

REO Plastics, Inc.

Financial Report
April 30, 2021

Contents

Independent auditor's report	1
<hr/>	
Financial statements	
Balance sheets	2
Statements of income	3
Statements of stockholders' equity	4
Statements of cash flows	5
Notes to financial statements	6-11



RSM US LLP

Independent Auditor's Report

Board of Directors and Stockholders
REO Plastics, Inc.

Report on the Financial Statements

We have audited the accompanying financial statements of REO Plastics, Inc., which comprise the balance sheets as of April 30, 2021 and 2020, the related statements of income, stockholders' equity and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of REO Plastics, Inc. as of April 30, 2021 and 2020, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

RSM US LLP

Minneapolis, Minnesota
June 30, 2021

REO Plastics, Inc.

Balance Sheets
April 30, 2021 and 2020

	2021	2020
Assets		
Current assets:		
Cash	\$ 5,158,800	\$ 1,074,184
Short-term investments	-	1,750,000
Trade receivables, net	8,106,720	5,864,697
Inventories, net:		
Raw materials	6,012,416	4,505,488
Work in process	1,038,646	1,298,680
Finished goods	1,848,276	2,613,102
Customer molds in process	651,445	631,129
Prepaid and other current assets	71,568	46,513
Total current assets	22,887,871	17,783,793
Property and equipment, at cost:		
Land	217,593	217,593
Building	5,100,764	4,793,557
Machinery and equipment	18,708,460	18,062,147
Construction in progress	1,262,936	90,833
	25,289,753	23,164,130
Less accumulated depreciation	17,973,059	16,840,329
	7,316,694	6,323,801
	\$ 30,204,565	\$ 24,107,594
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 3,892,680	\$ 1,816,210
Income taxes payable	114,673	110,472
Accrued expenses, principally compensation	1,339,118	1,036,069
Customer deposits	382,648	496,879
Total current liabilities	5,729,119	3,459,630
Long-term liabilities:		
Deferred compensation, less current portion	457,113	467,883
Deferred income taxes	740,000	692,000
	1,197,113	1,159,883
Commitments and contingencies		
Stockholders' equity:		
Common stock, par value \$0.10 per share; authorized 1,000,000 shares; issued and outstanding 446,009 shares as of April 30, 2021, and 447,709 shares as of April 30, 2020	44,601	44,771
Additional paid-in capital	224,488	225,338
Retained earnings	23,009,244	19,217,972
	23,278,333	19,488,081
	\$ 30,204,565	\$ 24,107,594

See notes to financial statements.

REO Plastics, Inc.

Statements of Income
Years Ended April 30, 2021 and 2020

	2021	2020
Net sales	\$ 36,663,340	\$ 30,538,162
Cost of goods sold	<u>31,402,668</u>	<u>27,798,303</u>
Gross profit	<u>5,260,672</u>	<u>2,739,859</u>
Operating expenses:		
General and administrative	1,896,320	1,811,547
Selling	874,594	858,119
Deferred compensation	<u>29,230</u>	<u>39,647</u>
	<u>2,800,144</u>	<u>2,709,313</u>
Operating income	2,460,528	30,546
Nonoperating income (expense):		
Interest income	16,850	47,926
Gain on forgiveness of PPP loan	2,012,144	-
Other, net	<u>(26,770)</u>	<u>(10,595)</u>
Net income before income tax expense	<u>4,462,752</u>	<u>67,877</u>
Income tax expense	<u>(630,000)</u>	<u>(35,000)</u>
Net income	<u>\$ 3,832,752</u>	<u>\$ 32,877</u>
Income per common share	<u>\$ 8.58</u>	<u>\$ 0.07</u>
Weighted-average common shares outstanding	<u>446,759</u>	<u>447,709</u>

See notes to financial statements.

REO Plastics, Inc.

**Statements of Stockholders' Equity
Years Ended April 30, 2021 and 2020**

	Common Stock	Additional Paid-In Capital	Retained Earnings	Total
Balance, April 30, 2019	\$ 44,771	\$ 225,338	\$ 19,185,095	\$ 19,455,204
Net income	-	-	32,877	32,877
Balance, April 30, 2020	44,771	225,338	19,217,972	19,488,081
Purchase of 1,700 shares of common stock for retirement	(170)	(850)	(41,480)	(42,500)
Net income	-	-	3,832,752	3,832,752
Balance, April 30, 2021	\$ 44,601	\$ 224,488	\$ 23,009,244	\$ 23,278,333

See notes to financial statements.

REO Plastics, Inc.

Statements of Cash Flows
Years Ended April 30, 2021 and 2020

	2021	2020
Cash flows from operating activities:		
Net income	\$ 3,832,752	\$ 32,877
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	1,259,638	1,301,964
Loss (gain) on disposal of equipment	22,734	(22,621)
Deferred income taxes	48,000	(99,000)
Deferred compensation expense	29,230	39,647
PPP loan forgiveness	(2,012,144)	-
Noncash interest expense on PPP loan	15,144	-
Changes in operating assets and liabilities:		
Trade receivables	(2,242,023)	455,996
Inventories	(482,068)	(537,339)
Customer molds in process	(20,316)	(112,897)
Prepaid and other current assets	(25,055)	3,037
Accounts payable and accrued expenses	2,379,519	(535,209)
Customer deposits	(114,231)	96,182
Income taxes payable	4,201	68,341
Net cash provided by operating activities	2,695,381	690,978
Cash flows from investing activities:		
Proceeds from redemptions of investments	2,500,000	3,066,882
Purchases of investments	(750,000)	(2,269,000)
Purchases of property and equipment	(2,296,265)	(1,198,155)
Proceeds from disposal of property and equipment	21,000	28,000
Net cash used in investing activities	(525,265)	(372,273)
Cash flows from financing activities:		
Deferred compensation payments	(40,000)	(20,000)
Purchase of shares of common stock for retirement	(42,500)	-
Proceeds from forgivable PPP loan	1,997,000	-
Net cash provided by (used in) financing activities	1,914,500	(20,000)
Increase in cash	4,084,616	298,705
Cash:		
Beginning	1,074,184	775,479
Ending	\$ 5,158,800	\$ 1,074,184
Supplemental disclosures of cash flow information:		
Cash payments for income taxes	\$ 575,000	\$ 73,000

See notes to financial statements.

REO Plastics, Inc.

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies

Nature of business: REO Plastics, Inc.'s (the Company) operations principally involve the custom injection molding, decorating and assembling of thermoplastics for customers in various industries, on a national basis and on credit terms that the Company establishes with each customer.

A summary of the Company's significant accounting policies follows:

Use of estimates in the preparation of financial statements: 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 the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Revenue recognition: The Company recognizes revenue in accordance with *FASB Accounting Standards Codification (ASC) Topic 606*, which provides a five-step model for recognizing revenue from contracts with customers as follows:

- Identify the contract with a customer.
- Identify the performance obligations in the contract.
- Determine the transaction price.
- Allocate the transaction price to the performance obligations in the contract.
- Recognize revenue when or as performance obligations are satisfied.

The Company's revenue is derived from sales of custom injection tooling, moldings, decorating and assembling of thermoplastics for original equipment manufacturers in various industries, primarily in the United States. Sales of products are subject to economic conditions and may fluctuate based on changes in the industry, trade policies and financial markets.

Nature of products and services: Revenue from the sale of the Company's products is recognized at a point in time, upon transfer of control to the customer, which is typically upon shipment, Free on Board (FOB) shipping point. The Company has elected to treat shipping and handling activities related to contracts with customers as costs to fulfill the promise to transfer the associated equipment and not as a separate performance obligation.

Transaction price: The transaction price is the amount of consideration to which the Company expects to be entitled in exchange for transferring goods to the customer. Revenue is recorded based on the transaction price, which includes fixed consideration and estimates of variable consideration such as early payment discounts, rebates, rights of return, and other allowances.

The amount of variable consideration included in the transaction price is constrained and is included only to the extent it is probable that a significant reversal of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is subsequently resolved. Variable consideration is estimated using the expected-value method (i.e., probability-weighted approach) based on review of specific transactions, historical experience, and market and economic conditions. Variable consideration is not significant to the overall transaction price.

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Contract balances: The timing of revenue recognition aligns with the right to invoice the customer. The Company records accounts receivable when it has the unconditional right to issue an invoice and receive payment, which is upon shipment of the product to the customer or completion of the delivery. Payment terms on invoiced amounts are typically 45 to 75 days. The primary purpose of the Company's invoicing terms is to provide customers with simplified and predictable ways of purchasing the products and not to provide financing to the customer.

The Company excludes from revenue sales taxes and other government-assessed and imposed taxes on revenue-generating activities that are invoiced to customers.

Warranties: The Company generally provides limited-assurance-type warranties for standard equipment and work performed under its contracts. The warranty periods typically extend for a limited duration following transfer of control of the equipment. Historically, warranty claims have not resulted in material costs incurred. The Company does not consider these warranties to be performance obligations.

Costs to obtain a contract: The Company has elected to apply the practical expedient to expense sales commissions and associated costs as incurred when the expected amortization period is one year or less, which applies to all customer contracts.

Cash: For purposes of reporting cash flows, the Company considers all money market funds to be cash. The Company maintains its cash in bank deposit accounts that, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts.

Short-term investments: At times, the Company has short-term investments that consist of certificates of deposit, treasury bills (T-bills) and treasury notes (T-notes). The certificates of deposit, T-bills and T-notes are held at one bank until maturity, with maturities of less than one year from the date of purchase, and are recorded at cost, which approximates fair value due to the short-term nature of these investments.

Trade receivables: Trade receivables are carried at original invoice amount less an estimate made for doubtful receivables based on a review of all outstanding amounts on a periodic basis. Management determines the allowance for doubtful accounts by regularly evaluating individual customer receivables and considering a customer's financial condition and credit history, and current economic conditions. The allowance for doubtful accounts approximates \$21,000 as of April 30, 2021 and 2020. Trade receivables are written off when deemed uncollectible. Recoveries of trade receivables previously written off are recorded when received. A trade receivable is generally considered to be past due if any portion of the receivable balance is outstanding for more than 90 days.

Inventories: Raw materials are stated at the lower of cost (first-in, first-out) or market. Inventories of work in process and finished goods are stated at standard costs, which approximate the lower of cost (first-in, first-out) or market. Inventories are reduced by valuation reserves of approximately \$19,000 and \$101,000 as of April 30, 2021 and 2020, respectively.

REO Plastics, Inc.

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Property and equipment: Property and equipment is stated at acquisition cost. Repair and maintenance are expensed as incurred. Major improvements and betterments are capitalized. Depreciation is provided using the straight-line method based on the following estimated useful lives:

	<u>Years</u>
Building	10-40
Machinery and equipment	3-10

The Company had repairs and maintenance expense of approximately \$712,000 and \$805,000 for the years ended April 30, 2021 and 2020, respectively.

Long-lived assets: Long-lived assets are evaluated for impairment whenever events or changes in circumstances indicate the carrying value of an asset may not be recoverable or if depreciable lives should be modified. To date, management has determined that no impairment of long-lived assets exists.

Customer mold in process and customer deposits: The Company requires a cash deposit for customer-specific mold production. Molds are recorded as current assets during production and transferred to cost of goods sold upon customer acceptance of the mold. Revenue, and the corresponding cost of goods sold, is recognized on the molds when product samples have been approved by the customer.

Income taxes: Deferred income taxes are provided on an asset and liability method whereby deferred tax assets are recognized for deductible temporary differences, and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance if, in the opinion of management, it is more likely than not that some portion of the deferred tax assets may not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. The Company classifies all deferred income taxes as a single, noncurrent net asset in the accompanying balance sheets.

The Company recognizes income tax liabilities when the Company believes that certain positions may not be fully sustained upon review by tax authorities. Benefits from income tax positions are measured at the largest amount of benefit that is greater than 50% likely of being realized upon settlement. Management has evaluated the Company's income tax positions and determined there are no material uncertain income tax positions that require adjustment to the financial statements. To the extent that the final income tax outcome of these matters is different from the amounts recorded, such differences impact income tax expense in the period in which such determination is made. Interest and penalties, if any, related to accrued liabilities for potential income tax assessments are included in income tax expense.

Income per common share: Income per common share is computed by dividing net income by the weighted-average number of shares of common stock outstanding during the year.

REO Plastics, Inc.

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Recent accounting pronouncement: In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-02, *Leases (Topic 842)*. The guidance in this ASU supersedes the leasing guidance in Topic 840, Leases. Under the new guidance, lessees are required to recognize lease assets and lease liabilities on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard will be effective for the Company's fiscal year ending April 30, 2023, with early adoption permitted. The Company is currently evaluating the impact of the pending adoption of the new standard on the financial statements.

In December 2019, the FASB issued ASU No. 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes*, which is intended to simplify various aspects related to accounting for income taxes. ASU 2019-12 removes certain exceptions to the general principles in ASC 740 and also clarifies and amends existing guidance to improve consistent application. This ASU is effective for the Company beginning on May 1, 2022. The Company is currently evaluating the impact of the pending adoption of the new standard on the financial statements.

Subsequent events: The Company has evaluated subsequent events through June 30, 2021, the date on which the financial statements were available to be issued.

Note 2. Federal and State Income Taxes

Deferred income taxes consist of the following components:

	April 30	
	2021	2020
Deferred tax assets:		
Accounts receivable	\$ 5,000	\$ 5,000
Inventory	37,000	80,000
Accrued expenses	90,000	72,000
Deferred compensation	120,000	124,000
	<u>252,000</u>	<u>281,000</u>
Deferred tax liabilities:		
Property and equipment	(992,000)	(973,000)
Net deferred tax liabilities	<u>\$ (740,000)</u>	<u>\$ (692,000)</u>

The provision for income taxes charged to operations consisted of the following:

	Years Ended April 30	
	2021	2020
Current tax expense	\$ 582,000	\$ 134,000
Deferred tax (benefit) expense	48,000	(99,000)
Income tax expense	<u>\$ 630,000</u>	<u>\$ 35,000</u>

REO Plastics, Inc.

Notes to Financial Statements

Note 2. Federal and State Income Taxes (Continued)

For the years ended April 30, 2021 and 2020, the difference between the tax expense and that which would be computed by applying the U.S. federal income tax rate (21%) to pretax net income is as follows:

	Years Ended April 30	
	2021	2020
Computed "expected" federal tax expense at statutory rates	\$ 937,000	\$ 14,000
State income tax expense, net of federal effect	110,000	13,000
Permanent differences	5,000	3,000
PPP loan forgiveness income	(423,000)	-
Other	1,000	5,000
Income tax expense (benefit)	<u>\$ 630,000</u>	<u>\$ 35,000</u>

Note 3. Commitments and Contingencies

Employee benefit plans: The Company has a 401(k) tax-deferred savings plan in effect for its employees. Employees over the age of 21 are eligible to participate after 60 days of employment. The Company matches 50 cents of each dollar contributed by the employee, up to 6% of the employee's salary. Matching contributions are made on a weekly basis. The Company recorded employer match expense of approximately \$113,000 and \$106,000 for the years ended April 30, 2021 and 2020, respectively.

Lease commitments: The Company leases a portion of its warehouse facilities under a noncancelable agreement that expires in August 2024. In addition to base rent, the Company is required to pay its share of maintenance and real estate taxes.

Future minimum rental payments due under noncancelable operating leases are approximately as follows:

Years ending April 30:	
2022	\$ 375,000
2023	366,000
2024	376,000
2025	122,000
	<u>\$ 1,239,000</u>

Rent expense under operating leases was approximately \$386,000 and \$362,000 for the years ended April 30, 2021 and 2020, respectively.

Litigation: The Company is involved in certain legal proceedings and claims incidental to the normal course of business. Although the ultimate outcome of these outstanding claims cannot be determined, management believes their final resolution will not have a material adverse effect on the financial position of the Company.

REO Plastics, Inc.

Notes to Financial Statements

Note 4. Major Customers

Net sales and trade receivables for the years ended April 30, 2021 and 2020, from major customers (in excess of 10% of total net sales) were as follows:

	Net Sales, Years Ended April 30		Trade Receivables as of April 30	
	2021	2020	2021	2020
Customer A	40%	25%	\$ 4,166,000	\$ 2,350,000
Customer B	12%	16%	645,000	716,000

Note 5. Paycheck Protection Program Loan

In May 2020, the Company entered into a note payable with a bank in the amount of \$1,997,000, under the Paycheck Protection Program (PPP), authorized under the Coronavirus Aid, Relief, and Economic Security (CARES) Act. This was a two-year loan with 1.00% interest, which was forgiven under conditions as defined in the CARES Act. The Company submitted the loan for forgiveness and on February 10, 2021, the Company was notified that the full note payable and related accrued interest of approximately \$15,000 was forgiven, resulting in a gain upon debt forgiveness of approximately \$2,012,000 recognized in the statement of income for the year ended April 30, 2021. All expenses related to the required expenditures under the PPP loan are included in operations for the year ended April 30, 2021. The PPP loan forgiveness is subject to audit by the Small Business Administration for a period up to six years after the loan has been forgiven. No provision has been recorded as the Company believes they met the eligibility criteria to qualify for the loan used the proceeds for qualified operating expenses.

Note 6. Deferred Compensation

The Company has deferred compensation arrangements with four key executives of the Company. Upon retirement, as defined, each executive receives annual payments of \$20,000 for a period of 11 years. The payments cease upon the death of the executive. All deferred compensation benefits were fully vested as of the signing of the contracts. Deferred compensation expense was approximately \$29,000 and \$40,000 for the years ended April 30, 2021 and 2020, respectively, and consists of the change in the present value of the remaining payments, including estimated retirement dates, and the difference between actual deferred compensation payment and the mortality adjusted expected payments.

Based on estimated retirement dates, the Company expects deferred compensation payments to continue through 2033. Future deferred compensation payments approximate as follows:

Years ending April 30:	
2022	\$ 60,000
2023	80,000
2024	80,000
2025	80,000
2026	80,000
Thereafter	400,000
	<hr/>
	780,000
Less amounts representing interest and life expectancy adjustments	(263,000)
	<hr/>
	\$ 517,000
	<hr/>