that serve the mobile radio, commercial communications and defense electronics markets. Sales to one OEM customer decreased $238,434 to $1,182,621, or 38.1% of total sales, during the fiscal year ended September 30, 2020 compared to sales of $1,421,055, or 36.2% of total sales, during the fiscal year ended September 30, 2019. These sales are in connection with a multiyear program in which the Company is a subcontractor. The Company continues to invest in production engineering and infrastructure development to penetrate OEM market segments as they become popular. MFC is concentrating its technical resources and product development efforts toward potential high volume customers as part of a concentrated effort to provide substantial long-term growth. Over the last year, MFC, in conjunction with various OEM’s, has developed and supplied prototypes as well as small production runs in support of new programs being introduced to the marketplace. It is our belief that a continuation of this effort will help increase sales as well as reinforcing MFC’s position as a quality manufacturer of RF filters and assemblies.

MFC's Satellite product sales decreased $10,609 or 1% to $1,000,738 during the fiscal year ended September 30, 2020 when compared to sales of $1,011,347 during the fiscal year ended September 30, 2019. The decrease can be attributed to a decrease in demand for filters which suppress strong out-of-band interference caused by military and civilian radar systems and other sources. Management expects demand for these types of filters to continue with the proliferation of earth stations world wide and increased sources of interference.

MFC's Broadcast TV product sales decreased $457,912 or 55.8% to $362,602 for the fiscal year ended September 30, 2020 when compared to sales of $820,514 for the fiscal year ended September 30, 2019. The decrease can primarily be attributed to one customer.

MFC's Cable TV product sales decreased $181,295 or 40% to $272,338 during the fiscal year ended September 30, 2020 when compared to Cable TV product sales of $453,633 during the fiscal year ended September 30, 2019. The decrease can primarily be attributed to one customer. Management continues to project flat or a decrease in demand for Cable TV products due to the shift from analog to digital television. Due to the inherent nature of digital modulation versus analog modulation, fewer filters will be required. The Company has developed filters for digital television and there will still be requirements for analog filters for limited applications in commercial and private cable systems.

At September 30, 2020, the Company's total backlog of orders, which represents firm orders from customers, equaled $631,764 compared to $827,981 at September 30, 2019. The total Company backlog at September 30, 2020 is scheduled to ship during fiscal 2021. However, backlog is not necessarily indicative of future sales. Accordingly, the Company does not believe that its backlog as of any particular date is representative of actual sales for any succeeding period.

Gross profit decreased $562,878 to $1,077,536 during the fiscal year ended September 30, 2020 when compared to gross profit of $1,640,414 during the fiscal year ended September 30, 2019. The decrease in gross profit can be attributed the lower sales volume providing a lower base to absorb overhead expenses.

Selling, general and administrative (SG&A) expenses decreased $87,128 or 6% to $1,372,019 during the fiscal year ended September 30, 2020 when compared to SG&A expenses of $1,459,147 during the fiscal year ended September 30, 2019 . The decrease can be attributed to lower payroll costs.

Other income (expense) was income of $1,896 for the fiscal year ended September 30, 2020 compared to expense of $353 for the fiscal year ended September 30, 2019 primarily due to interest expense of $8,719 offset by interest income of $6,092 and miscellaneous non-operating income of $4,523 for the fiscal year ended September 30, 2020 and interest expense of $11,084 offset by interest income of $8,039 and miscellaneous non-operating income of $2,692 for the fiscal year ended September 30, 2019. Other income generally consists of sales of scrap material, the forfeiture of non-refundable deposits and other incidental items.

The Company recorded income taxes of $50 and $50 for the fiscal year ended September 30, 2020 and September 30. 2019. Any other provision for income tax expense was fully offset by a reversal of a portion of the Company's valuation allowance. Any benefit for losses has been subject to a valuation allowance since the realization of the deferred tax benefit is not considered more likely than not. As required by FASB ASC 740 the Company has evaluated the positive and negative evidence bearing upon the realization of its deferred tax assets. The Company has determined that, at this time, it is more likely than not that the Company will not realize all of the benefits of federal and state deferred tax assets, and, as a result, a valuation allowance was established. See Note 7 to the consolidated financial statements.

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Independent Accountant's Review Report

December 4, 2020

To the Board of Directors and Stockholders
of Microwave Filter Company, Inc.

Opinion on the Financial Statements

We have reviewed the accompanying consolidated financial statements of Microwave Filter Company, Inc. and Subsidiaries (the "Company"), which comprise the balance sheets as of September 30, 2020 and 2019, and the related statements of operations, stockholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements. A review includes primarily applying analytical procedures to management's financial data and making inquiries of company management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the consolidated financial statements as a whole. Accordingly, we do not express such an opinion.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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.

Accountant's Responsibility

Our responsibility is to conduct the review engagement in accordance with Statements on Standards for Accounting and Review Services promulgated by the Accounting and Review Services Committee of the American Institute of Certified Public Accountants (AICPA). Those standards require us to perform procedures to obtain limited assurance as a basis for reporting whether we are aware of any material modifications that should be made to the consolidated financial statements for them to be in accordance with accounting principles generally accepted in the United States of America. We believe that the results of our procedures provide a reasonable basis for our conclusion.

We are required to be independent of the Company and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements related to our reviews.

Accountant's Conclusion

Based on our review, we are not aware of any material modifications that should be made to the accompanying consolidated financial statements in order for them to be in accordance with accounting principles generally accepted in the United States of America.

Dannible & McKee, LLP

MICROWAVE FILTER COMPANY, INC.
AND SUBSIDIARIES

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

Microwave Filter Company and Subsidiaries
Consolidated Balance Sheets

	September 30, 2020	September 30, 2019
Assets		
Current assets:		
Cash and cash equivalents	$ 764,169	$ 718,071
Accounts receivable-trade, net of allowance for doubtful accounts of $4,000 and $4,000	411,567	490,784
Inventories, net of obsolete inventory reserve of $533,572 and $491,363	371,643	375,747
Prepaid expenses and other currant assets	66,561	87,389
Total current assets	1,613,940	1,671,991
Property, plant and equipment, net	317,624	272,344
Right-of-use lease asset	9,851	16,060
Total Assets	$ 1,941,415	$ 1,960,395
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 166,318	$ 125,851
Customer deposits	54,182	78,129
Accrued payroll and related expenses	44,282	47,753
Accrued compensated absences	103,711	87,667
Notes Payable - Short Term	55,972	53,456
Other current liabilities	21,672	15,346
Current portion of lease liability	6,493	6,209
PPP loan payable	298,282	0
Total current liabilities	750,912	414,411
Notes Payable - Long Term	109,643	165,615
Lease liability - net of current portion	3,358	9,851
Total other liabilities	113,001	175,466
Total liabilities	863,913	589,877
Stockholders' equity:		
Common stock, $.10 par value. Authorized 5,000,000 shares Issued 4,324,140 in 2020 and 2019, Outstanding 2,578,630 in 2020 and 2,579,179 in 2019	432,414	432,414
Additional paid-in capital	3,248,706	3,248,706
Accumulated deficit	(908,217)	(615,580)
Common stock in treasury, at cost, 1,745,510 shares in 2020 and 1,744,961 shares in 2019	(1,695,401)	(1,695,022)
Total stockholders' equity	1,077,502	1,370,518
Total Liabilities and Stockholders' Equity	$ 1,941,415	$ 1,960,395

See independent accountant's review report and related notes to financial statements.

Microwave Filter Company and Subsidiaries
Consolidated Statements of Operations

	For the Years Ended September 30	
	2020	2019
Net sales	$ 3,107,610	$ 3,920,338
Cost of goods sold	2,030,074	2,279,924
Gross profit	1,077,536	1,640,414
Selling, general and administrative expenses	1,365,215	1,454,044
Operating lease expense	6,804	5,103
(Loss) profit from operations	(294,483)	181,267
Non-operating income (expense)		
Interest income	6,092	8,039
Interest expense	(8,719)	(11,084)
Miscellaneous	4,523	2,692
(Loss) profit before income taxes	(292,587)	180,914
Provision for income taxes	(50)	(50)
NET (LOSS) PROFIT	$ (292,637)	$ 180,864
Per share data:		
Basic and Diluted Earnings (Loss) Per Common Share	$ (0.11)	$ 0.07
Shares used in computing net earnings (loss) per common share:		
Basic and diluted	2,578,880	2,579,392

See independent accountant’s review report and related notes to financial statements.

Microwave Filter Company and Subsidiaries
Consolidated Statements of Stockholders' Equity
For the Years Ended September 30, 2020 and 2019

	Common Stock		Additional Paid-in	Accumulated	Treasury Stock		Total Stockholders'
	Shares	Amt	Capital	Deficit	Shares	Amt	Equity
September 30, 2018 (Audited)	4,324,140	$ 432,414	$ 3,248,706	$ (796,444)	1,744,460	$ (1,694,764)	$ 1,189,912
(Unaudited)							
Net profit				180,864			180,864
Purchase of treasury stock					501	(258)	(258)
September 30, 2019 (Unaudited)	4,324,140	432,414	3,248,706	(615,580)	1,744,961	(1,695,022)	1,370,518
(Unaudited)							
Net loss				(292,637)			(292,637)
Purchase of treasury stock					549	(379)	(379)
September 30, 2020 (Unaudited)	4,324,140	$ 432,414	$ 3,248,706	$ (908,217)	1,745,510	$ (1,695,401)	$ 1,077,502

See independent accountant's review report and related notes to financial statements.

Microwave Filter Company and Subsidiaries
Consolidated Statements of Cash Flows

	For the Years Ended September 30	
	2020	2019
Cash flows from operating activities:		
Net (loss) profit	$ (292,637)	$ 180,864
Adjustments to reconcile net (loss) profit to net cash (used in) provided by operating activities:		
Depreciation	37,020	50,450
Inventory obsolescence provision	42,209	28,077
Changes in assets and liabilities:		
Accounts receivable-trade	79,217	(88,024)
Inventories	(38,105)	(26,221)
Prepaid and other current assets	(16,197)	(32,973)
Accounts payable and customer deposits	16,520	51,764
Accrued payroll, compensated absences and related expenses	12,573	6,260
Other current liabilities	6,326	(13,492)
Net cash (used in) provided by operating activities	(153,074)	156,705
Cash flows from investing activities:		
Capital expenditures	(45,275)	(61,320)
Net cash used in investing activities	(45,275)	(61,320)
Cash flows from financing activities:		
Repayment of note payable	(53,456)	(51,101)
Proceeds from PPP loan	298,282	0
Purchase of treasury stock	(379)	(258)
Net cash provided by (used in) financing activities	244,447	(51,359)
Net increase in cash and cash equivalents	46,098	44,026
Cash and cash equivalents at beginning of year	718,071	674,045
Cash and cash equivalents at end of year	$ 764,169	$ 718,071
Supplemental disclosures of cash flows:		
Cash paid during the year for :		
Interest	$ 8,908	$ 11,263
Taxes	$ 50	$ 50

See independent accountant’s review report and related notes to financial statements.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. Nature of Business

Microwave Filter Company, Inc. (MFC) operates primarily in the United States and principally in one industry. The Company extends credit to business customers based upon ongoing credit evaluations. Microwave Filter Company, Inc. designs, develops, manufactures and sells electronic filters, both for radio and microwave frequencies, to help process signal distribution and to prevent unwanted signals from disrupting transmit or receive operations. Markets served include cable television, television and radio broadcast, satellite broadcast, mobile radio, commercial communications and defense electronics.

b. Basis of Consolidation

The consolidated financial statements include the accounts of Microwave Filter Company, Inc. (MFC) and its wholly-owned subsidiaries, Niagara Scientific, Inc. (NSI) and Microwave Filter International, LTD. (MFI) (dormant); located in Syracuse, New York. All significant intercompany balances and transactions have been eliminated in consolidation.

c. Revenue Recognition

The Company recognizes revenue at a point in time, once control over the finished products has transferred to the customer. Accordingly, revenue is recognized when the customer takes title and assumes the risks and rewards of ownership, generally at the time of shipment. When revenue is recognized in accordance with the above terms, the trade receivable is recorded.

Disaggregation of Revenue

The following tables provide details of revenue by major products group:

Product group	Fiscal 2020	Fiscal 2019
Microwave Filter:		
RF/Microwave	$ 1,471,799	$ 1,634,760
Satellite	1,000,738	1,011,347
Broadcast TV	362,602	820,514
Cable TV	272,338	453,633
Niagara Scientific	133	84
Total	$ 3,107,610	$ 3,920,338
Sales backlog at 9/30	$ 631,764	$ 827,981

d. Adoption of ASU 2016-02 “Leases”

On October 1, 2018, the Company early adopted ASU 2016-02 “Leases” and all subsequent amendments to the ASU (collectively, “Topic 842”), which create recognition of assets and liabilities that arise from leases. The Company’s existing lease for office equipment is classified as an operating lease and is within the scope of Topic 842. Refer to Note 6, Operating Lease Commitments, for further discussion on the Company’s accounting policies for leases. As a result of the adoption, the lease term is in excess of 12 months was recognized on the balance sheet with a right-of-use asset and liability. Additionally, certain accounts in the prior year financial statements have been reclassified for comparative purposes to conform with the presentation in the current year consolidated financial statements. The impact on the consolidated financial statements and opening fiscal 2019 stockholders’ equity was not material.

e. Product Warranty

The Company has established a warranty reserve which provides for the estimated cost of product returns based upon historical experience and any known conditions or circumstances. No revenues are recognized in connection with the performance of the warranty repair or fulfillment function. The warranty obligation is affected by product that does not meet specifications and performance requirements and any related costs of addressing such matters. Products must be returned within one year of the date of purchase. The warranty liability was insignificant at September 30, 2020 and September 30, 2019.

f. Cash and Cash Equivalents

The Company's financial instruments that are exposed to concentrations of credit risk consist primarily of cash and accounts receivable. Cash and cash equivalents consist of cash in banks and money market funds. The Company considers all highly liquid investments with original maturities of three months or less to be cash equivalents. The Company's cash is held at federally insured institutions and balances may periodically exceed insured limits. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk with respect to cash. The Company also routinely assesses the financial strength of its customers and, as a consequence, believes that its trade accounts receivable credit risk exposure is limited.

g. Trade Accounts Receivable and Allowance for Doubtful Accounts

Trade accounts receivable are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the Company's existing accounts receivable. The Company reviews its allowance for doubtful accounts monthly. Past due balances are reviewed individually for collectability. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. The Company does not have any off-balance-sheet credit exposure related to its customers.

h. Inventories and Reserve for Obsolescence

Inventories are stated at the lower of cost determined on the first-in, first-out method or net realizable value.

Net realizable value is determined as the estimated selling price in the normal course of business minus the cost of completion, disposal and transportation.

The Company records a reserve for obsolete or excess inventory. The Company considers inventory quantities greater than a three year supply based on current year activity as well as any additional specifically identified inventory to be excess. The Company also provides for the total value of inventories that are determined to be obsolete based on criteria such as customer demand and changing technologies.

i. Research and Development

Costs in connection with research and development, which amount to $371,612 and $372,702 for the fiscal years 2020 and 2019, respectively, are charged to operations as incurred.

j. Advertising

The Company expenses advertising costs as incurred. Advertising expense was approximately $23,700 and $24,400 for the years ended September 30, 2020 and 2019, respectively, and is included in the selling, general and administrative expenses in the consolidated statements of operations.

k. Property, Plant and Equipment

Property, plant and equipment are recorded at cost. Depreciation is provided using the straight-line method over the estimated useful lives of the respective assets. Buildings and building improvements are depreciated over an estimated service life of 10 to 30 years. Machinery and equipment are depreciated over an estimated useful life of 3 to 10 years. Office equipment and fixtures are depreciated over an estimated useful life of 3 to 10 years. At the time of sale or retirement, the cost and accumulated depreciation are removed from the respective accounts and the resulting gain or loss is recognized in income.

l. Income Taxes

The Company accounts for income taxes under FASB ASC 740-10. Deferred tax assets and liabilities are based on the difference between the financial statement and income tax basis of assets and liabilities as measured by the enacted tax rates which are anticipated to be in effect when these differences reverse. The deferred tax provision is the result of the net change in the deferred tax assets and liabilities. A valuation allowance is established when it is necessary to reduce deferred tax assets to amounts expected to be realized. The Company has provided a full valuation allowance against its deferred tax assets.

The Company follows FASB ASC 740-10, which clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements and prescribes a recognition threshold and measurement attributes for financial statement disclosure of tax positions taken or expected to be taken on a tax return. Additionally, it provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The Company will include interest on income tax liabilities in interest expense and penalties in operations if such amounts arise. The Company determined it has no uncertain tax positions and therefore no amounts are recorded.

m. Earnings Per Share

The Company presents basic earnings per share ("EPS"), computed based on the weighted average number of common shares outstanding for the period, and when applicable diluted EPS, which gives the effect to all dilutive potential shares outstanding (i.e. options) during the period after restatement for any stock dividends. There were no dividends declared during the fiscal year ended September 30, 2020 and 2019. Profit (loss) used in the EPS calculation is net profit (loss) for each year. There were no dilutive potential shares outstanding for the years ended September 30, 2020 and 2019.

n. Fair Value of Financial Instruments

The carrying value of the Company cash and cash equivalents, accounts receivable and accounts payable approximate fair value because of the short maturity of those instruments. The carrying value of the Company's note payable approximates its fair value.

The Company currently does not trade in or utilize derivative financial instruments.

o. Miscellaneous Non-operating Income

Miscellaneous non-operating income generally consists of sales of scrap material and the forfeiture of non-refundable deposits and other incidental items.

p. Use of Estimates

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

q. Impairment of Long-Lived Assets

The carrying values of long-lived assets other than goodwill are generally evaluated for impairment only if events or changes in facts and circumstances indicate that carrying values may not be recoverable. Any impairment determined would be recorded in the current period and would be measured by comparing the fair value of the related asset to its carrying value. Fair value is generally determined by identifying estimated undiscounted cash flows to be generated by those assets. No impairments have been recorded for the fiscal years ended September 30, 2020 and 2019.

r. Risks and Uncertainties

During fiscal 2020, local, U.S., and world governments have encouraged self-isolation to curtail the spread of the global pandemic, Coronavirus Disease (COVID-19), by mandating work stoppage in many sectors and imposing limitations on travel and size and duration of group meetings. Most industries are experiencing disruption to business operations and the impact of reduced consumer spending. There is unprecedented uncertainty surrounding the duration of the pandemic, its potential economic ramifications, and any government actions to mitigate them. During the COVID-19 pandemic, the Company's services have been essential in nature. As the situation evolves, the Company continues to closely monitor the impact of the COVID-19 pandemic on all aspects of the business, including how it impacts customers, subcontractors, suppliers, vendors and employees, in addition to how the COVID-19 pandemic impacts the Company's ability to provide services to their customers. We believe the ultimate impact of the COVID-19 pandemic on operating results, cash flows and financial condition is likely to be determined by factors which are uncertain, unpredictable and outside of the Company's control. The situation surrounding COVID-19 remains fluid, and if disruptions do arise, they could further materially adversely impact business.

s. Subsequent Events

Management has evaluated subsequent events though December 4, 2020, the date which the consolidated financial statements were available for issue.

2. INVENTORIES

Inventories net of provision for obsolescence consisted of the following:

	September 30	
	2020	2019
Raw materials and stock parts	$ 310,664	$ 333,638
Work-in-process	27,783	16,752
Finished goods	33,196	25,357
	$ 371,643	$ 375,747

The Company's reserve for obsolescence equaled $533,572 at September 30, 2020 and $491,363 at September 30, 2019.

3. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consisted of the following:

	September 30 2020	September 30 2019
Land	$ 143,000	$ 143,000
Building and improvements	2,057,549	1,983,499
Machinery and equipment	3,510,175	3,501,925
Office equipment and fixtures	1,925,598	1,925,598
	7,636,322	7,554,022
Less: Accumulated depreciation	7,318,698	7,281,678
Property, plant and equipment, net	$ 317,624	$ 272,344
Depreciation expense	$ 37,020	$ 50,450

4. NOTES PAYABLE

On July 2, 2013, Microwave Filter Company, Inc. (the "Company") entered into a Ten Year Term Loan with KeyBank National Association in the amount of Five Hundred Thousand and No/100 Dollars ($500,000.00). The amount of all advances outstanding together with accrued interest thereon shall be due and payable on July 2, 2023 ("Maturity"). The Company shall pay interest on the outstanding principal balance of this Note at the rate per annum equal to 4.5%. The net proceeds from the Term Loan will be available to provide working capital as needed. The total amount outstanding as of September 30, 2020 and 2019 was $165,615 and $219,072 respectively. Interest accrued as of September 30, 2020 and 2019 was $580 and $767 respectively.

The Company has secured this Note by: (a) a Mortgage, Assignment of Rents, Security Agreement and Fixture Filing which creates a 1st lien on real property situated in the Town of Dewitt, County of Onondaga, and State of New York and known as 6743 Kinne Street, East Syracuse, New York; (b) a General Assignment of Rents and Leases; (c) an Environmental Compliance and Indemnification; and (d) such other security as may now or hereafter be given to Lender as collateral for the loan. The future obligations of the loan are as follows:

Year Ended September 30,	Principal Payments	Interest Payments	Total Payments
2021	$ 55,972	$ 6,392	$ 62,364
2022	58,680	3,684	62,364
2023	50,963	1,007	51,970
	$ 165,615	$ 11,083	$ 176,698

The Company is required to comply with a loan covenant requiring submission to the Bank of audited financial statements subsequent to year end. The Company has received a waiver of non-compliance with this covenant.

On May 5, 2020, the Company qualified for and received a loan pursuant to the Paycheck Protection Program, a program implemented by the U.S. Small Business Administration under the Coronavirus Aid, Relief, and Economic Security Act, from a qualified lender (the “PPP Lender”), for an aggregate principal amount of approximately $298,000 (the "PPP Loan"). The PPP Loan bears interest at a fixed rate of 1.0% per annum, with the first six months of interest deferred, has a term of five years, and is unsecured and guaranteed by the U.S. Small Business Administration. The principal amount of the PPP Loan is subject to forgiveness under the Paycheck Protection Program upon the Company’s request to the extent that the PPP Loan proceeds are used to pay expenses permitted by the Paycheck Protection Program, including payroll costs, covered rent and mortgage obligations, and covered utility payments incurred by the Company. The Company intends to apply for forgiveness of the PPP Loan with respect to these covered expenses, accordingly, the PPP loan has been included in current liabilities. To the extent that all or part of the PPP Loan is not forgiven, the Company will be required to pay interest on the PPP Loan at a rate of 1.0% per annum. The terms of the PPP Loan provide for customary events of default including, among other things, payment defaults, breach of representations and warranties, and insolvency events. The PPP Loan may be accelerated upon the occurrence of an event of default.

5. PROFIT SHARING AND 401-K PLANS

The Company maintains both a non-contributory profit sharing plan and a contributory 401-K plan for all employees over the age of 21 with one year of service. Annual contributions to the profit sharing plan are determined by the Board of Directors and are made from current or accumulated earnings, while contributions to the 401-K plan were matched at a rate of 100% of an employee’s first 6% of contributions during fiscal 2020. The maximum corporate match was 6% of an employee’s compensation during fiscal 2020.

The Company’s matching contributions to the 401-K plan for the years ended September 30, 2020 and 2019 were $64,869 and $67,670, respectively. Additionally, the Company may make discretionary contributions to the non-contributory profit sharing plan. These contributions were $0 in 2020 and 2019.

6. OPERATING LEASE COMMITMENTS

The Company has entered into an operating lease arrangement for office equipment in Syracuse, NY beginning January 1, 2019. During the years ended September 30, 2020 and 2019, rent expenses were recognized with the operating lease as fixed rent expense of $6,804 and $5,103, respectively.

Amounts recognized as a right-of-use asset related to the operating lease in the right-of-use lease asset, while related lease liabilities are shown as current liabilities and long-term liabilities. As of September 30, 2020 and 2019, right-of-use lease assets and lease liabilities relating to the operating lease were as follows:

	2020	2019 As adjusted
Right-of-use lease asset	$ 9,851	$ 16,060
Operating lease liabilties:		
Current portion of lease liabilities	6,493	6,209
Lease liability - net of current portion	3,358	9,851

During the years ended September 30, 2020 and 2019, the Company had the following cash and non –cash activities associated with operating leases:

	2020	2019 As adjusted
Cash paid for amounts included in the measurement of lease liabilities:		
Operating cash flows from operating leases	$ 6,804	$ 5,103

No non-cash activity during the period. The establishment of the right-of-use asset and corresponding lease liabilities in both 2020 and 2019 did not require or use cash, and accordingly have been excluded from the statements of cash flows.

Minimum rental commitments at September 30, 2020 for this lease are:

Year Ended September 30	Lease Payments
2021	$ 6,804
2022	3,402
	10,206
Amount representing interest	(355)
	$ 9,851

As of September 30, 2020 and 2019, the weighted-average remaining lease term for the operating lease is 1.5 and 2.5 years, respectively.

Because the Company does not have access to the rate implicit in the lease, the incremental borrowing rate was utilized as the discount rate. The weighted average discount rate associated with the operating lease as of September 30,2020 and 2019 is 4.50%.

7. INCOME TAXES

The components of the provision for income taxes in the accompanying consolidated statements of operations are as follows:

	Year Ended September 30, 2020	2019
Currently payable:		
Federal	$ 0	$ 0
State	50	50
Deferred (credit)	0	0
	$ 50	$ 50

The components of the provision for income taxes differs from the amount that would result from applying the federal statutory rate for the periods ended September 30, 2020 and 2019 is as follows:

	Year ended September 30,			
	2020		2019	
	Amount	%	Amount	%
Statutory tax rate	$ (61,454)	(21.0 %)	$ 37,992	21.0 %
Research and development tax credits	(22,031)	(7.5 %)	(18,412)	(10.2 %)
Valuation allowance change	20,846	7.1 %	(19,580)	(10.8 %)
Permanent differences	62,639	21.4 %	0	0.0 %
	$ 0	0.0 %	$ 0	0.0 %

The temporary differences which give rise to deferred tax assets and (liabilities) at September 30 are as follows:

	2020	2019
Inventory	$ 115,760	$ 106,771
Accrued warranty	2,625	2,625
Accrued vacation	18,629	14,420
Accounts receivable	885	885
Accelerated depreciation	25,490	24,501
Research and development tax credit carryforward	352,138	323,769
AMT credit carryforward	37,521	37,521
NOL carryforward	165,872	187,584
Valuation allowance	(718,920)	(698,076)
Net deferred tax assets	$ 0	$ 0

As required by FASB ASC 740 the Company has evaluated the positive and negative evidence bearing upon the realization of its net deferred tax assets. The Company has determined that, at this time, it is more likely than not that the Company will not realize all of the benefits of Federal and state net deferred tax assets, and, as a result, a valuation allowance was established. The research and development tax credit carryforwards and NOL carryforwards generated through September 30, 2020, of approximately $352,000 and $519,000 expire at various times through 2038. Pursuant to the ACT, any of the Company's newly-generated Federal NOL carryforwards can be carried forward indefinitely, while being limited to 80% of taxable income (determined without regard to the deduction.) Pursuant to the CARES Act, there is no limit to the usage of the Company's NOL through tax years ending before January 1, 2021. For tax years beginning after December 31, 2020, the NOL's will again be limited to 80% of taxable income (determined without regard to the deduction.) As of September 30, 2020, the Company's Federal AMT credit carryforward of approximately $35,000 is available in any year prior to 2023, in an amount equal to 50% (100% for tax years beginning in 2022) of the excess minimum tax credit for the tax year, over the amount of the credit allowable for the year against the regular tax liability. The Company is currently open to audit under the statute of limitations by the Internal Revenue Service for the fiscal years September 30, 2017 through September 30, 2020. The Company has no uncertain tax positions. As of September 30, 2020 and 2019, there is no accrual for interest or penalties related to uncertain tax positions.

8. INDUSTRY SEGMENT DATA

The Company's primary business segment involves the operations of Microwave Filter Company, Inc. (MFC) which designs, develops, manufactures and sells electronic filters, both for radio and microwave frequencies, to help process signal distribution and to prevent unwanted signals from disrupting transmit or receive operations.

9. SIGNIFICANT CUSTOMERS

Sales to one customer s represented 38.1% of total sales for the fiscal year ended September 30, 2020 compared to sales to two customers who represented 53.5% of total sales for the fiscal year ended September 30, 2019. A loss of this customer or programs related to this customer could materially impact the Company.

10. LEGAL MATTERS

None.

11. LIQUIDITY AND CAPITAL RESOURCES

MFC defines liquidity as the ability to generate adequate funds to meet its operating and capital needs. The Company's primary source of liquidity has been funds provided by operations and its existing cash balances.

	September 30	
	2020	2019
Cash & cash equivalents	$ 764,169	$ 718,071
Working capital	$ 863,028	$ 1,257,580
Current ratio	2.15 to 1	4.03 to 1
Long-term debt	$ 113,001	$ 175,466

Cash and cash equivalents increased $46,098 to $764,169 at September 30, 2020 when compared to $718,071 at September 30, 2019. The increase was a result of $153,074 in net cash used in operating activities, $45,275 in net cash used for capital expenditures, $53,456 in net cash used for repayment of a note payable, $298,282 in proceeds from a PPP loan and $379 in net cash used to purchase treasury stock.

Net cash provided by operating activities fluctuates between periods primarily as a result of differences in sales and net income and the timing of the collection of accounts receivable, purchase of inventory, and payment of accounts payable.

The $45,275 in fixed asset purchases consisted of $37,025 to replace part of the roof and $8,250 used to purchase tooling.

During 2020, the Company received a loan totaling $298,282 from the Small Business Administration (SBA) under the Paycheck Protection Program of the Coronavirus Aid, Relief and Economic Security (CARES) Act. Some or all of the loan may be forgiven if certain criteria are met, accordingly, the PPP loan has been included in current liabilities, see Note 4. Otherwise, the loan is unsecured, has a deferment on payment for 6 months after a decision on forgiveness has been made, then the loan is payable over a negotiated period of time, and bears interest at 1%.

On July 2, 2013, Microwave Filter Company, Inc. (the "Company") entered into a Ten Year Term Loan with KeyBank National Association in the amount of Five Hundred Thousand and No/100 Dollars ($500,000.00). The amount of all advances outstanding together with accrued interest thereon shall be due and payable on July 2, 2023 ("Maturity"). The Company shall pay interest on the outstanding principal balance of this Note at the rate per annum equal to 4.5%. The net proceeds from the Term Loan will be available to provide working capital as needed. The total amount outstanding as of September 30, 2020 and 2019 was $165,615 and $219,071, respectively.

The Company has secured this Note by: (a) a Mortgage, Assignment of Rents, Security Agreement and Fixture Filing which creates a 1st lien on real property situated in the Town of Dewitt, County of Onondaga, and State of New York and known as 6743 Kinne Street, East Syracuse, New York; (b) a General Assignment of Rents and Leases; (c) an Environmental Compliance and Indemnification; and (d) such other security as may now or hereafter be given to Lender as collateral for the loan.

Management believes that its working capital requirements for the foreseeable future will be met by its existing cash balances, future cash flows from operations and its current credit arrangements.

Off-Balance Sheet Arrangements

At September 30, 2020 and 2019, the Company did not have any unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which might have been established for the purpose of facilitating off-balance sheet arrangements.