

Optex Systems Holdings Inc  
Form 424B3  
March 23, 2017

**Filed pursuant to Rule 424(b)(3)**

**Registration No. 333-212654**

**PROSPECTUS SUPPLEMENT NO. 1**

**(to post-effective amendment no. 2 to prospectus dated February 28, 2017)**

**Optex Systems Holdings, Inc.**

2,291,900 Class A units consisting of common stock and warrants and 400 Class B units consisting of shares of Series C convertible preferred stock and warrants (and an aggregate of 5,625,500 shares of common stock underlying (i) shares of Series C convertible preferred stock and (ii) warrants)

This prospectus supplement relates to Registration Statements on Form S-1 (File Nos. 333-212654 and 333-213255) declared effective by the Securities and Exchange Commission on or about August 22, 2016 and August 23, 2016 respectively, as amended by that certain Post-Effective Amendment No. 1 on Form S-1 declared effective by the SEC on or about January 17, 2017 and as further amended by that certain Post-Effective Amendment No. 2 on Form S-1 declared effective by the SEC on or about February 28, 2017 the following:

2,291,900 Class A units consisting of common stock and warrants and 400 Class B units consisting of shares of Series C convertible preferred stock and warrants (and an aggregate of 5,625,500 shares of common stock underlying (i) shares of Series C convertible preferred stock and (ii) warrants)

**This prospectus supplement relates to** Registration Statements on Form S-1 (File Nos. 333-212654 and 333-213255) declared effective by the Securities and Exchange Commission on or about August 22, 2016 and August 23, 2016 respectively, **and does not cover securities beyond those covered by the existing Registration Statement. There are no additional securities being offered under this prospectus supplement – this is merely a document required under the securities laws to update information previously filed in the original prospectus and prior prospectus supplements thereto.**

If all of the warrants are exercised for cash, we will receive a total of \$6,187,800 in gross proceeds, which we expect to use for general corporate purposes. We cannot assure you that any warrants will be exercised for cash. The selling

stockholders may offer and sell the shares covered by the prospectus at prevailing prices quoted on the OTCQB or at privately negotiated prices. The selling stockholders may sell the shares directly or through underwriters, brokers or dealers. The selling stockholders will bear any applicable sales commissions, transfer taxes and similar expenses. We will pay all other expenses incident to the registration of the shares. See “Plan of Distribution” in the prospectus for more information on this topic.

We are filing this prospectus supplement to supplement and amend the information previously included in the prospectus, with the information contained in our Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on February 22, 2017. Accordingly, we have attached our Quarterly Report on Form 10-Q to this prospectus supplement. You should read this prospectus supplement together with the prospectus and any prior prospectus supplements thereto, which is to be delivered with this prospectus supplement.

Our common stock is traded on the OTCQB under the symbol “OPXS.” On February 21, 2017, the last reported sale price of our common stock on the OTCQB was \$0.68 per share.

**Investing in our securities involves significant risks, including those set forth in the “Risk Factors” section of the prospectus beginning at page 8.**

NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED OF THESE SECURITIES OR DETERMINED IF THE PROSPECTUS OR THIS PROSPECTUS SUPPLEMENT IS TRUTHFUL OR COMPLETE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The date of this prospectus supplement is March 23, 2017

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

**FORM 10-Q**

**<sup>x</sup> QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934**

**For the quarterly period ended January 1, 2017**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_.**

**OPTEX SYSTEMS HOLDINGS, INC.**

(Exact Name of Registrant as Specified in Charter)

Delaware	<b>000-54114</b>	<b>90-0609531</b>
(State or other jurisdiction of incorporation)	(Commission File Number)	(IRS Employer Identification No.)

1420 Presidential Drive, Richardson, TX	75081-2439
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (972) 764-5700

Check whether the issuer (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for such shorter period that the issuer was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No ..

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

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer  Smaller Reporting Company

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

Indicate by check mark whether the registrant is a shell company as defined in Rule 12b-2 of the Exchange Act.

Yes  No

State the number of shares outstanding of each of the issuer’s classes of common equity, as of February 20, 2017:  
8,190,101 shares of common stock.

**OPTEX SYSTEMS HOLDINGS, INC.**

**FORM 10-Q**

**For the period ended January 1, 2017**

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**Part 1. Financial Information**

**Item 1. Consolidated Financial Statements**

OPTEX SYSTEMS HOLDINGS, INC.

UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

AS OF JANUARY 1, 2017

CONSOLIDATED BALANCE SHEETS AS OF JANUARY 1, 2017 (UNAUDITED) AND OCTOBER 2, 2016 F-1

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**Optex Systems Holdings, Inc.****Condensed Consolidated Balance Sheets**

	(Thousands, except share and per share data)	
	January 1, 2017 (Unaudited)	October 2, 2016
<b>ASSETS</b>		
Cash and Cash Equivalents	\$ 2,069	\$ 2,568
Accounts Receivable, Net	1,858	2,095
Net Inventory	6,585	6,214
Prepaid Expenses	75	120
Current Assets	10,587	10,997
Property and Equipment, Net	1,698	1,651
Other Assets		
Prepaid Royalties - Long Term	83	90
Security Deposits	23	23
Other Assets	106	113
Total Assets	\$ 12,391	\$ 12,761
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities		
Accounts Payable	\$ 393	\$ 706
Accrued Expenses	992	810
Accrued Warranties	28	28
Customer Advance Deposits	487	559
Credit Facility	300	300
Current Liabilities	2,200	2,403
Warrant Liability	2,688	3,118
Total Liabilities	4,888	5,521
Stockholders' Equity	-	-

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Preferred Stock Series B (\$0.001 par 1,010 authorized, 0 and 994 issued and outstanding, respectively)		
Preferred Stock Series C (\$0.001 par 400 authorized, 342 and 360 issued and outstanding, respectively)	-	-
Common Stock – (\$0.001 par, 2,000,000,000 authorized, 8,144,302 and 8,266,601 shares issued and outstanding, respectively)	8	8
Additional Paid-in-capital	26,788	26,879
Accumulated Deficit	(19,293	) (19,647
		)
Stockholders' Equity	7,503	7,240
Total Liabilities and Stockholders' Equity	\$ 12,391	\$ 12,761

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

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**Optex Systems Holdings, Inc.****Condensed Consolidated Statements of Operations****(Unaudited)**

	(Thousands, except share and per share data)	
	Three months ended	
	January 1, 2017	December 27, 2015
Revenue	\$ 3,512	\$ 3,213
Cost of Sales	2,740	2,746
Gross Margin	772	467
General and Administrative Expense	844	694
Operating Loss	(72 )	(227 )
Gain on Change in Fair Value of Warrants	430	-
Interest Expense	(4 )	(18 )
Other Income (Expense)	426	(18 )
Income (Loss) Before Taxes	354	(245 )
Deferred Income Taxes (Benefit)	-	-
Net income (loss) applicable to common shareholders	\$ 354	\$ (245 )
Basic income (loss) per share	\$ 0.04	\$ (0.75 )
Weighted Average Common Shares Outstanding - basic	8,175,309	326,122
Diluted income (loss) per share	0.04	(0.75 )
Weighted average common shares outstanding - Diluted	9,600,309	326,122

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



**Optex Systems Holdings, Inc.**  
**Condensed Consolidated Statements of Cash Flows**

**(Unaudited)**

	(Thousands)	
	Three months ended	
	January 1, 2017	December 27, 2015
Cash flows from operating activities:		
Net (income) loss	\$ 354	\$ (245 )
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	83	86
(Gain) on change in fair value of warrants	(430 )	-
Noncash interest expense	-	(6 )
Stock compensation expense	64	24
(Increase) decrease in accounts receivable	82	1,636
(Increase) decrease in inventory	(371 )	(150 )
(Increase) decrease in prepaid expenses	45	(94 )
Increase (decrease) in accounts payable and accrued expenses	(131 )	63
Decrease in prepaid royalties - long term	7	7
Increase (decrease) in customer advance deposits	(72 )	(99 )
Increase (decrease) in accrued estimated loss on contracts	-	-
Total adjustments	(723 )	1,467
Net cash (used in) provided by operating activities	(369 )	1,222
Cash flows to investing activities		
Purchases of property and equipment	(130 )	-
Net cash used in investing activities	(130 )	-
Cash flows to financing activities		
Proceeds to credit facility (net)	-	(500 )
Net cash used in financing activities	-	(500 )
Net (decrease) increase in cash and cash equivalents	(499 )	722
Cash and cash equivalents at beginning of period	2,568	683
Cash and cash equivalents at end of period	\$ 2,069	\$ 1,405
Supplemental cash flow information:		
Exchange of common stock for non-trade accounts receivable	\$ 155	\$ -
Exchange of preferred stock for common stock	90	-
Cash paid for interest	4	24

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

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## **Note 1 - Organization and Operations**

Concurrent with the filing of the Optex Systems Holdings, Inc.'s Form 10-Q for the three months ending January 1, 2017, Optex Systems Holdings, Inc. (the "Company") has filed an Amendment No. 1 to its Annual Report on Form 10-K for the year ended October 2, 2016, which was originally filed with the Securities and Exchange Commission on December 23, 2016. The Company has restated its consolidated financial statements for the year ended October 2, 2016 to correct the manner in which the Company recorded 4,125,200 warrants that were issued in conjunction with common stock and Series C preferred shares pursuant to a public offering on August 26, 2016. These restatements have been reflected in the amended financial statements contained herein. The errors which were included in the December 23, 2016 Form 10-K Annual Report were incurred during the final month of the 2016 fiscal year and were subsequently identified in the following quarter prior to submission of any interim reports with the Securities and Exchange Commission and as such, the restated balances are limited to the Annual Report Form 10-K for fiscal year ending October 2, 2016.

Optex Systems Holdings manufactures optical sighting systems and assemblies, for the U.S. Department of Defense, foreign military applications and commercial markets. Its products are installed on a variety of U.S. military land vehicles, such as the Abrams and Bradley fighting vehicles, light armored and advanced security vehicles, and have been selected for installation on the Stryker family of vehicles. Optex Systems Holdings also manufactures and delivers numerous periscope configurations, rifle and surveillance sights and night vision optical assemblies. Optex Systems Holdings' products consist primarily of build to customer print products that are delivered both directly to the military and to other defense prime contractors or commercial customers.

Optex Systems Holdings' operations are based in Dallas and Richardson, Texas in leased facilities comprising 93,967 square feet. As of January 1, 2017, Optex Systems Holdings operated with 90 full-time equivalent employees.

Sileas is the majority owner (parent) of Optex Systems Holdings, owning approximately 53.3% of the issued and outstanding equity interests in Optex Systems Holdings. The financial statements of Optex Systems Holdings represent subsidiary statements and do not include the accounts of its majority owner.

Optex Systems Holdings, Inc. has two reportable segments which include Optex Systems (OPX)-Richardson, and Applied Optics Center (AOC) – Dallas. The accounting policies for each segment are the same as those described in the summary of significant accounting policies. Optex Systems Holdings, Inc. evaluates performance based on profit and loss from operations before income taxes excluding nonrecurring gains and losses.

### **Optex Systems (OPX) – Richardson, Texas**

Optex Systems, Inc. manufactures optical sighting systems and assemblies, primarily for Department of Defense applications. Its products are installed on various types of U.S. military land vehicles, such as the Abrams and Bradley fighting vehicles, light armored and armored security vehicles and have been selected for installation on the Stryker family of vehicles. Optex Systems, Inc. also manufactures and delivers numerous periscope configurations, rifle and surveillance sights and night vision optical assemblies. We have capabilities which include machining, bonding, painting engraving and assembly and can perform both optical and environmental testing in-house. Optex Systems, Inc. products consist primarily of build-to-customer print products that are delivered both directly to the armed services and to other defense prime contractors. Optex Systems in Richardson is both a prime and sub-prime contractor to the Department of Defense. Sub-prime contracts are typically issued through major defense contractors such as General Dynamics Land Systems, Raytheon Corp., BAE, NorcaTec and others. Optex Systems is also a military supplier to foreign governments such as Israel, Australia and NAMSA and South American countries and as a subcontractor for several large U.S. defense companies serving foreign governments.

During the three months ended January 1, 2017, 86% of Optex Systems – Richardson revenues were in support of prime and subcontracted military customers. The Optex Systems segment serves domestic military customers, 74%, foreign military customers, 12%, and domestic commercial customers of 14%. The Optex Systems segment revenue for the three months ending January 1, 2017 was derived from external customers consisting of General Dynamics, 22%, the U.S. government, 26%, Oasis Advanced Engineering 14%, BAE Systems, 10% and other external customers, 28%.

Optex Systems is located in Richardson, Texas, with leased premises consisting of approximately 49,100 square feet. As of January 1, 2017, the Richardson facility operated with 52 full time equivalent employees in a single shift operation. Optex Systems in Richardson serves as the home office for both the Optex Systems (OPX) and Applied Optics Center (AOC) segments.

### **Applied Optics Center (AOC) – Dallas**

On November 3, 2014, Optex Systems, Inc. entered into a Purchase Agreement with L-3 pursuant to which Optex Systems, Inc. purchased from L-3 the assets comprising L-3's Applied Optics Center Products Line. Applied Optics Center is engaged in the production, marketing and sales of precision optical assemblies and components which utilize thin film coating technologies. Most of the AOC products and services are directly related to the deposition of thin-film coatings. AOC is both a prime and sub-prime contractor to the Department of Defense. Sub-prime contracts are typically issued through major defense contractors such as General Dynamics Land Systems, Raytheon Corp., L-3 Communications, Harris Corporation and others. AOC also creates a new sector of opportunity for commercial products. Globally, commercial optical products use thin film coatings to create product differentiation and performance levels. These coatings can be used for redirecting light (mirrors), blocking light (laser protection), absorbing select light (desired wavelengths), and many other combinations. They are used in telescopes, rifle scopes, binoculars, microscopes, range finders, protective eyewear, photography, etc. The Applied Optics Center is a key supplier to Nightforce Optics, Inc. and provides optical assembly components to their markets of interest in commercial sporting optics and select military optics. Given this broad potential, the commercial applications are a key opportunity going forward. The Applied Optics Center segment also serves as the key supplier of the laser coated filters used in the production of periscope assemblies at the Optex Systems Richardson segment.

The Applied Optics Center serves primarily domestic U.S. customers. During the three months ended January 1, 2017, sales to commercial customers represent 59% and military sales to prime and subcontracted customers represent 17% of the total segment revenue. Intersegment sales to Optex Systems – Richardson, comprised 24% of the total segments revenue and was primarily in support of military contracts. The Applied Optics Center external customer revenue for the three months ending January 1, 2017 was derived from L3 Communications, 14%, Nightforce Optics, Inc., 74% and other external customers, 12%.

The Applied Optics Center (AOC), is located in Dallas, Texas with leased premises consisting of approximately 44,867 square feet of space. As of January 1, 2017, AOC operated with 38 full time equivalent employees in a single shift operation.

## **Note 2 - Accounting Policies**

### **Basis of Presentation**

***Principles of Consolidation:*** The consolidated financial statements include the accounts of Optex Systems Holdings and its wholly-owned subsidiary, Optex Systems, Inc. All significant inter-company balances and transactions have been eliminated in consolidation.

The condensed consolidated financial statements of Optex Systems Holdings included herein have been prepared by Optex Systems Holdings, without audit, pursuant to the rules and regulations of the SEC. Certain information and footnote disclosures normally included in financial statements prepared in conjunction with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although Optex Systems Holdings believes that the disclosures are adequate to make the information presented not misleading.

These condensed consolidated financial statements should be read in conjunction with the annual audited consolidated financial statements and the notes thereto included in the Optex Systems Holdings' Form 10-K/A for the year ended October 2, 2016 and other reports filed with the SEC.

The accompanying unaudited interim consolidated financial statements reflect all adjustments of a normal and recurring nature which are, in the opinion of management, necessary to present fairly the financial position, results of operations and cash flows of Optex Systems Holdings for the interim periods presented. The results of operations for these periods are not necessarily comparable to, or indicative of, results of any other interim period or for the fiscal year taken as a whole. Certain information that is not required for interim financial reporting purposes has been omitted.



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

**Inventory:** Inventory is recorded at the lower of cost or market value, and adjusted, as necessary, for decreases in valuation and obsolescence. Adjustments to the valuation and obsolescence reserves are made after analyzing market conditions, current and projected sales activity, inventory costs and inventory balances to determine appropriate reserve levels. Cost is determined using the first-in first-out method. Under arrangements by which progress payments are received against certain contracts, the customer retains a security interest in the undelivered inventory identified with these contracts. Payments received for such undelivered inventory are classified as unliquidated progress payments and deducted from the gross inventory balance. As of January 1, 2017 and October 2, 2016, there were no unliquidated progress payments. As of January 1, 2017 and October 2, 2016, inventory included:

	(Thousands)	
	January 1, 2017	October 2, 2016
Raw Material	\$4,518	\$ 4,655
Work in Process	3,152	2,830
Finished Goods	566	380
Gross Inventory	\$8,236	\$ 7,865
Less: Inventory Reserves	(1,651)	(1,651)
Net Inventory	\$6,585	\$ 6,214

Net inventory increased by \$371 thousand during the three months ending January 1, 2017 in support of contracts deliverable over the next six months.

**Revenue Recognition:** Optex Systems Holdings recognizes revenue based on the modified percentage of completion method utilizing the units-of-delivery method, in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 605-35:

The units-of-delivery method recognizes as revenue the contract price of units of a basic production product delivered during a period and as the cost of earned revenue the costs allocable to the delivered units. Costs allocable to undelivered units are reported in the balance sheet as inventory or work in progress. The method is used in circumstances in which an entity produces units of a basic product under production-type contracts in a continuous or sequential production process to buyers' specifications.

Optex Systems Holdings contracts are fixed price production type contracts whereby a defined order quantity is delivered to the customer during a continuous or sequential production process tailored to the buyer's specifications (build to print). Optex Systems Holdings' deliveries against these contracts generally occur in monthly increments across fixed delivery periods spanning from 3 to 36 months.

**Customer Advance Deposits:** Customer advance deposits represent amounts collected from customers in advance of shipment or revenue recognition, which relate to undelivered product or other cash in advance payment terms. As of January 1, 2017, Optex Systems, Inc. had a balance of \$0.5 million in short term customer advance deposits for materials purchased in support of deliveries to occur within the next twelve months.

**Stock-Based Compensation:** FASB ASC 718 establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services, but primarily focuses on transactions whereby an entity obtains employee services for share-based payments. FASB ASC 718 requires that the compensation cost relating to share-based payment transactions be recognized in the consolidated financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. It also addresses transactions in which an entity incurs liabilities in exchange for goods or services that are based on the fair value of the entity's equity instruments or that may be settled by the issuance of those equity instruments.

The Company's accounting policy for equity instruments issued to consultants and vendors in exchange for goods and services follows the provisions of FASB ASC 505-50. The measurement date for the fair value of the equity instruments issued is determined at the earlier of (i) the date at which a commitment for performance by the consultant or vendor is reached or (ii) the date at which the consultant or vendor's performance is complete. In the case of equity instruments issued to consultants, the fair value of the equity instrument is recognized over the term of the consulting agreement. Stock-based compensation related to non-employees is accounted for based on the fair value of the related stock or options or the fair value of the services, whichever is more readily determinable in accordance with FASB ASC 718.

**Segment Reporting:** FASB ASC 280 requires that a public business enterprise report financial and descriptive information about its reportable operating segments. Operating segments are components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. Generally, financial information is required to be reported on the basis that it is used internally for evaluating segment performance and deciding how to allocate resources to segments. Segments are determined based on differences in products, internal reporting and how operational decisions are made. Management has determined that the Optex Systems, Richardson plant, and the Applied Optics Center, Dallas plant, which was acquired on November 3, 2014, are separately managed, organized, and internally reported as separate business segments. The FASB ASC 280 requires that a public business enterprise report a measure of segment profit or loss, certain specific revenue and expense items, and segment assets. It requires reconciliations of total segment revenues, total segment profit or loss, total segment assets, and other amounts disclosed for segments to corresponding amounts in the enterprise's general-purpose financial statements.

**Financial Instruments Indexed to and Potentially Settled in the Company's Common Stock:** The Company evaluates all financial instruments issued in connection with its equity offerings when determining the proper accounting treatment for such instruments in the Company's financial statements. The Company considers a number of generally accepted accounting principles under U.S. GAAP to determine such treatment and evaluates the features of the instrument to determine the appropriate accounting treatment. For financial instruments either classified as a liabilities pursuant to ASC 480 "Distinguishing Liabilities from Equity" indexed to and potentially settled in the Company's common stock that are determined to be classified as liabilities on the consolidated balance sheet, changes in fair value are recorded as a gain or loss in the Company's consolidated statement of operations with the corresponding amount recorded as an adjustment to the liability on its consolidated balance sheets.

**Fair Value of Financial Instruments:** FASB ASC 825-10 requires disclosure of fair value information about certain financial instruments, including, but not limited to, cash and cash equivalents, accounts receivable, refundable tax credits, prepaid expenses, accounts payable, accrued expenses, notes payable to related parties and convertible debt-related securities. Fair value estimates discussed herein are based upon certain market assumptions and pertinent information available to management as of the financial statement presentation date.

The carrying value of the balance sheet cash and cash equivalents, accounts and notes receivable, accounts payable, accrued liabilities, and notes payable, are carried at, or approximate, fair value as of the reporting date because of their short-term nature. Fair values for the Company's warrant liabilities and derivatives are estimated by utilizing valuation models that consider current and expected stock prices, volatility, dividends, market interest rates, forward yield curves and discount rates. Such amounts and the recognition of such amounts are subject to significant estimates that may change in the future.

The accounting guidance FASB ASC 820-10, "Fair Value Measurements and Disclosures" establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value and requires that assets and liabilities carried at fair value be classified and disclosed in one of the following three categories:

Level 1: Quoted market prices in active markets for identical assets or liabilities.

Level 2: Observable market-based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs reflecting the reporting entity's own assumptions.

The accounting guidance establishes a hierarchy which requires an entity to maximize the use of quoted market prices and minimize the use of unobservable inputs. An asset or liability's level is based on the lowest level of input that is significant to the fair value measurement. Fair value estimates are reviewed at the origination date and again at the each applicable measurement date and interim or annual financial reporting dates, as applicable for the financial instrument, and are based upon certain market assumptions and pertinent information available to management at those times.

The methods and significant inputs and assumptions utilized in estimating the fair value of the warrant liabilities are discussed further in Note 7 "Warrant Liabilities". Each of the measurements is considered a Level 3 measurement as a result of at least one unobservable input.

**Income Tax/Deferred Tax:** FASB ASC 740 requires recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the consolidated financial statements or tax returns. Under this method, deferred tax assets and liabilities are determined based on differing treatment of items for financial reporting and income tax reporting purposes. The deferred tax balances are adjusted to reflect tax rates by tax jurisdiction, based on currently enacted tax laws, which will be in effect in the years in which the temporary differences are expected to reverse. Under FASB ASC 740, 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. A valuation allowance is provided for certain deferred tax assets if it is more likely than not that the Company will not realize tax assets through future operations.

**Earnings per Share:** Basic earnings per share is computed by dividing income available for common shareholders (the numerator) by the weighted average number of common shares outstanding (the denominator) for the period. Diluted earnings per share reflect the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock.

The potentially dilutive securities that Optex Systems Holdings has outstanding are convertible preferred stock, unvested restricted stock units, stock options and warrants. In computing the dilutive effect of convertible preferred stock, the numerator is adjusted to add back any convertible preferred dividends and the denominator is increased to assume the conversion of the number of additional common shares. Optex Systems Holdings uses the Treasury Stock Method to compute the dilutive effect of any dilutive shares. Convertible preferred stock, unvested restricted stock units, stock options and warrants that are anti-dilutive are excluded from the calculation of diluted earnings per common share.

For the three months ended January 1, 2017, 132,000 unvested restricted stock units, 56,290 stock options and 4,125,200 warrants were excluded from the earnings per share calculation as anti-dilutive. For the three months ended December 27, 2015, 1001 shares of Series A preferred stock, 969 shares of Series B preferred stock, 62,847 stock

options and 1,000 warrants were excluded from the earnings per share calculation as anti-dilutive.

### **Note 3 Segment Reporting**

Optex Systems Holdings reportable segments are strategic businesses offering similar products to similar markets and customers; however the companies are operated and managed separately due to differences in manufacturing technology, equipment, geographic location, and specific product mix. Applied Optics Center was acquired as a unit, and the management at the time of the acquisition was retained.

The Applied Optics Center segment also serves as the key supplier of laser coated filters used in the production of periscope assemblies for the Optex Systems Richardson segment. Intersegment sales and transfers are accounted for at annually agreed to pricing rates based on estimated segment product cost, which includes segment direct manufacturing and general and administrative costs, but exclude profits that would apply to third party external customers.

Optex Systems – Richardson, serves as the home office for both segments and shared general and administrative costs attributable to both segments are allocated directly to the segments based on the government Cost Accounting Standard (CAS) 403 – “Allocation of Home Office Expenses to Segments”. The purpose of CAS 403 is to provide criteria for allocating home office expenses to the segments of an organization based on the beneficial or causal relationships between the expenses and the receiving segments. Based on CAS 403, Optex Systems Holdings allocates home office expenses based on a three factor formula which is the average of the following three percentages for each of the segments fiscal year:

- (1) The percentage of segment payroll dollars to total payroll dollars of all segments;
- (2) The percentage of the segment’s operating revenue to the total operating revenue of all segments
- (3) The percentage of the average net book value of the sum of the segment’s tangible capital assets plus inventories to the total average net book value of such assets of all segments.

The financial table below presents the information for each of the reportable segments profit or loss as well as segment assets for each year. Optex Systems Holdings, Inc. does not allocate interest expense, income taxes or unusual items to segments.

	Reportable Segment Financial Information (thousands)			
	Three months ended January 1, 2017			
	Optex Systems Richardson	Applied Optics Center Dallas	Other (non allocated costs and intersegment eliminations)	Consolidated Total
Revenues from external customers	\$ 2,039	\$ 1,473	\$ -	\$ 3,512
Intersegment revenues	-	462	(462 )	-
Total Revenue	\$ 2,039	\$ 1,935	\$ (462 )	\$ 3,512
Interest (income) expense	-	-	4	4
Depreciation and Amortization	16	67	-	83
Income (Loss) before taxes	(41 )	(31 )	426	354
Other significant noncash items:				
Allocated home office expense	(166 )	166	-	-
(Gain) on Change in Fair Value of Warrants	-	-	(430 )	(430 )
Stock compensation expense	64	-	-	64

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Royalty expense amortization	7	-	-	7
Provision for (use of) contract loss reserves	-	-	-	-
Segment Assets	8,339	4,052	-	12,391
Expenditures for segment assets	4	126	-	130

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	Reportable Segment Financial Information (thousands)			
	Three months ended December 27, 2015			
	Optex Systems Richardson	Applied Optics Center Dallas	Other (non allocated costs and intersegment eliminations)	Consolidated Total
Revenues from external customers	\$ 2,167	\$ 1,046	\$ -	\$ 3,213
Intersegment revenues	-	221	(221)	-
Total Revenue	\$ 2,167	\$ 1,267	\$ (221)	\$ 3,213
Interest (income) expense	-	-	18	18
Depreciation and Amortization	19	67	-	86
Income (Loss) before taxes	15	(242)	(18)	(245)
Other significant noncash items:				
Allocated home office expense	(188)	188	-	-
Stock option compensation expense	24	-	-	24
Royalty expense amortization	7	-	-	7
Provision for (use of) contract loss reserves	-	(15)	-	(15)
Segment Assets	6,842	3,941	-	10,783
Expenditures for segment assets	-	-	-	-

#### Note 4 - Commitments and Contingencies

##### *Rental Payments under Non-cancellable Operating Leases*

Optex Systems Holdings leases its office and manufacturing facilities for the Optex Systems, Inc., Richardson address and the Applied Optics Center Dallas address, under non-cancellable operating leases.

The leased facility under Optex Systems Inc. at 1420 Presidential Drive, Richardson, Texas consists of 49,100 square feet of space and expires March 31, 2021. Pursuant to the terms of the most recent amendment to the Richardson site facilities lease, there was no base rent payment due from January 1, 2014 through March 31, 2014, with payments beginning April 2014, and annual rental payment inflationary increases between 3.4% and 4.8% occurring each year beginning in 2016.

The leased facility under the Applied Optics Center at 9839 and 9827 Chartwell Drive, Dallas, Texas, consists of 44,867 square feet of space at the premises. On November 17, 2016, we received a countersigned new lease for the Applied Optics Center from the landlord, dated October 21, 2016, and which commenced retroactive to October 1, 2016. The new lease term will expire on October 31, 2021, with two renewal options available to the tenant, each with a renewal term duration of five years. The monthly base rent is \$19.4 thousand through September 30, 2017 and escalates approximately 3% October 1, each year thereafter through 2021. The lease includes a one month base rent abatement for October 1 through October 31, 2016 for \$19.4 thousand. The monthly rent includes approximately \$4.9 thousand for additional Common Area Maintenance fees and taxes (CAM), to be adjusted annually based on actual expenses incurred by the landlord. The total monthly rent including CAM is \$24.3 thousand beginning November 1, 2016. Our obligations to make payments under the lease are secured by a \$250,000 standby letter of credit which we may be reduced to \$125,000 on October 31, 2019.

As of January 1, 2017 the unamortized deferred rent was \$127 thousand as compared to \$108 thousand as of October 2, 2016. Deferred rent expense is amortized monthly over the life of the lease.

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As of January 1, 2017, the remaining minimum lease and estimated adjusted common area maintenance (CAM) payments under the non-cancelable office and facility space leases are as follows:

### Non-cancellable Operating Leases Minimum Payments

Fiscal Year	(Thousands)				
	Optex Systems		Applied Optics Center Dallas		
	Richardson				
	Lease Payments	CAM Estimate	Lease Payments	CAM Estimate	Total Payments
2017	\$200	\$ 81	\$ 175	\$ 45	\$ 501
2018	271	108	240	60	679
2019	281	110	248	61	700
2020	291	112	255	62	720
2021	147	57	262	63	529
2022	-	-	22	5	27
Total minimum lease payments	\$ 1,190	\$ 468	\$ 1,202	\$ 296	\$ 3,156

Total facilities rental and CAM expense for both facility lease agreements as of the three months ended January 1, 2017 was \$166 thousand. Total expense under facility lease agreements as of the three months ended December 27, 2015 was \$154 thousand.

### Note 5 – Prepaid Royalties

Prepaid royalties represent payments made for the purchase of non-transferable, non-exclusive patent rights associated with a patent license. The patent license allows for development of current and future products in our digital line of periscopes. We completed our first international shipment utilizing this technology in 2014 and are currently in production to support a U.S. Government Foreign Military Sale contract awarded in January 2016. We estimate the commercial life of the patent at seven years. As of January 1, 2017, the balance of the patent license is \$82.8 thousand net of accumulated amortization. The royalty expenses for the associated patent license are amortized on a straight line basis starting in fiscal year 2013. The amortized royalty expense for the three months ending January 1, 2017 and December 27, 2015 was \$7.5 thousand, respectively.

### Note 6 - Debt Financing

**Related Parties**

*Sileas Secured Promissory Note Due on May 29, 2021 to Longview Fund, LP*

On June 5, 2015, Sileas Corp., the majority owner of Optex Systems, Inc. (Delaware), executed and delivered to Longview, an amended Secured Promissory Note in the amount of \$18.0 million and maturing on May 29, 2021.. The note is secured by and convertible into the Optex Systems Holdings Inc. common stock.

On August 4, 2016, Longview Fund, L.P. converted \$250 thousand of the note principal for 100,000 shares of Optex Systems Holdings common stock pursuant to the note conversion terms.

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On October 31, 2016, Longview Fund, L.P. converted \$2.7 million of the Sileas note principal in exchange for 800,000 shares of Optex Systems Holdings common stock. The Sileas note balance to the Longview Fund, LP as of January 1, 2017 is \$15.1 million.

On October 31, 2016, Longview Fund L.P. authorized the return to Optex Systems Holdings' treasury of 197,299 common shares, held by Sileas Corporation in settlement of \$155 thousand of accounts receivable due for expenses paid by Optex Systems Inc. on behalf of the Sileas Corporation. The shares were subsequently cancelled in satisfaction of the outstanding accounts receivable balance as of October 31, 2016.

### **Credit Facility — Avidbank**

The Company amended its revolving credit facility with Avidbank on October 17, 2016 from \$2 million to \$2.2 million. The interest rate for all advances against the line of credit shall be the then in effect prime rate plus 2.5% and is subject to a minimum interest payment requirement per six month period of \$10,000. The renewable revolving maturity date is January 22, 2018 and is secured by a first lien on all of its assets in favor of Avidbank. In order to meet the security requirement under the lease, we entered into a letter of credit with Avidbank on October 17, 2016 in the amount of \$250,000, which expires on October 17, 2017 and is renewable by us for successive one year periods unless the bank notifies us no later than 60 days prior to the end of the initial or any extended term that it shall not renew the letter of credit.

As of January 1, 2017 and October 2, 2016, the outstanding principal and accrued interest balance on the line of credit was \$300 thousand. For the three months ended January 1, 2017 and December 27, 2015, the total interest expense against the outstanding line of credit balance was \$4 thousand and \$18 thousand, respectively.

### **Note 7-Warrant Liabilities**

On August 26, 2016, Optex Systems Holdings Inc. issued 4,125,200 warrants to new shareholders and the underwriter, in connection with a public share offering. The warrants entitle the holder to purchase one share of our common stock at an exercise price equal to \$1.50 per share at any time on or after August 26, 2016 (the "Initial Exercise Date") and on or prior to the close of business on August 26, 2021 (the "Termination Date"). The Company determined that these warrants are free standing financial instruments that are legally detachable and separately exercisable from the common stock included in the public share offering. Management also determined that the warrants are puttable for cash upon a fundamental transaction at the option of the holder and as such required classification as a liability pursuant to ASC 480 "*Distinguishing Liabilities from Equity*". In accordance with the accounting guidance, the outstanding warrants are recognized as a warrant liability on the balance sheet and are

measured at their inception date fair value and subsequently re-measured at each reporting period with changes being recorded as a component of other income in the statement of operations.

The fair value of the warrant liabilities were measured using a binomial lattice model (“Binomial”). Significant inputs into the model at the inception and reporting period measurement dates are as follows:

Binomial Assumptions	<b>Issuance date</b> <sup>(1)</sup> <b>August 26, 2016</b>	Period ending October 2, 2016	Period ending January 1, 2017		
Exercise Price <sup>(1)</sup>	\$ 1.50	\$ 1.50	\$ 1.50		
Warrant Expiration Date <sup>(1)</sup>	August 26, 2021	August 26, 2021	August 26, 2021		
Stock Price <sup>(2)</sup>	\$ 0.95	\$ 0.77	\$ 0.67		
Interest Rate (annual) <sup>(3)</sup>	1.23	% 1.14	% 1.94	%	%
Volatility (annual) <sup>(4)</sup>	246.44	% 242.17	% 228.25	%	%
Time to Maturity (Years)	5.0	4.9	4.65		
Number of Steps (Years)	5	5	5		
Calculated fair value per share	\$ 0.93	\$ 0.76	\$ 0.65		

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(1) Based on the terms provided in the warrant agreement to purchase common stock of Optex Systems Holdings, Inc. dated August 26, 2016.

(2) Based on the trading value of common stock of Optex Systems Holdings, Inc. as of August 26, 2016 and each presented period ending date.

(3) Interest rate for U.S. Treasury Bonds, as of August 26, 2016 and each presented period ending date, as published by the U.S. Federal Reserve.

(4) Based on the historical daily volatility of Optex Systems Holdings, Inc. as of August 26, 2016 and each presented period ending date.

The warrants outstanding and fair values at each of the respective valuation dates are summarized below:

Warrant Liability	Warrants Outstanding	Fair Value per Share	<b>Fair Value</b> (000's)
Fair Value at initial measurement date of 8/26/2016	4,125,200	\$ 0.9349	\$ 3,857
(Gain) on Change in Fair Value of Warrant Liability			(739 )
Fair Value as of period ending 10/2/2016	4,125,200	\$ 0.7558	\$ 3,118
(Gain) on Change in Fair Value of Warrant Liability			(430 )
Fair Value as of period ending 1/1/2017	4,125,200	\$ 0.6516	\$ 2,688

During the three months ending January 1, 2017 Optex Systems Holdings recorded a gain on changes in fair value of warrant liability of \$430 thousand. During the three months ending December 27, 2015 there were no warrant liabilities or corresponding changes in valuation.

The warrant liabilities are considered Level 3 liabilities on the fair value hierarchy as the determination of fair value includes various assumptions about of future activities and the Company's stock prices and historical volatility as inputs. During the three months ending January 1, 2017, none of the warrants have been exercised.

#### Note 8-Stock Based Compensation

**Stock Options issued to Employees, Officers and Directors**

The Optex Systems Holdings 2009 Stock Option Plan provides for the issuance of up to 75,000 shares to Optex Systems Holdings officers, directors, employees and to independent contractors who provide services to Optex Systems Holdings as either incentive or nonstatutory stock options determined at the time of grant. As of January 1, 2017, Optex Systems Holdings has granted stock options to officers and employees as follows:

Date of Grant	Options Granted	Exercise Price	Options Outstanding As of 1/01/17	Expiration Date	Vesting Period
12/09/11	46,070	\$ 10.00	35,040	12/08/2018	4 years
12/19/13	25,000	\$ 10.00	25,000	12/18/2020	4 years
Total	71,070		60,040		

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The following table summarizes the status of Optex Systems Holdings' aggregate stock options granted under the incentive stock option plan:

Subject to Exercise	Number of Shares Remaining Options	Weighted Average Fair Value	Weighted Average Life (Years)	Aggregate Value (Thousands)
Outstanding as of September 27, 2015	62,858	\$ —	2.32	\$ —
Granted – 2016	—			
Forfeited – 2016	(2,518 )			—
Exercised – 2016	—			—
Outstanding as of October 2, 2016	60,340	\$ —	1.40	\$ —
Granted – 2017	—			
Forfeited – 2017	(300 )			—
Exercised – 2017	—			—
Outstanding as of January 1, 2017	60,040	\$ —	1.24	\$ —
Exercisable as of October 2, 2016	52,840	\$ —	1.07	\$ —
Exercisable as of January 1, 2017	56,290	\$ —	1.06	\$ —

There were no options granted in the three months ended January 1, 2017 or twelve months ending October 2, 2016.

The following table summarizes the status of Optex Systems Holdings' aggregate non-vested shares granted under the 2009 Stock Option Plan:

	Number of Non-vested Shares Subject to Options	Weighted- Average Grant- Date Fair Value
Non-vested as of September 27, 2015	22,592	\$ 7.66
Non-vested granted — year ended October 2, 2016	—	—
Vested — year ended October 2, 2016	(12,574 )	7.33
Forfeited — year ended October 2, 2016	(2,518 )	—
Non-vested as of October 2, 2016	7,500	\$ 8.00
Non-vested granted — three months ended January 1, 2017	—	—
Vested — three months ended January 1, 2017	(3,750 )	8.00
Forfeited — three months ended January 1, 2017	—	—
Non-vested as of January 1, 2017	3,750	\$ 8.00

## **Restricted Stock Units issued to Officers and Employees**

On June 14, 2016, the Compensation Committee (“Committee”) of the Board of Directors of Optex Systems Holdings, Inc. approved the Company’s 2016 Restricted Stock Unit Plan (the “Plan”). The Plan provides for the issuance of stock units (“RSU”) for up to 1,000,000 shares of the Company’s common stock to Optex Systems Holdings officers and employees. Each RSU constitutes a right to receive one share of the Company’s common stock, subject to vesting, which unless otherwise stated in an RSU agreement, shall vest in equal amounts on the first, second and third anniversary of the grant date. Shares of the Company’s common stock underlying the number of vested RSUs will be delivered as soon as practicable after vesting. During the period between grant and vesting, the RSUs may not be transferred, and the grantee has no rights as a shareholder until vesting has occurred. If the grantee’s employment is terminated for any reason (other than following a change in control of the Company or a termination of an officer other than for cause), then any unvested RSUs under the award will automatically terminate and be forfeited. If an officer grantee’s employment is terminated by the Company without cause or by the grantee for good reason, then, provided that the RSUs have not been previously forfeited, the remaining unvested portion of the RSUs will immediately vest as of the officer grantee’s termination date. In the event of a change in control, the Company’s obligations regarding outstanding RSUs shall, on such terms as may be approved by the Committee prior to such event, immediately vest, be assumed by the surviving or continuing company or cancelled in exchange for property (including cash).

On June 15, 2016, the Company issued 150,000 RSUs to its Chief Executive Officer, Danny Schoening, and 50,000 RSUs to its Chief Financial Officer, Karen Hawkins. The RSUs issued to Mr. Schoening and Ms. Hawkins vest as follows: 34% on January 1, 2017, 33% on January 1, 2018 and 33% on January 1, 2019. The total market value of the restricted stock units based on the shares price of \$1.85 as of June 15, 2016 is \$372 thousand. The cost of the shares is amortized on a straight line basis across the vesting periods.

As of January 1, 2017 and October 2, 2016, 68,000 and zero of the restricted stock units had vested, respectively. As of January 1, 2017 there are 132,000 outstanding unvested restricted stock units remaining to vest.

### Consulting and Vendor Equity Issues

On April 29, 2016, Optex Systems Holdings, Inc. issued 40,000 common “restricted” shares at a market price of \$2.35 per share (\$94,000) in support of the IRTH Communications agreement. The cost of the shares is amortized on a straight line basis through April 2017. There were no other equity instruments issued to consultants and vendors during the twelve months ended October 2, 2016 or the three months ending January 1, 2017.

### Stock Based Compensation Expense

Equity compensation is amortized based on a straight line basis across the vesting or service period as applicable. The recorded compensation costs for options and shares granted and restricted stock units awarded as well as the unrecognized compensation costs are summarized in the table below:

	<b>Stock Compensation (thousands)</b>		<b>Unrecognized Compensation Expense</b>	
	<b>Recognized Compensation Expense</b>		<b>As of period ending</b>	
	<b>Three months ended</b>		<b>As of period ending</b>	
	<b>January</b>		<b>As of period ending</b>	
	<b>1, 2017</b>	<b>December 27, 2015</b>	<b>January 1, 2017</b>	<b>October 2, 2016</b>
Stock Options	\$ 10	\$ 24	\$ 38	\$ 48
Restricted Stock Units	31	-	248	279
Consultant Shares (IRTH)	23	-	24	47
<b>Total Stock Compensation</b>	<b>\$ 64</b>	<b>\$ 24</b>	<b>\$ 310</b>	<b>\$ 374</b>

**Note 9 Stockholders' Equity**

*Common stock*

As of September 27, 2015, Optex Systems had 314,867 common shares outstanding.

On August 26, 2016, 2,291,900 Class A units consisting of common stock and warrants and 400 Class B units consisting of shares of Series C convertible stock and warrants were issued pursuant to a public offering. The offering is comprised of Class A Units, priced at a public offering price of \$1.20 per unit, with each unit consisting of one share of common stock and one five-year warrant to purchase one share of common stock with an exercise price of \$1.50 per share (each, a "warrant"), and Class B Units, priced at a public offering price of \$5,000 per unit, with each unit comprised of one share of preferred stock with a conversion price of \$1.20 which is convertible into 4,167 shares of common stock and warrants to purchase 4,167 shares of common stock. The net proceeds from the offering were \$4,245 thousand (Gross proceeds of \$4,750 thousand less underwriter expenses of \$505 thousand). Deferred public offering costs incurred by Optex in connection with the offering was included \$252 thousand in paid expenses and 166,500 stock warrants issued to the underwriter.

During the twelve months ending October 2, 2016, Optex Systems Holdings issued 5,619,587 common shares due to conversions of Series A, Series B and Series C preferred stock, 2,291,900 shares were issued in connection with the public offering, 247 common shares were issued to correct Depository Trust and Clearing Corporation (DTC) rounding errors occurring from the October 7, 2015 reverse split and 40,000 common shares were issued to a vendor. There were no other issuances of common or preferred stock during the twelve months ended October 2, 2016. As of October 2, 2016, the outstanding common shares are 8,266,601.

On October 31, 2016, Longview Fund L.P. authorized the return to Optex Systems Holdings' treasury of 197,299 common shares, held by Sileas Corporation in settlement of \$155 thousand of accounts receivable due for expenses paid by Optex Systems Inc. on behalf of the Sileas Corporation. The shares were subsequently cancelled in satisfaction of the outstanding accounts receivable balance as of October 31, 2016.

During the three months ending January 1, 2017, Optex Systems Holdings issued 75,000 common shares due to conversions of Series C preferred stock and cancelled 197,299 common shares which were returned by Sileas. There were no other issuances of common or preferred stock during the three months ended January 1, 2017. As of January 1, 2017, the outstanding common shares are 8,144,302.

### *Series A preferred stock*

Optex Systems Holdings has filed a Certificate of Designation with the Secretary of State of the State of Delaware authorizing a series of preferred stock, under its articles of incorporation, known as "Series A preferred stock". The Certificate of Designation currently sets forth the following terms for the Series A preferred stock: (i) number of authorized shares: 1,027; (ii) per share stated value: \$6,860; (iii) liquidation preference per share: stated value; (iv) conversion price: \$1.20 per share, as adjusted from time to time; and (v) voting rights: votes along with the common stock on an as converted basis with one vote per share (vi) par value \$0.001 per share. Holders of preferred shares receive preferential rights in the event of liquidation. Additionally the preferred stock shareholders are entitled to vote together with the common stock on an "as-converted" basis. Each share of preferred stock is immediately convertible into common shares at the option of the holder which entitles the holder to receive the equivalent number of common shares equal to the stated value of the preferred shares divided by the conversion price of \$1.20 per share pursuant to the August 22, 2016 public offering of common shares at \$1.20 per share.

The Series A preferred stock entitles the holders to receive cumulative dividends at the rate of 6% per annum, payable in cash at the discretion of the Board of Directors. As of April 1, 2012, the preferred shareholders agreed to waive the past dividends in arrears through June 29, 2014 of \$884 thousand in exchange for an increase in the stated value to \$6,860. On February 21, 2012, in connection with the purchase of the 5,000 shares of common stock of Optex Systems Holdings by Alpha Capital, the preferred shareholders executed an irrevocable waiver for any and all previously accrued and outstanding dividends and the right to receive any future dividends on the Series A Preferred

Stock. The per share conversion price of the Optex Systems Holdings' Series A Preferred Stock was automatically reset to \$10.00 per share in accordance with the reset provision as set forth in paragraph 4(d)(ii) of the Series Designation for the Optex Systems Holdings' Series A Preferred Stock. The total amount of dividends waived as a result of the February 21, 2012 waiver is \$213 thousand. As of October 2, 2016 and September 27, 2015 as a result of the executed waiver dated February 21, 2012, there were no dividends in arrears on preferred shares and no future dividends will accrue on the preferred shares.

Optex Systems Holdings had 1,001 of preferred shares outstanding as of September 27, 2015. During the twelve months ending October 2, 2016 there were conversions of 935 preferred Series A shares, or \$6,415 thousand, into 5,318,896 common shares, and cash redemptions for \$455 thousand of 66 Series A preferred shares. There were no issuances of preferred Series A stock during the three months ended January 1, 2017. As of J