

ULTRALIFE CORP  
Form 10-Q  
May 10, 2012  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended April 1, 2012

or

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

For the transition period from            to

Commission File Number 000-20852

**ULTRALIFE CORPORATION**

(Exact name of registrant as specified in its charter)

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**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**16-1387013**  
(I.R.S. Employer  
Identification No.)

**2000 Technology Parkway, Newark, New York 14513**  
(Address of principal executive offices)

**(315) 332-7100**  
(Zip Code)

**(315) 332-7100**  
(Registrant's telephone number, including area code)

**(Former name, former address and former fiscal year, if changed since last report)**

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

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

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes  No

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

Common stock, \$.10 par value 17,388,435 shares of common stock outstanding, net of 1,372,757 treasury shares, as of April 29, 2012.

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## PART I FINANCIAL INFORMATION

## Item 1. Financial Statements

## ULTRALIFE CORPORATION

## CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in Thousands, Except Per Share Amounts)

|   | (Unaudited)      |                      |
|---|------------------|----------------------|
|   | April 1,<br>2012 | December 31,<br>2011 |
| <b>ASSETS</b>   |                  |                      |
| <b>Current assets:</b>  |                  |                      |
| Cash and cash equivalents   | \$ 4,136         | \$ 5,320             |
| Restricted cash   | 171              | 166                  |
| Trade accounts receivable (less allowance for doubtful accounts of \$664 at April 1, 2012 and \$683 at December 31, 2011) | 18,469           | 19,903               |
| Inventories   | 31,788           | 34,967               |
| Due from insurance company  | 1,746            | 1,730                |
| Deferred tax asset - current  | 161              | 161                  |
| Income taxes receivable   | 189              | 220                  |
| Prepaid expenses and other current assets   | 1,916            | 1,766                |
| <b>Total current assets</b>   | <b>58,576</b>    | <b>64,233</b>        |
| <b>Property, plant and equipment, net</b>   | <b>12,200</b>    | <b>12,588</b>        |
| <b>Other assets:</b>  |                  |                      |
| Goodwill  | 18,378           | 18,356               |
| Intangible assets, net  | 5,412            | 5,533                |
| Security deposits and other long-term assets  | 98               | 105                  |
|   | 23,888           | 23,994               |
| <b>Total Assets</b>   | <b>\$ 94,664</b> | <b>\$ 100,815</b>    |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>  |                  |                      |
| <b>Current liabilities:</b>   |                  |                      |
| Current portion of debt   | \$ 19            | \$                   |
| Accounts payable  | 8,994            | 13,766               |
| Income taxes payable  | 11               | 11                   |
| Deferred tax liability - current  | 145              | 187                  |
| Other current liabilities   | 8,753            | 9,194                |
| <b>Total current liabilities</b>  | <b>17,922</b>    | <b>23,158</b>        |
| <b>Long-term liabilities:</b>   |                  |                      |
| Deferred tax liability - long-term  | 4,237            | 4,170                |
| Other long-term liabilities   | 193              | 261                  |
| <b>Total long-term liabilities</b>  | <b>4,430</b>     | <b>4,431</b>         |

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**Commitments and contingencies (Note 10)**

**Shareholders' equity:**

Ultralife equity:

Preferred stock, par value \$0.10 per share, authorized 1,000,000 shares; none issued and outstanding

Common stock, par value \$0.10 per share, authorized 40,000,000 shares; issued - 18,757,192 at April 1, 2012

and 18,716,921 at December 31, 2011

|                                      |          |          |
|--------------------------------------|----------|----------|
|                                      | 1,878    | 1,874    |
| Capital in excess of par value       | 172,745  | 172,309  |
| Accumulated other comprehensive loss | (837)    | (985)    |
| Accumulated deficit                  | (93,782) | (92,280) |

|  |        |        |
|--|--------|--------|
|  | 80,004 | 80,918 |
|--|--------|--------|

Less - Treasury stock, at cost - 1,372,757 shares at April 1, 2012 and 1,372,757 shares at December 31, 2011  
outstanding

|  |       |       |
|--|-------|-------|
|  | 7,658 | 7,658 |
|--|-------|-------|

|                        |        |        |
|------------------------|--------|--------|
| Total Ultralife equity | 72,346 | 73,260 |
|------------------------|--------|--------|

|                         |      |      |
|-------------------------|------|------|
| Noncontrolling interest | (34) | (34) |
|-------------------------|------|------|

|                            |        |        |
|----------------------------|--------|--------|
| Total shareholders' equity | 72,312 | 73,226 |
|----------------------------|--------|--------|

|  |           |            |
|--|-----------|------------|
| Total Liabilities and Shareholders' Equity | \$ 94,664 | \$ 100,815 |
|--|-----------|------------|

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

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## ULTRALIFE CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(In Thousands, Except Per Share Amounts)

(unaudited)

|  | Three-Month Periods Ended |                  |
|--|---------------------------|------------------|
|  | April 1,<br>2012          | April 3,<br>2011 |
| <b>Revenues</b>  | \$ 27,501                 | \$ 27,915        |
| <b>Cost of products sold</b>   | 20,908                    | 23,501           |
| <b>Gross profit</b>  | 6,593                     | 4,414            |
| <b>Operating expenses:</b>   |                           |                  |
| Research and development (including \$65 and \$78, respectively, of amortization of intangible assets)             | 2,139                     | 2,505            |
| Selling, general, and administrative (including \$60 and \$79, respectively, of amortization of intangible assets) | 5,743                     | 5,845            |
| <b>Total operating expenses</b>  | 7,882                     | 8,350            |
| <b>Operating income (loss)</b>   | (1,289)                   | (3,936)          |
| <b>Other income (expense):</b>   |                           |                  |
| Interest income  | 1                         | 1                |
| Interest expense   | (104)                     | (156)            |
| Miscellaneous  | 52                        | 299              |
| <b>Income (loss) from continuing operations before income taxes</b>  | (1,340)                   | (3,792)          |
| Income tax provision-current   | 79                        | 4                |
| Income tax provision-deferred  | 12                        | 54               |
| Total income taxes provision   | 91                        | 58               |
| <b>Net income (loss) from continuing operations</b>  | (1,431)                   | (3,850)          |
| <b>Discontinued operations:</b>  |                           |                  |
| Income (loss) from discontinued operations, net of tax   | (71)                      | (1,853)          |
| <b>Net income (loss)</b>   | (1,502)                   | (5,703)          |
| Net (income) loss attributable to noncontrolling interest  |                           | 13               |
| <b>Net income (loss) attributable to Ultralife</b>   | \$ (1,502)                | \$ (5,690)       |
| <b>Other comprehensive income (loss):</b>  |                           |                  |
| Foreign currency translation adjustments   | 148                       | 227              |
| <b>Comprehensive income (loss) attributable to Ultralife</b>   | \$ (1,354)                | \$ (5,463)       |
| <b>Net income (loss) attributable to Ultralife common shareholders - basic</b>                                     |                           |                  |
| Continuing operations  | \$ (0.08)                 | \$ (0.22)        |
| Discontinued operations  | \$ (0.01)                 | \$ (0.11)        |

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|  |           |           |
|--|-----------|-----------|
| Total  | \$ (0.09) | \$ (0.33) |
| <b>Net income (loss) attributable to Ultralife common shareholders - diluted</b> |           |           |
| Continuing operations  | \$ (0.08) | \$ (0.22) |
| Discontinued operations  | \$ (0.01) | \$ (0.11) |
| Total  | \$ (0.09) | \$ (0.33) |
| <b>Weighted average shares outstanding - basic</b>                               | 17,358    | 17,276    |
| <b>Weighted average shares outstanding - diluted</b>                             | 17,358    | 17,276    |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

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## ULTRALIFE CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in Thousands)

(unaudited)

|   | Three-Month Periods Ended |                  |
|---|---------------------------|------------------|
|   | April 1,<br>2012          | April 3,<br>2011 |
| <b>OPERATING ACTIVITIES</b>   |                           |                  |
| Net income (loss)   | \$ (1,502)                | \$ (5,703)       |
| Loss from discontinued operations, net of tax   | 71                        | 1,853            |
| Adjustments to reconcile net income (loss) from continuing operations to net cash provided from operating activities: |                           |                  |
| Depreciation and amortization of financing fees   | 880                       | 923              |
| Amortization of intangible assets   | 125                       | 157              |
| (Gain) loss on long-lived asset disposal and write-offs   | 6                         |                  |
| Foreign exchange gain   | (46)                      | (290)            |
| Non-cash stock-based compensation   | 341                       | 284              |
| Changes in deferred income taxes  | 12                        | 54               |
| Changes in operating assets and liabilities:  |                           |                  |
| Accounts receivable   | 1,882                     | 13,237           |
| Inventories   | 3,178                     | (9,224)          |
| Income taxes receivable   | 29                        |                  |
| Prepaid expenses and other current assets   | (160)                     | 66               |
| Income taxes payable  |                           | (24)             |
| Accounts payable and other liabilities  | (6,016)                   | 702              |
| Net cash provided from (used in) operating activities from continuing operations                                      | (1,200)                   | 2,035            |
| Net cash provided from operating activities from discontinued operations  |                           | 31               |
| Net cash provided from (used in) operating activities   | (1,200)                   | 2,066            |
| <b>INVESTING ACTIVITIES</b>   |                           |                  |
| Purchase of property and equipment  | (209)                     | (492)            |
| Payments for acquired companies, net of cash acquired   |                           | (50)             |
| Net cash used in investing activities from continuing operations  | (209)                     | (542)            |
| Net cash provided from investing activities from discontinued operations  |                           | 15               |
| Net cash used in investing activities   | (209)                     | (527)            |
| <b>FINANCING ACTIVITIES</b>   |                           |                  |
| Net change in revolving credit facility   | 19                        | 1,654            |
| Proceeds from issuance of common stock  | 99                        | 53               |
| Principal payments on debt and capital lease obligations  |                           | (2)              |
| Net cash provided from financing activities from continuing operations  | 118                       | 1,705            |
| Net cash used in financing activities from discontinued operations  |                           | (40)             |
| Net cash provided from financing activities   | 118                       | 1,665            |

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|  |          |          |
|--|----------|----------|
| Effect of exchange rate changes on cash          | 107      | 301      |
| Change in cash and cash equivalents              | (1,184)  | 3,505    |
| Cash and cash equivalents at beginning of period | 5,320    | 4,641    |
| Cash and cash equivalents at end of period       | \$ 4,136 | \$ 8,146 |
| SUPPLEMENTAL CASH FLOW INFORMATION               |          |          |
| Cash paid for income taxes                       | \$ 47    | \$ 28    |
| Cash paid for interest                           | \$ 69    | \$ 163   |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

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ULTRALIFE CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollar Amounts in Thousands Except Share and Per Share Amounts)

(unaudited)

1. BASIS OF PRESENTATION

The accompanying unaudited Condensed Consolidated Financial Statements of Ultralife Corporation and our subsidiaries have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals and adjustments) considered necessary for a fair presentation of the Condensed Consolidated Financial Statements have been included. Results for interim periods should not be considered indicative of results to be expected for a full year. Reference should be made to the Consolidated Financial Statements contained in our Form 10-K for the twelve-month period ended December 31, 2011.

The year-end condensed consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

Certain items previously reported in specific financial statement captions have been reclassified to conform to the current presentation.

Our monthly closing schedule is a 4/4/5 weekly-based cycle for each fiscal quarter, as opposed to a calendar month-based cycle for each fiscal quarter. While the actual dates for the quarter-ends will change slightly each year, we believe that there are not any material differences when making quarterly comparisons.

2. DISPOSITIONS AND EXIT ACTIVITIES

**RedBlack Communications, Inc.**

On February 15, 2012, our senior management, as authorized by our Board of Directors, decided to divest our RedBlack Communications business. As a result of management's ongoing review of our business portfolio, management had determined that RedBlack offers limited opportunities to achieve the operating margin thresholds of our business and decided to refocus our operations on profitable growth opportunities presented in the other product lines that comprise our business segments, Battery & Energy Products and Communications Systems. Since 2008, our RedBlack Communications business has incurred significant operating losses. We are actively seeking to sell our RedBlack business as a going concern and will be engaging appropriate professionals to assist in that effort. We anticipate that the actions taken to divest the RedBlack Communications business will result in the elimination of approximately 30 jobs and the transfer of the RedBlack facility located in Hollywood, Maryland. We expect the RedBlack divestiture to occur within the next twelve months. Commencing with the first quarter of 2012 and concluding with the ultimate closing of the transaction, the results of the RedBlack operations and related divestiture costs will be reported as a discontinued operation.

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As a result, the presentation of results herein excludes the RedBlack operations from the results of continuing operations. The following amounts have been reported as discontinued operations for the three-month periods ended April 1, 2012 and April 3, 2011:

|   | Three-Month Periods Ended |                  |
|---|---------------------------|------------------|
|   | April 1,<br>2012          | April 3,<br>2011 |
| Net sales                                     | \$ 1,186                  | \$ 541           |
| Loss from discontinued operations             | (12)                      | (184)            |
| Provision for income taxes                    | 11                        | 12               |
| Loss from discontinued operations, net of tax | (23)                      | (196)            |

We cannot at this time determine an estimate or a range of estimates of the extent of the restructuring charges we will incur in connection with the RedBlack divestiture.

**Energy Services Business**

On March 8, 2011, our senior management, as authorized by our Board of Directors, decided to exit our Energy Services business, which included standby power and systems design, installation and maintenance activities. As a result of management's review of our business segments and products, and taking into account the lack of growth and profitability potential of the Energy Services segment as well as its sizeable operating losses, we determined it was appropriate to refocus our operations on profitable growth opportunities presented in our other segments, Battery & Energy Products and Communications Systems. In the fourth quarter of 2010, we recorded a non-cash impairment charge of \$13,793 to write-off the goodwill and intangible assets and certain fixed assets associated with the standby power portion of our Energy Services business.

The actions taken to exit our Energy Services segment resulted in the elimination of approximately 40 jobs and the closing of five facilities, primarily in California, Florida and Texas, over several months. As of the end of the second quarter of 2011, all exit activities with respect to our Energy Services segment were completed. As a result, the presentation of results herein excludes the Energy Services segment from the results of continuing operations. The following amounts have been reported as discontinued operations for the three-month periods ended April 1, 2012 and April 3, 2011:

|   | Three-Month Periods Ended |                  |
|---|---------------------------|------------------|
|   | April 1,<br>2012          | April 3,<br>2011 |
| Net sales                                     | \$                        | \$ 2,288         |
| Loss from discontinued operations             | (48)                      | (1,657)          |
| Provision for income taxes                    |                           |                  |
| Loss from discontinued operations, net of tax | (48)                      | (1,657)          |

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Included in the Loss from discontinued operations described above, we recorded the following exit charges:

|  | Three-Month Periods Ended |                  |
|--|---------------------------|------------------|
|  | April 1,<br>2012          | April 3,<br>2011 |
| Inventory and fixed asset write-downs            | \$                        | \$ 469           |
| Employee related, including termination benefits |                           | 266              |
| Lease termination costs                          |                           |                  |
| Other costs                                      |                           | 50               |
| <b>Total Exit Costs</b>                          | <b>\$</b>                 | <b>\$ 785</b>    |
| Cash Component                                   | \$                        | \$ 318           |

**3. INVENTORIES**

Inventories are stated at the lower of cost or market with cost determined under the first-in, first-out (FIFO) method. The composition of inventories was:

|                 | April 1, 2012 | December 31, 2011 |
|-----------------|---------------|-------------------|
| Raw materials   | \$ 20,995     | \$ 20,097         |
| Work in process | 3,945         | 4,770             |
| Finished goods  | 6,848         | 10,100            |
|                 | \$ 31,788     | \$ 34,967         |

**4. PROPERTY, PLANT AND EQUIPMENT**

Major classes of property, plant and equipment consisted of the following:

|                                      | April 1, 2012 | December 31, 2011 |
|--------------------------------------|---------------|-------------------|
| Land                                 | \$ 123        | \$ 123            |
| Buildings and leasehold improvements | 7,010         | 7,000             |
| Machinery and equipment              | 45,068        | 44,770            |
| Furniture and fixtures               | 1,910         | 1,894             |
| Computer hardware and software       | 3,822         | 3,815             |
| Construction in progress             | 1,019         | 641               |
|                                      | 58,952        | 58,243            |
| Less: Accumulated depreciation       | 46,752        | 45,655            |
|                                      | \$ 12,200     | \$ 12,588         |

Depreciation expense for property, plant and equipment was \$836 and \$1,022 for the three-month periods ended April 1, 2012 and April 3, 2011, respectively.



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## 5. GOODWILL AND INTANGIBLE ASSETS

## a. Goodwill

The following table summarizes the goodwill activity by segment for the three-month periods ended April 1, 2012 and April 3, 2011:

|   | Battery &<br>Energy Products | Communications<br>Systems | Discontinued<br>Operations | Total     |
|---|------------------------------|---------------------------|----------------------------|-----------|
| Balance at December 31, 2010            | \$ 4,758                     | \$ 11,493                 | \$ 2,025                   | \$ 18,276 |
| Effect of foreign currency translations | 17                           |                           |                            | 17        |
| Balance at April 3, 2011                | 4,775                        | 11,493                    | 2,025                      | 18,293    |
| Effect of foreign currency translations | 63                           |                           |                            | 63        |
| Balance at December 31, 2011            | 4,838                        | 11,493                    | 2,025                      | 18,356    |
| Effect of foreign currency translations | 22                           |                           |                            | 22        |
| Balance at April 1, 2012                | \$ 4,860                     | \$ 11,493                 | \$ 2,025                   | \$ 18,378 |

## b. Intangible Assets

The composition of intangible assets was:

|                           | Gross<br>Assets | April 1, 2012<br>Accumulated<br>Amortization | Net      |
|---------------------------|-----------------|--|----------|
| Trademarks                | \$ 3,564        | \$   | \$ 3,564 |
| Patents and technology    | 4,497           | 3,509  | 988      |
| Customer relationships    | 4,002           | 3,206  | 796      |
| Distributor relationships | 381             | 317  | 64       |
| Non-compete agreements    | 397             | 397  |          |
| Total intangible assets   | \$ 12,841       | \$ 7,429                                     | \$ 5,412 |

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|                           |              | December 31, 2011        |          |
|---------------------------|--------------|--------------------------|----------|
|                           | Gross Assets | Accumulated Amortization | Net      |
| Trademarks                | \$ 3,563     | \$                       | \$ 3,563 |
| Patents and technology    | 4,492        | 3,440                    | 1,052    |
| Customer relationships    | 3,993        | 3,143                    | 850      |
| Distributor relationships | 378          | 310                      | 68       |
| Non-compete agreements    | 396          | 396                      |          |
| Total intangible assets   | \$ 12,822    | \$ 7,289                 | \$ 5,533 |

Amortization expense for intangible assets was \$125 and \$157 for the three-month periods ended April 1, 2012 and April 3, 2011, respectively.

The change in the cost value of total intangible assets from December 31, 2011 to April 1, 2012 is a result of the effect of foreign currency translations.

## 6. DEBT

On February 17, 2010, we entered into a new senior secured asset based revolving credit facility ( Credit Facility ) of up to \$35,000 with RBS Business Capital, a division of RBS Asset Finance, Inc. ( RBS ). The proceeds from the Credit Facility can be used for general working capital purposes, general corporate purposes, and letter of credit foreign exchange support. The Credit Facility has a maturity date of February 17, 2013 ( Maturity Date ). The Credit Facility is secured by substantially all of our assets. At closing, we paid RBS a facility fee of \$263.

On February 18, 2010, we drew down \$9,870 from the Credit Facility to repay all outstanding amounts due under our previous credit facility with JP Morgan Chase Bank, N.A. and Manufacturers and Traders Trust Company. Our available borrowing under the Credit Facility fluctuates from time to time based upon amounts of eligible accounts receivable and eligible inventory. Available borrowings under the Credit Facility equals the lesser of (1) \$35,000 or (2) 85% of eligible accounts receivable plus the lesser of (a) up to 70% of the book value of our eligible inventory or (b) 85% of the appraised net orderly liquidation value of our eligible inventory. The borrowing base under the Credit Facility is further reduced by (1) the face amount of any letters of credit outstanding, (2) any liabilities under hedging contracts with RBS and (3) the value of any reserves as deemed appropriate by RBS. We are required to have at least \$3,000 available under the Credit Facility at all times.

On January 19, 2011, we entered into a First Amendment to the Credit Agreement ( First Amendment ) with RBS. The First Amendment amended the Credit Facility as follows:

(i) Included foreign (non-U.S.) accounts subject to credit insurance payable to RBS under the definition of eligible accounts receivable under the Credit Facility (for the determination of available borrowings - formerly, such accounts were not eligible without arranging letter of credit facilities satisfactory to RBS).

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(ii) Decreased the interest rate that will accrue on outstanding indebtedness, as set forth in the following table:

| Excess Availability                                     | LIBOR Rate Plus |
|---|-----------------|
| Greater than \$10,000                                   | 3.00%           |
| Greater than \$6,000 but less than or equal to \$10,000 | 3.25%           |
| Greater than \$3,000 but less than or equal to \$6,000  | 3.50%           |

Interest currently accrues on outstanding indebtedness under the Credit Facility at LIBOR plus 3.00%. We have the ability, in certain circumstances, to fix the interest rate for up to 90 days from the date of borrowing.

In addition to paying interest on the outstanding principal under the Credit Facility, we are required to pay an unused line fee of 0.50% on the unused portion of the \$35,000 Credit Facility. We must also pay customary letter of credit fees equal to the LIBOR rate and the applicable margin and any other customary fees or expenses of the issuing bank. Interest that accrues under the Credit Facility is to be paid monthly with all outstanding principal, interest and applicable fees due on the Maturity Date.

We are required to maintain a fixed charge coverage ratio of 1.20 to 1.00 or greater at all times as of and after March 28, 2010. As of April 1, 2012, our fixed charge coverage ratio was 3.50 to 1.00. Accordingly, we were in compliance with the financial covenants of the Credit Facility. All borrowings under the Credit Facility are subject to the satisfaction of customary conditions, including the absence of an event of default and accuracy of our representations and warranties. The Credit Facility also includes customary representations and warranties, affirmative covenants and events of default. If an event of default occurs, RBS would be entitled to take various actions, including accelerating the amount due under the Credit Facility, and all actions permitted to be taken by a secured creditor.

As of April 1, 2012, we had \$19 outstanding under the Credit Facility. At April 1, 2012, the interest rate on the asset based revolver component of the Credit Facility was 3.24%. As of April 1, 2012, the revolver arrangement had approximately \$13,369 of additional borrowing capacity, including outstanding letters of credit. At April 1, 2012, we had \$413 of outstanding letters of credit under the Credit Facility.

## 7. SHAREHOLDERS EQUITY

### a. Common Stock

In February 2012, we issued 16,271 shares of common stock to our non-employee directors, valued at \$76.

### b. Treasury Stock

At April 1, 2012 and December 31, 2011, we had 1,372,757 shares of treasury stock outstanding, valued at \$7,658.

### c. Stock Options

We have various stock-based employee compensation plans, for which we follow the provisions of the Financial Accounting Standards Board's (FASB) guidance on share-based payments, which requires that compensation cost relating to share-based payment transactions be recognized in the financial statements. The cost is measured at the grant date, based on the fair value of the award, and is recognized as an expense over the employee's requisite service period (generally the vesting period of the equity award).

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Our shareholders have approved various equity-based plans that permit the grant of stock options, restricted stock and other equity-based awards. In addition, our shareholders have approved certain grants of stock options outside of these plans.

In June 2004, shareholders adopted the 2004 Long-Term Incentive Plan ( LTIP ) pursuant to which we were authorized to issue up to 750,000 shares of common stock and grant stock options, restricted stock awards, stock appreciation rights and other stock-based awards. Through shareholder approved amendments to the LTIP in 2006, 2008 and 2011, the total number of authorized shares under the LTIP increased to 2,900,000.

Stock options granted under the LTIP are either Incentive Stock Options ( ISOs ) or Non-Qualified Stock Options ( NQSOs ). Key employees are eligible to receive ISOs and NQSOs; however, directors and consultants are eligible to receive only NQSOs. Most ISOs vest over a three- or five-year period and expire on the sixth or seventh anniversary of the grant date. All NQSOs issued to non-employee directors vest immediately and expire on either the sixth or seventh anniversary of the grant date. Some NQSOs issued to non-employees vest immediately and expire within three years; others have the same vesting characteristics as options issued to employees. As of April 1, 2012, there were 2,239,528 stock options outstanding under the LTIP.

On December 19, 2005, we granted our former President and Chief Executive Officer, John D. Kavazanjian, an option to purchase 48,000 shares of common stock at \$12.96 per share outside of any of our equity-based compensation plans, subject to shareholder approval. Shareholder approval was obtained on June 8, 2006. The stock option is fully vested and expires on June 8, 2013.

On March 7, 2008, in connection with his becoming employed by us, we granted our Chief Financial Officer and Treasurer, Philip A. Fain, an option to purchase 50,000 shares of common stock at \$12.74 per share outside of any of our equity-based compensation plans. The stock option is fully vested and expires on March 7, 2015.

On December 30, 2010, pursuant to the terms of his employment agreement, we granted our President and Chief Executive Officer, Michael D. Popielec, options to purchase shares of common stock under the LTIP as follows: (i) 50,000 shares at \$6.42, vesting in annual increments of 12,500 shares over a four-year period commencing December 30, 2011; (ii) 250,000 shares at \$6.42, vesting in annual increments of 62,500 shares over a four-year period commencing December 30, 2011; (iii) 200,000 shares at \$10.00, with vesting to begin on the date the stock reaches a closing price of \$10.00 per share for 15 trading days within a 30-day trading period, with such vesting in annual increments of 50,000 shares over the four anniversary dates of that date; and (iv) 200,000 shares at \$15.00, with vesting to begin on the date the stock reaches a closing price of \$15.00 per share for 15 trading days within a 30-day trading period, with such vesting in annual increments of 50,000 shares over the four anniversary dates of that date. All such options in items (i) and (ii) shall expire on December 30, 2017. All such options in items (iii) and (iv) shall expire as of the later of December 30, 2017 and five years after the initial vesting commences, but in no event later than December 30, 2020. The options set forth in items (ii), (iii) and (iv) were subject to shareholder approval of an amendment to the LTIP, which approval was obtained on June 7, 2011.

On January 3, 2011, pursuant to the terms of his employment agreement, we granted our President and Chief Executive Officer, Michael D. Popielec, an option to purchase 50,000 shares of common stock at \$6.58 under the LTIP. The option vests in annual increments of 12,500 shares over a four-year period commencing December 30, 2011. The option expires on December 30, 2017.

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In conjunction with FASB's guidance for share-based payments, we recorded compensation cost related to stock options of \$264 and \$239 for the three-month periods ended April 1, 2012 and April 3, 2011, respectively. As of April 1, 2012, there was \$1,493 of total unrecognized compensation cost related to outstanding stock options, which is expected to be recognized over a weighted average period of 2.14 years.

We use the Black-Scholes option-pricing model to estimate the fair value of non-market performance stock-based awards. The following weighted average assumptions were used to value non-market performance stock options granted during the three-month periods ended April 1, 2012 and April 3, 2011.

|  | Three-Month Periods Ended |               |
|--|---------------------------|---------------|
|  | April 1, 2012             | April 3, 2011 |
| Risk-free interest rate                | 0.66%                     | 1.64%         |
| Volatility factor                      | 62.93%                    | 54.61%        |
| Dividends                              | 0.00%                     | 0.00%         |
| Weighted average expected life (years) | 3.91                      | 3.89          |

We use a Monte Carlo simulation option-pricing model to estimate the fair value of market performance stock-based awards. There were no market performance stock options granted during the three-months ended April 1, 2012 and April 3, 2011.

We calculate expected volatility for stock options by taking an average of historical volatility over the past five years and a computation of implied volatility. The computation of expected term was determined based on historical experience of similar awards, giving consideration to the contractual terms of the stock-based awards and vesting schedules. The interest rate for periods within the contractual life of the award is based on the U.S. Treasury yield in effect at the time of grant.

Stock option activity for the first three months of 2012 is summarized as:

|   | Number<br>of Shares | Weighted<br>Average<br>Exercise Price<br>Per Share | Weighted<br>Average<br>Remaining<br>Contractual<br>Term | Aggregate<br>Intrinsic<br>Value |
|---|---------------------|--|---|---------------------------------|
| Shares under option at January 1, 2012          | 2,356,228           | \$ 8.34  |   |                                 |
| Options granted                                 | 31,000              | 3.98   |   |                                 |
| Options exercised                               | (24,000)            | 4.12   |   |                                 |
| Options forfeited                               | (4,200)             | 4.59   |   |                                 |
| Options expired                                 | (21,500)            | 17.12  |   |                                 |
| Shares under option at April 1, 2012            | 2,337,528           | \$ 8.25  | 4.76 years  | \$ 681                          |
| Vested and expected to vest as of April 1, 2012 | 2,074,104           | \$ 8.62  | 4.64 years  | \$ 565                          |
| Options exercisable at April 1, 2012            | 1,045,537           | \$ 9.21  | 2.89 years  | \$ 252                          |

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The total intrinsic value of stock options (which is the amount by which the stock price exceeded the exercise price of the options on the date of exercise) exercised during the three-month period ended April 1, 2012 was \$24.

FASB's guidance for share-based payments requires cash flows from excess tax benefits to be classified as a part of cash flows from financing activities. Excess tax benefits are realized tax benefits from tax deductions for exercised stock options in excess of the deferred tax asset attributable to stock compensation costs for such stock options. We did not record any excess tax benefits in the first three months of 2012 and 2011. Cash received from stock option exercises under our stock-based compensation plans for the three-month periods ended April 1, 2012 and April 3, 2011 was \$99 and \$53, respectively.

d. Restricted Stock Awards

No restricted stock was awarded during the three-month periods ended April 1, 2012 and April 3, 2011.

The activity of restricted stock awards for the three months of 2012 is summarized as follows:

|                               | Number of Shares | Weighted Average<br>Grant Date Fair Value |
|-------------------------------|------------------|---|
| Unvested at December 31, 2011 | 1,218            | \$ 11.33                                  |
| Granted                       |                  |   |
| Vested                        | (1,218)          | 11.33                                     |
| Forfeited                     |                  |   |
| Unvested at April 1, 2012     |                  | \$  |

We recorded compensation cost related to restricted stock awards of \$1 and \$(32) for the three-month periods ended April 1, 2012 and April 3, 2011, respectively. As of April 1, 2012, we had \$-0- of total unrecognized compensation cost related to restricted stock awards. The total fair value of these grants that vested during the three-month period ended April 1, 2012 was \$5.

8. INCOME TAXES

The asset and liability method, prescribed by FASB's guidance on the accounting for income taxes, is used in accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax basis of assets and liabilities and are measured using the enacted tax rates and laws that are expected to be in effect when the differences are expected to reverse.

For the three-month periods ended April 1, 2012 and April 3, 2011, we recorded \$102 and \$70, respectively, in income tax expense. The expense is primarily due to the recognition of deferred tax liabilities generated from goodwill and certain intangible assets that cannot be predicted to reverse for book purposes during our loss carryforward periods. The remaining expense in 2012 was primarily due to the income reported for our China operations during the period.

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Our effective consolidated tax rate for the three-month periods ended April 1, 2012 and April 3, 2011 was:

|   | Three-Month Periods Ended |            |
|---|---------------------------|------------|
|   | April 1,                  | April 3,   |
|   | 2012                      | 2011       |
| Income (Loss) from continuing operations before Incomes Taxes (a) | \$ (1,340)                | \$ (3,792) |
| Total Income Tax Provision (b)                                    | \$ 91                     | \$ 58      |
| Effective Tax Rate (b/a)  | 6.8%                      | 1.5%       |

The overall effective rate is the result of the combination of income and losses in each of our tax jurisdictions, which is particularly influenced by the fact that we have not recognized a deferred tax asset pertaining to cumulative historical losses for our U.S. operations and our U.K. subsidiary, as management does not believe, at this time, it is more likely than not that we will realize the benefit of these losses. We have substantial net operating loss carryforwards which offset taxable income in the United States. However, we remain subject to the alternative minimum tax in the United States. The alternative minimum tax limits the amount of net operating loss available to offset taxable income to 90% of the current year income. The alternative minimum tax did not have an impact on income taxes determined for three-month periods ended April 1, 2012 and April 3, 2011. The payment of the alternative minimum tax normally results in the establishment of a deferred tax asset; however, we have established a valuation allowance for our net U.S. deferred tax asset. Therefore, the expected payment of the alternative minimum tax does not result in a net deferred tax asset.

As of December 31, 2011, we had foreign and domestic net operating loss carryforwards totaling approximately \$57,977 available to reduce future taxable income. Foreign loss carryforwards of approximately \$11,479 can be carried forward indefinitely. The domestic net operating loss carryforwards of \$46,498 expire from 2019 through 2031. The domestic net operating loss carryforwards include approximately \$2,949 for which a benefit will be recorded in capital in excess of par value when realized.

We have adopted FASB's guidance for the accounting for uncertainty in income taxes. As a result of the implementation of this guidance, there was no cumulative effect adjustment for unrecognized tax benefits, which would have been accounted for as an adjustment to retained earnings.

Our unrecognized tax benefits related to uncertain tax positions at April 1, 2012 relate to Federal and various state jurisdictions. The following table summarizes the activity related to our unrecognized tax benefits:

|  | Three-Month Periods Ended |          |
|--|---------------------------|----------|
|  | April 1,                  | April 3, |
|  | 2012                      | 2011     |
| Balance at beginning of the period                           | \$ 6,779                  | \$       |
| Increases related to current year tax positions              |                           |          |
| Increases related to prior year tax positions                |                           |          |
| Decreases related to prior year tax positions                |                           |          |
| Expiration of statute of limitations for assessment of taxes |                           |          |
| Settlements  |                           |          |
| Balance at end of the period                                 | \$ 6,779                  | \$       |

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The total unrecognized tax benefit balance at April 1, 2012 is comprised of tax benefits that, if recognized, would result in a deferred tax asset and a corresponding increase in our valuation allowance. As a result, because the benefit would be offset by an increase in the valuation allowance, there would be no effect on the effective tax rate.

We are not required to accrue interest and penalties as the unrecognized tax benefits have been recorded as a decrease in our net operating loss carryforward. Interest and penalties would begin to accrue in the period in which the net operating loss carryforwards related to the uncertain tax positions are utilized. We do not expect our unrecognized tax benefits to change significantly over the next twelve months.

As a result of our operations, we file income tax returns in various jurisdictions including U.S. federal, U.S. state and foreign jurisdictions. We are routinely subject to examination by taxing authorities in these various jurisdictions. Our U.S. tax matters for the years 1999 through 2011 remain subject to examination by the Internal Revenue Service ( IRS ) due to our net operating loss carryforwards. Our U.S. tax matters for the years 1999 through 2011 remain subject to examination by various state and local tax jurisdictions due to our net operating loss carryforwards. Our tax matters for the years 2006 through 2011 remain subject to examination by the respective foreign tax jurisdiction authorities. The IRS has completed the examination of our 2009 U.S. federal income tax return, with no resulting material effect to our financial position or results of operations.

We have determined that a change in ownership, as defined under Internal Revenue Code Section 382, occurred during 2005 and 2006. As such, the domestic net operating loss carryforwards will be subject to an annual limitation estimated to be in the range of approximately \$12,000 to \$14,500. The unused portion of the annual limitation can be carried forward to subsequent periods. We believe such limitation will not impact our ability to realize the deferred tax asset. The use of our U.K. net operating loss carryforwards may be limited due to the change in our U.K. operation during 2008 from a manufacturing and assembly center to primarily a distribution and service center.

## 9. EARNINGS PER SHARE

On January 1, 2009, we adopted the provisions of FASB's guidance for determining whether instruments granted in share-based payment transactions are participating securities. The guidance requires that all outstanding unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (such as restricted stock awards granted by us) be considered participating securities. Because restricted stock awards are participating securities, we are required to apply the two-class method of computing basic and diluted earnings per share (the Two-Class Method ).

Basic earnings per share ( EPS ) is determined using the Two-Class Method and is computed by dividing earnings attributable to Ultralife common shareholders by the weighted-average shares outstanding during the period. The Two-Class Method is an earnings allocation formula that determines earnings per share for each class of common stock and participating security according to dividends declared and participation rights in undistributed earnings. Diluted EPS includes the dilutive effect of securities, if any, and reflects the more dilutive EPS amount calculated using the treasury stock method or the Two-Class Method. For the three-month periods ended April 1, 2012 and April 3, 2011, both the Two-Class Method and the treasury stock method calculations for diluted EPS yielded the same result.

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The computation of basic and diluted earnings per share is summarized as follows:

|  | Three-Month Period Ended |                  |
|--|--------------------------|------------------|
|  | April 1,<br>2012         | April 3,<br>2011 |
| Net Income (Loss) from continuing operations attributable to Ultralife   | \$ (1,431)               | \$ (3,837)       |
| Net Income (Loss) from continuing operations attributable to participating securities<br>(unvested restricted stock awards) (-0- and -0- shares, respectively) |                          |                  |
| Net Income (Loss) from continuing operations attributable to Ultralife common<br>shareholders (a)  | (1,431)                  | (3,837)          |
| Effect of Dilutive Securities  |                          |                  |
| Net Income (Loss) from continuing operations attributable to Ultralife common<br>shareholders - Adjusted (b)   | \$ (1,431)               | \$ (3,837)       |
| Net Income (Loss) from discontinued operations attributable to Ultralife common<br>shareholders (c)  | \$ (71)                  | \$ (1,853)       |
| Effect of Dilutive Securities  |                          |                  |
| Net Income (Loss) from discontinued operations attributable to Ultralife common<br>shareholders - Adjusted (d)   | \$ (71)                  | \$ (1,853)       |
| Average Common Shares Outstanding Basic (e)  | 17,358,000               | 17,276,000       |
| Effect of Dilutive Securities:   |                          |                  |
| Stock Options / Warrants   |                          |                  |
| Convertible Notes Payable  |                          |                  |
| Average Common Shares Outstanding Diluted (f)  | 17,358,000               | 17,276,000       |
| EPS Basic (a/e) - continuing operations  | \$ (0.08)                | \$ (0.22)        |
| EPS Basic (c/e) - discontinued operations  | \$ (0.01)                | \$ (0.11)        |
| EPS Diluted (b/f) - continuing operations  | \$ (0.08)                | \$ (0.22)        |
| EPS Diluted (d/f) - discontinued operations  | \$ (0.01)                | \$ (0.11)        |

There were 2,337,528 and 1,882,812 outstanding stock options, warrants and restricted stock awards for the three-month periods ended April 1, 2012 and April 3, 2011, respectively, that were not included in EPS as the effect would be anti-dilutive.

## 10. COMMITMENTS AND CONTINGENCIES

### a. Purchase Commitments

As of April 1, 2012, we have made commitments to purchase approximately \$560 of production machinery and equipment.

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## b. Product Warranties

We estimate future costs associated with expected product failure rates, material usage and service costs in the development of our warranty obligations. Warranty reserves are based on historical experience of warranty claims and generally will be estimated as a percentage of sales over the warranty period. In the event the actual results of these items differ from the estimates, an adjustment to the warranty obligation would be recorded. Changes in our product warranty liability during the first three months of 2012 were as follows:

|                                |            |
|--------------------------------|------------|
| Balance at December 31, 2011   | \$ 839     |
| Accruals for warranties issued | 60         |
| Settlements made               | (108)      |
| <br>Balance at April 1, 2012   | <br>\$ 791 |

## c. Contingencies and Legal Matters

We are subject to legal proceedings and claims that arise in the normal course of business. We believe that the final disposition of such matters will not have a material adverse effect on our financial position, results of operations or cash flows.

*Arista Power Litigation*

On September 23, 2011, we initiated an action against Arista Power, Inc. (Arista) and our former senior sales and engineering employee, David Modeen, in the State of New York Supreme Court, County of Wayne (Index No. 73379). In our Complaint, we allege that Arista recruited all but one of the members of its executive team from us, subsequently changed its business to compete directly with us by using our confidential information, and during the summer of 2011, recruited Modeen to become an Arista employee. We allege that, as a result of actions by Arista and Modeen: (i) Modeen has breached the terms of his Employee Confidentiality, Non-Disclosure, Non-Compete, Non-Disparagement and Assignment Agreement with us; (ii) Modeen has breached certain agreements, duties and obligations he owed us, including to protect and refrain from disclosing our trade secrets and confidential and proprietary information; (iii) Arista's employment of Modeen will inevitably lead to the disclosure and use of our trade secrets by Arista, in violation of Modeen's duties and obligations to us; (iv) Arista unlawfully induced Modeen to breach his agreements with and duties and obligations to us; and (v) Arista's recruitment and employment of Modeen has breached a subcontract between Arista and us. We seek damages as determined at trial and preliminary and permanent injunctive relief. The defendants have answered the allegations set forth in the Complaint, without asserting any counterclaims. Discovery has commenced and is ongoing.

On December 5, 2011, Arista served us with a Complaint it filed on November 29, 2011 in the State of New York Supreme Court, County of Monroe (Index No. 11-13896) against us, our officers, several of our directors, and an employee. In its Complaint, Arista alleges that we and our named defendants have violated the terms of a Confidentiality Agreement with Arista and have unfairly competed against Arista by unlawfully appropriating Arista's trade secrets and that as a result of such activity, Arista has incurred damages in excess of \$60,000. Arista seeks damages, an accounting, and preliminary and permanent injunctive relief.

On December 21, 2011, we and our officers, directors and employee named in Arista's Complaint filed a motion to dismiss Arista's Complaint against our officers, directors and employee as Arista's Complaint fails to state any cause of action against any of them and to dismiss the claim of fraud against our officers, directors and employee. Subsequently, Arista filed an Amended Complaint alleging essentially the same causes of action but adding additional factual allegations against us and our officers, directors and employee. In addition, Arista filed a motion to disqualify our outside legal counsel representing us and our officers, directors and employee in both Arista's Complaint and our Complaint against Arista. In response, we and our officers, directors and employee filed a new motion to dismiss Arista's Complaint against us in its entirety and seeking dismissal of the fraud claim against us. Arista's motion to disqualify our outside legal counsel was denied on February 10, 2012. On March 9, 2012, the Court issued its decision on our motion to dismiss, granting the motion to the extent of dismissing some claims against us, but denying the motion to dismiss the individuals from the lawsuit at this preliminary stage. On April 19, 2012, an Answer was filed on behalf of us, our officers, directors and employee.

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We initiated the September 23, 2011 Complaint against Arista Power to protect our customers, employees and shareholders from the unauthorized use and theft of our investments in intellectual property, trade secrets and confidential information by Arista and its employees. Protecting our collective intellectual property and know-how, developed at great cost to us to form our competitive position in the marketplace and create value for our shareholders, is a fundamental responsibility of all our employees.

We believe the November 29, 2011 Arista Complaint is retaliatory and without merit. Our development of the foundation for the new product concept for which Arista claims we allegedly used its trade secrets commenced in 2008, long prior to the departure of those individuals who now constitute the executive team of Arista. Furthermore, we believe the purported damage of \$60,000 being claimed by Arista is based solely on the reduction in its market capitalization between November 2009 and the filing date of the Complaint. This market value loss is totally unrelated to any actions on account of us, and claims for recovery of this or any other amount are legally and factually baseless.

Accordingly, we will vigorously pursue our complaint against Arista and defend what we believe to be a meritless action on the part of Arista Power.

*9-Volt Battery Litigation*

In July 2010, we were served with a summons and complaint filed in Japan by one of our 9-volt battery customers. The complaint alleges damages associated with claims of breach of warranty in an amount of approximately \$1,100. We dispute the customer's allegations against us and intend to vigorously defend the lawsuit. At this time, we have no basis for assessing whether we may incur any liability as a result of the lawsuit and no accrual has been made or reflected in the condensed consolidated financial statements as of April 1, 2012.

d. Post-Audits of Government Contracts

We had certain exigent, non-bid contracts with the U.S. government, which were subject to audit and final price adjustment, which resulted in decreased margins compared with the original terms of the contracts. As of April 1, 2012, there were no outstanding exigent contracts with the U.S. government. As part of its due diligence, the U.S. government has conducted post-audits of the completed exigent contracts to ensure that information used in supporting the pricing of exigent contracts did not differ materially from actual results. In September 2005, the Defense Contracting Audit Agency (DCAA) presented its findings related to the audits of three of the exigent contracts, suggesting a potential pricing adjustment of approximately \$1,400 related to reductions in the cost of materials that occurred prior to the final negotiation of these contracts. In addition, in June 2007, we received a request from the Office of Inspector General of the Department of Defense (DoD IG) seeking certain information and documents relating to our business with the Department of Defense. We cooperated with the DCAA audit and DoD IG inquiry by making available to government auditors and investigators our personnel and furnishing the requested information and documents. The DCAA Audit and DoD IG inquiry were consolidated and the US Attorney's Office represented the government in connection with these matters. Under applicable federal law, we may have been subject up to treble damages and penalties associated with the potential pricing adjustment. In light of the uncertainty, we decided to enter into discussions with the U.S. Attorney's Office in April 2011 to negotiate a settlement that would be in the best interests of our customers, employees and shareholders. On April 21, 2011, we were advised by the government that there was a \$2,730 settlement-in-principle to resolve all claims related to the contracts, subject to final approval by the Department of Justice. As a result, we recorded a \$2,730 charge as a reduction in revenues for the first quarter of 2011. On June 1, 2011, we entered into a Settlement Agreement with the United States of America, acting through the United States Department of Justice and on behalf of the Department of Defense which provides that we shall pay the U.S. \$2,700 plus accrued interest thereon at the rate of 2.625% per annum from May 6, 2011, with principal payments of \$1,000, \$567, \$567 and \$566 being due on June 8, 2011, December 1, 2011, June 1, 2012 and December 1, 2012, respectively. Each principal payment will be accompanied by a payment of accrued interest. As of April 1, 2012, we have made the first two required payments.

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e. Government Grants/Loans

In conjunction with the City of West Point, Mississippi, we applied for a Community Development Block Grant ( CDBG ) from the State of Mississippi for infrastructure improvements to our leased facility that is owned by the City of West Point, Mississippi. The CDBG was awarded and as of April 1, 2012, approximately \$480 has been distributed under the grant. Under an agreement with the City of West Point, we agreed to employ at least 30 full-time employees at the facility, of which 51% of the jobs had to be filled or made available to low or moderate income families, within three years of completion of the CDBG improvement activities. In addition, we agreed to invest at least \$1,000 in equipment and working capital into the facility within the first three years of operation of the facility. While we have yet to receive formal notice from the applicable government agency confirming the closure of the grant, we believe that both of these commitments were satisfied as of March 2011 and, therefore, have not recorded an accrual with respect to any potential liability for the grant amounts received under the CDBG.

In conjunction with Clay County, Mississippi, we applied for a Mississippi Rural Impact Fund Grant ( RIFG ) from the State of Mississippi for infrastructure improvements to our leased facility that is owned by the City of West Point, Mississippi. The RIFG was awarded and as of April 1, 2012, approximately \$150 has been distributed under the grant. Under an agreement with Clay County, we agreed to employ at least 30 full-time employees at the facility, of which 51% of the jobs had to be filled or made available to low or moderate income families, within two years of completion of the RIFG improvement activities. In September 2010, we received an extension for this commitment to March 31, 2011. In addition, we agreed to invest at least \$1,000 in equipment and working capital into the facility within the first three years of operation of the facility. While we have yet to receive formal notice from the applicable government agency confirming the closure of the grant, we believe that both of these commitments were satisfied as of March 2011 and, therefore, have not recorded an accrual with respect to any potential liability for the grant amounts received under the RIFG.

11. BUSINESS SEGMENT INFORMATION

On March 8, 2011, our senior management, as authorized by our Board of Directors, decided to exit our Energy Services business, which previously was a stand alone business segment. See Note 2 in these Notes to Condensed Consolidated Financial Statements for additional information.

On February 15, 2012, our senior management, as authorized by our Board of Directors, decided to divest our RedBlack Communications business, which previously was reported in the Communications Systems segment. See Note 2 in these Notes to Condensed Consolidated Financial Statements for additional information.

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We report our results in two operating segments: Battery & Energy Products and Communications Systems. The Battery & Energy Products segment includes: lithium 9-volt, cylindrical and various other non-rechargeable batteries, in addition to rechargeable batteries, uninterruptable power supplies, charging systems and accessories, such as cables. The Communications Systems segment includes: power supplies, cable and connector assemblies, RF amplifiers, amplified speakers, equipment mounts, case equipment, integrated communication system kits and communications and electronics systems design. We believe that reporting performance at the gross profit level is the best indicator of segment performance. As such, we report segment performance at the gross profit level and operating expenses as Corporate charges.

The components of segment performance were as follows:

**Three-Month Period Ended April 1, 2012**

|                                    | Battery &<br>Energy<br>Products | Communications<br>Systems | Discontinued<br>Operations | Corporate | Total      |
|------------------------------------|---------------------------------|---------------------------|----------------------------|-----------|------------|
| Revenues                           | \$ 20,082                       | \$ 7,419                  | \$                         | \$        | \$ 27,501  |
| Segment contribution               | 3,943                           | 2,650                     |                            | (7,882)   | (1,289)    |
| Interest expense, net              |                                 |                           |                            | (103)     | (103)      |
| Miscellaneous                      |                                 |                           |                            | 52        | 52         |
| Income taxes-current               |                                 |                           |                            | (79)      | (79)       |
| Income taxes-deferred              |                                 |                           |                            | (12)      | (12)       |
| Loss from discontinued operations  |                                 |                           | (71)                       |           | (71)       |
| Noncontrolling interest            |                                 |                           |                            |           |            |
| Net loss attributable to Ultralife |                                 |                           |                            |           | \$ (1,502) |
| Total assets                       | \$ 51,597                       | \$ 30,524                 | \$ 3,125                   | \$ 9,418  | \$ 94,664  |

**Three-Month Period Ended April 3, 2011**

|                                      | Battery &<br>Energy<br>Products | Communications<br>Systems | Discontinued<br>Operations | Corporate | Total      |
|--------------------------------------|---------------------------------|---------------------------|----------------------------|-----------|------------|
| Revenues                             | \$ 24,248                       | \$ 3,667                  | \$                         | \$        | \$ 27,915  |
| Segment contribution                 | 3,041                           | 1,373                     |                            | (8,350)   | (3,936)    |
| Interest expense, net                |                                 |                           |                            | (155)     | (155)      |
| Miscellaneous                        |                                 |                           |                            | 299       | 299        |
| Income taxes-current                 |                                 |                           |                            | (4)       | (4)        |
| Income taxes-deferred                |                                 |                           |                            | (54)      | (54)       |
| Loss from discontinued operations    |                                 |                           | (1,853)                    |           | (1,853)    |
| Noncontrolling interest              |                                 |                           |                            | 13        | 13         |
| Net income attributable to Ultralife |                                 |                           |                            |           | \$ (5,690) |
| Total assets                         | \$ 56,419                       | \$ 35,636                 | \$ 7,960                   | \$ 12,376 | \$ 112,391 |

**12. FAIR VALUE OF FINANCIAL INSTRUMENTS**

FASB's guidance for the disclosure regarding fair value of financial instruments requires disclosure of an estimate of the fair value of certain financial instruments. The fair value of financial instruments pursuant to FASB's guidance for the disclosure regarding fair value of financial instruments approximated their carrying values at April 1, 2012 and December 31, 2011. The fair value of cash, trade accounts receivable, trade accounts payable, accrued liabilities, and our revolving credit facility approximates carrying value due to the short-term nature of these instruments.

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**13. FIRE AT MANUFACTURING FACILITY**

In June 2011, we experienced a fire that damaged certain inventory and machinery and equipment at our facility in China. The fire occurred after business hours and was fully extinguished quickly with no injuries, and the plant was back in full operation shortly thereafter with no significant disruption in supply or service to customers. We maintain adequate insurance coverage for this operation.

The total amount of the loss pertaining to assets and the related expenses was approximately \$1,587. The majority of the insurance claim is related to the recovery of damaged inventory. As of April 1, 2012, we reflect a receivable from the insurance company relating to this claim of \$1,455, which is net of our deductible of approximately \$132. The deductible charge was expensed in the second quarter of 2011 and reflected as a component of cost of products sold in the Condensed Consolidated Statements of Operations.

**14. RECENT ACCOUNTING PRONOUNCEMENTS AND DEVELOPMENTS**

In June 2011, the FASB issued Accounting Standards Update (ASU) No. 2011-05, Comprehensive Income (Topic 220): Presentation of Comprehensive Income. ASU No. 2011-05 requires entities to present the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements of net income and other comprehensive income. ASU No. 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of changes in shareholders' equity, which is our current presentation. Further, in December 2011, the FASB issued ASU No. 2011-12 Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05. This update defers the effective date of ASU No. 2011-05's requirement to present on the face of the financial statements reclassification adjustments for each component of accumulated other comprehensive income in both net income and other comprehensive income so that the FASB can reconsider those requirements during calendar 2012. These standards are effective retrospectively for annual and interim reporting periods beginning after December 15, 2011, with early adoption permitted. The partial adoption of ASU No. 2011-05, as of January 1, 2012, only impacted the presentation of our consolidated financial statements and did not have a material impact on our consolidated results of operations and financial condition. The adoption of the deferred portions of ASU No. 2011-05 is not expected to have a material impact on our consolidated results of operations or financial condition.

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Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. This report contains certain forward-looking statements and information that are based on the beliefs of management as well as assumptions made by and information currently available to management. The statements contained in this report relating to matters that are not historical facts are forward-looking statements that involve risks and uncertainties, including, but not limited to, future demand for our products and services, addressing the process of U.S. defense procurement, reduced U.S. defense spending, the successful commercialization of our products, our reliance on certain key customers, the impairment of our intangible assets, general domestic and global economic conditions, including the uncertainty with government budget approvals, the unique risks associated with our Chinese operations, government and environmental regulations, finalization of non-bid government contracts, competition and customer strategies, technological innovations in the non-rechargeable and rechargeable battery industries, changes in our business strategy or development plans, capital deployment, business disruptions, including those caused by fires, raw material supplies, and other risks and uncertainties, certain of which are beyond our control. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may differ materially from those forward-looking statements described herein. When used in this report, the words anticipate, believe, estimate or expect or words of similar import are intended to identify forward-looking statements. For further discussion of certain of the matters described above and other risks and uncertainties, see Item 1A, Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2011.

Undue reliance should not be placed on our forward-looking statements. Except as required by law, we disclaim any obligation to update any factors or to publicly announce the results of any revisions to any of the forward-looking statements contained in this Quarterly Report on Form 10-Q to reflect new information, future events or other developments.

The following discussion and analysis should be read in conjunction with the accompanying Condensed Consolidated Financial Statements and Notes thereto appearing elsewhere in this Form 10-Q and our Consolidated Financial Statements and Notes thereto contained in our Form 10-K for the year ended December 31, 2011.

The financial information in this Management's Discussion and Analysis of Financial Condition and Results of Operations is presented in thousands of dollars, except for share and per share amounts. All figures presented below represent results from continuing operations, unless otherwise specified.

**General**

We offer products and services ranging from portable power solutions to communications and electronics systems. Through our engineering and collaborative approach to problem solving, we serve government, defense and commercial customers across the globe. We design, manufacture, install and maintain power and communications systems including: rechargeable and non-rechargeable batteries, communications and electronics systems and accessories, and custom engineered systems and solutions. We sell our products worldwide through a variety of trade channels, including original equipment manufacturers (OEMs), industrial and retail distributors, national retailers and directly to U.S. and international defense departments.

We report our results in two operating segments: Battery & Energy Products and Communications Systems. The Battery & Energy Products segment includes: lithium 9-volt, cylindrical and various other non-rechargeable batteries, in addition to rechargeable batteries, uninterruptable power supplies, charging systems and accessories, such as cables. The Communications Systems segment includes: power supplies, cable and connector assemblies, RF amplifiers, amplified speakers, equipment mounts, case equipment, integrated communication system kits and communications and electronics systems design. We believe that reporting performance at the gross profit level is the best indicator of segment performance. As such we report segment performance at the gross profit level and operating expenses as Corporate charges.

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We continually evaluate ways to grow, including opportunities to expand through mergers, acquisitions and joint ventures, which can broaden the scope of our products and services, expand operating and market opportunities and provide the ability to enter new lines of business synergistic with our portfolio of offerings.

On March 8, 2011, our senior management, as authorized by our Board of Directors, decided to exit our Energy Services business. As a result of management's review of our business segments and products, and taking into account the lack of growth and profitability potential of the Energy Services segment as well as its sizeable operating losses, we determined it was appropriate to refocus our operations on profitable growth opportunities presented in our other segments, Battery & Energy Products and Communications Systems. In the fourth quarter of 2010, we recorded a non-cash impairment charge of \$13,793 to write-off the goodwill and intangible assets and certain fixed assets associated with the standby power portion of our Energy Services business. The actions taken to exit our Energy Services business resulted in the elimination of approximately 40 jobs and the closing of five facilities, primarily in California, Florida and Texas. We completed all exit activities with respect to our Energy Services segment by the end of the second quarter of 2011, and have reclassified our Energy Services segment as a discontinued operation.

In connection with the exit activities described above, we recorded total restructuring charges of approximately \$2,924. The restructuring charges include approximately \$703 of employee-related costs, including termination benefits, approximately \$250 of lease termination costs, approximately \$941 of inventory and fixed asset write-downs and approximately \$1,030 of other associated costs. The cash component of the aggregate total restructuring charges was approximately \$1,984. Subsequent to the completion of our exit activities, adjustments have been made to estimates of certain reserves and accruals that existed at that time. These adjustments amount to \$46 and were due to the difference in our actual experience compared to our expectations as of the completion of our exit activities.

In 2011, we implemented a series of Lean initiatives throughout our entire organization. Lean is a disciplined management philosophy which is 100% focused on using resources more effectively and the elimination of non-value added functions to any process. The expected result is a reduction in costs through becoming more efficient.

On February 15, 2012, our senior management, as authorized by our Board of Directors, decided to divest our RedBlack Communications business. As a result of management's ongoing review of our business portfolio, management had determined that RedBlack offers limited opportunities to achieve the operating margin thresholds of our new business model and decided to refocus our operations on profitable growth opportunities presented in the other product lines that comprise our business segments, Battery & Energy Products and Communications Systems. Since 2008, our RedBlack Communications business has incurred significant operating losses. We are actively seeking to sell our RedBlack business as a going concern and will be engaging appropriate professionals to assist in that effort. We anticipate that the actions taken to divest the RedBlack Communications business will result in the elimination of approximately 30 jobs and the transfer of the RedBlack facility located in Hollywood, Maryland. We expect the RedBlack divestiture to occur within the next twelve months. Commencing with the first quarter of 2012 and concluding with the ultimate closing of the transaction, the results of the RedBlack operations and related divestiture costs will be reported as a discontinued operation.

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### Overview

Consolidated revenues for the three-month period ended April 1, 2012 decreased by \$414, or 1.5%, from the three-month period ended April 3, 2011, reflecting the completion of large non-recurring telematics orders in 2011. To a lesser extent, the decline in revenue resulted from slower government and defense order rate for rechargeable and non-rechargeable batteries partially offset by higher amplifier shipments and the impact of the \$2,730 charge related to the DCAA settlement during the first quarter of 2011.

Gross profit for the first quarter of 2012 was \$6,593, or 24.0% of revenues, compared to \$4,414, or 15.8% of revenues, for the same quarter a year ago. The increase is due to higher Communications Systems revenues and last year's \$2,730 DCAA settlement charge, partially offset by unfavorable manufacturing variances resulting from lower battery production levels in 2012.

Operating expenses decreased to \$7,882 during the three-month period ended April 1, 2012 compared to \$8,350 during the three-month period ended April 3, 2011, resulting from continued actions to reduce general and administrative expenses, focused spending in the development of new products, partially offset by the expansion of our sales force to increase our geographic coverage and penetrate new markets.

Adjusted EBITDA from continuing operations, defined as net income (loss) attributable to Ultralife before net interest expense, provision (benefit) for income taxes, depreciation and amortization, plus/minus expenses/income that we do not consider reflective of our ongoing continuing operations, amounted to \$109 in the first quarter of 2012 compared to \$(2,260) for the first quarter of 2011. See the section Adjusted EBITDA from continuing operations beginning on page 30 for a reconciliation of Adjusted EBITDA from continuing operations to net income (loss) attributable to Ultralife.

The outstanding balance on our credit facility was \$19 at April 1, 2012. By comparison, at April 3, 2011 and at December 31, 2011, the outstanding revolver balance under our credit facility was \$10,195 and \$0, respectively. The decrease is primarily attributable to our financial performance and cash generated from our Lean initiatives, including a reduction in inventory.

### Outlook

Management confirmed its previous guidance of year-over-year revenue growth approaching double digits with operating income growth expected to outpace revenue growth and generate an operating margin of approximately 7.0% to 7.5%. Management cautions that the timing of orders and shipments may cause variability in quarterly results.

### Results of Operations

#### *Three-month periods ended April 1, 2012 and April 3, 2011*

**Revenues.** Consolidated revenues for the three-month period ended April 1, 2012 amounted to \$27,501, a decrease of \$414, or 1.5%, from the \$27,915 reported in the same quarter in 2011. Battery & Energy Products sales decreased \$4,166, or 17.2%, from \$24,248 during the first quarter last year to \$20,082 during the first quarter this year. Revenues for Battery & Energy Products decreased due to the completion of large non-recurring telematics orders in 2011 and, to a lesser extent, a slower government and defense order rate for rechargeable and non-rechargeable batteries. In addition, in 2011 Battery & Energy Products revenue included a \$2,730 charge related to the DCAA settlement.

Communications Systems revenues increased \$3,752, or 102.3%, from \$3,667 during the first quarter last year to \$7,419 during the first quarter this year, reflecting our broader focus on large, global modernization opportunities, which resulted in higher amplifier sales.

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**Cost of Products Sold.** Cost of products sold totaled \$20,908 for the quarter ended April 1, 2012, a decrease of \$2,593, or 11.0%, from the \$23,501 reported for the same three-month period a year ago. Consolidated cost of products sold as a percentage of total revenue decreased from 84.2% for the three-month period ended April 3, 2011 to 76.0% for the three-month period ended April 1, 2012. Correspondingly, consolidated gross margin was 24.0% for the three-month period ended April 1, 2012, compared with 15.8% for the three-month period ended April 3, 2011, primarily attributable to higher Communications Systems revenues and last year's \$2,730 DCAA settlement charge, partially offset by unfavorable manufacturing variances resulting from lower battery production levels in 2012.

In our Battery & Energy Products segment, the cost of products sold decreased \$5,068, from \$21,207 during the three-month period ended April 3, 2011 to \$16,139 during the three-month period ended April 1, 2012. Battery & Energy Products gross profit for the first quarter of 2012 was \$3,943, or 19.6% of revenues, an increase of \$902 from gross profit of \$3,041, or 12.5% of revenues, for the first quarter of 2011. Battery & Energy Products gross margin as a percentage of revenues increased for the three-month period ended April 1, 2012, reflecting last year's DCAA settlement charge partially offset by the impact of unfavorable manufacturing variances resulting from lower production levels in 2012.

In our Communications Systems segment, the cost of products sold increased \$2,475 from \$2,294 during the three-month period ended April 3, 2011 to \$4,769 during the first quarter of 2012. Communications Systems gross profit for the first quarter of 2012 was \$2,650, or 35.7% of revenues, an increase of \$1,277 from gross profit of \$1,373, or 37.4% of revenues, for the first quarter of 2011. The decrease in gross margin as a percentage of revenue during 2012 is primarily due to reduced volume pricing for certain large projects.

**Operating Expenses.** Total operating expenses for the three-month period ended April 1, 2012 totaled \$7,882, a decrease of \$468 from \$8,350 for the three-month period ended April 3, 2011, resulting from continued actions to reduce general and administrative expenses, focused spending in the development of new products, partially offset by the expansion of our sales force to increase our geographic coverage and penetrate new markets.

Overall, operating expenses as a percentage of revenues decreased to 28.7% during the first quarter of 2012 from 29.9% reported in the first quarter of 2011. Amortization expense associated with intangible assets related to our acquisitions was \$125 for the first quarter of 2012 (\$60 in selling, general and administrative expenses and \$65 in research and development costs), compared with \$157 for the first quarter of 2011 (\$79 in selling, general, and administrative expenses and \$78 in research and development costs). Research and development costs were \$2,139 in the first quarter of 2012, a decrease of \$366, or 14.6%, from the \$2,505 reported in the first quarter of 2011, as we focused our spending on the development of new products with the highest estimated return on investment. Selling, general, and administrative expenses decreased \$102, or 1.7%, to \$5,743 during the first quarter of 2012 as compared to the first quarter of 2011, reflecting continued actions to reduce general and administrative expenses, partially offset by the expansion of our sales force to increase our geographic coverage and penetrate new markets.

**Other Income (Expense).** Other income (expense) totaled \$(51) for the first quarter of 2012, compared to \$144 for the first quarter of 2011. Interest expense, net of interest income, decreased \$52, to \$103 for the first quarter of 2012 from \$155 for the comparable period in 2011, as a result of lower average borrowings under our revolving credit facilities. Miscellaneous income/expense amounted to income of \$52 for the first quarter of 2012 compared with income of \$299 for the first quarter of 2011. The income in the first quarters of 2012 and 2011 was primarily due to transactions impacted by changes in foreign currencies relative to the U.S. dollar.

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**Income Taxes.** We reflected a tax provision of \$91 for the first quarter of 2012 compared with \$58 during the first quarter of 2011. The effective consolidated tax rate for the three-month periods ended April 1, 2012 and April 3, 2011 was:

|                                 | Three-Month Periods Ended |               |
|---------------------------------|---------------------------|---------------|
|                                 | April 1, 2012             | April 3, 2011 |
| Income before Incomes Taxes (a) | \$ (1,340)                | \$ (3,792)    |
| Total Income Tax Provision (b)  | \$ 91                     | \$ 58         |
| Effective Tax Rate (b/a)        | 6.8%                      | 1.5%          |

See Note 8 in the Notes to Condensed Consolidated Financial Statements for additional information regarding our income taxes.

We have determined that a change in ownership, as defined under Internal Revenue Code Section 382, occurred in 2005 and 2006. As such, the domestic net operating loss ( NOL ) carryforward will be subject to an annual limitation estimated to be in the range of approximately \$12,000 to \$14,500. The unused portion of the annual limitation can be carried forward to subsequent periods. Our ability to utilize NOL carryforwards due to successive ownership changes is currently limited to a minimum of approximately \$12,000 annually, plus the carryover from unused portions of the annual limitations. We believe such limitation will not impact our ability to realize the deferred tax asset.

In addition, certain of our NOL carryforwards are subject to U.S. alternative minimum tax such that carryforwards can offset only 90% of alternative minimum taxable income. This limitation did not have an impact on income taxes determined for the first quarters of 2012 and 2011. The use of our U.K. NOL carryforwards may be limited due to the change in the U.K. operation during 2008 from a manufacturing and assembly center to primarily a distribution and service center.

**Discontinued Operations.** Loss from discontinued operations, net of tax, totaled \$71 for the first quarter of 2012, compared to \$1,853 for the first quarter of 2011. The first quarter of 2012 loss includes operating results and costs related to our previously announced divestiture of our RedBlack Communication business and our exit from the Energy Services business which was completed in the second quarter of 2011. The loss from discontinued operations for the first quarter of 2011 reflects the unfavorable performance of the Energy Services business for that period. For more information, see Note 2 to the Condensed Consolidated Financial Statements.

**Net Income Attributable to Ultralife.** Net loss attributable to Ultralife and loss attributable to Ultralife common shareholders per diluted share was \$1,502 and \$0.09, respectively, for the three months ended April 1, 2012, compared to a net loss attributable to Ultralife and loss attributable to Ultralife common shareholders per diluted share of \$5,690 and \$0.33, respectively, for the first quarter of 2011. Average common shares outstanding used to compute diluted earnings per share increased from 17,276,000 in the first quarter of 2011 to 17,358,000 in the first quarter of 2012, mainly due to stock option exercises and shares of common stock issued to our non-employee directors.

**Adjusted EBITDA from continuing operations**

In evaluating our business, we consider and use Adjusted EBITDA from continuing operations, a non-GAAP financial measure, as a supplemental measure of our operating performance. We define Adjusted EBITDA from continuing operations as net income (loss) attributable to Ultralife before net interest expense, provision (benefit) for income taxes, depreciation and amortization, plus/minus expenses/income that we do not consider reflective of our ongoing continuing operations. We use Adjusted EBITDA from continuing operations as a supplemental measure to review and assess our operating performance and to enhance comparability between periods. We also believe the use of Adjusted EBITDA from continuing operations facilitates investors' use of operating performance comparisons from period to period and company to company by backing out potential differences caused by variations in such items as capital structures (affecting relative interest expense and stock-based compensation expense), the book amortization of intangible assets (affecting relative amortization expense), the age and book value of facilities and equipment (affecting relative depreciation expense) and other significant non-operating expenses or income. We also present Adjusted EBITDA from continuing operations because we believe it is frequently used by securities analysts, investors and other interested parties as a measure of financial performance. We reconcile Adjusted EBITDA from continuing operations to net income (loss) attributable to Ultralife, the most comparable financial measure under U.S. generally accepted accounting principles ( U.S. GAAP ).

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We use Adjusted EBITDA from continuing operations in our decision-making processes relating to the operation of our business together with U.S. GAAP financial measures such as income (loss) from operations. We believe that Adjusted EBITDA from continuing operations permits a comparative assessment of our operating performance, relative to our performance based on our U.S. GAAP results, while isolating the effects of depreciation and amortization, which may vary from period to period without any correlation to underlying operating performance, and of non-cash stock-based compensation, which is a non-cash expense that varies widely among companies. We believe that by limiting Adjusted EBITDA to continuing operations, we assist investors in gaining a better understanding of our business on a going forward basis. We provide information relating to our Adjusted EBITDA from continuing operations so that securities analysts, investors and other interested parties have the same data that we employ in assessing our overall operations. We believe that trends in our Adjusted EBITDA from continuing operations are a valuable indicator of our operating performance on a consolidated basis and of our ability to produce operating cash flows to fund working capital needs, to service debt obligations and to fund capital expenditures.

The term Adjusted EBITDA from continuing operations is not defined under U.S. GAAP, and is not a measure of operating income, operating performance or liquidity presented in accordance with U.S. GAAP. Our Adjusted EBITDA from continuing operations has limitations as an analytical tool, and when assessing our operating performance, Adjusted EBITDA from continuing operations should not be considered in isolation, or as a substitute for net income (loss) attributable to Ultralife or other consolidated statement of operations data prepared in accordance with U.S. GAAP. Some of these limitations include, but are not limited to, the following:

Adjusted EBITDA from continuing operations does not reflect (1) our cash expenditures or future requirements for capital expenditures or contractual commitments; (2) changes in, or cash requirements for, our working capital needs; (3) the interest expense, or the cash requirements necessary to service interest or principal payments, on our debt; (4) income taxes or the cash requirements for any tax payments; and (5) all of the costs associated with operating our business;

although depreciation and amortization are non-cash charges, the assets being depreciated and amortized often will have to be replaced in the future, and Adjusted EBITDA from continuing operations does not reflect any cash requirements for such replacements;

while stock-based compensation is a component of cost of products sold and operating expenses, the impact on our consolidated financial statements compared to other companies can vary significantly due to such factors as assumed life of the stock-based awards and assumed volatility of our common stock;

although discontinued operations does not reflect our current business operations, discontinued operations includes the costs we incurred by exiting our Energy Services business and divesting our RedBlack Communications business; and

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other companies may calculate Adjusted EBITDA from continuing operations differently than we do, limiting its usefulness as a comparative measure.

We compensate for these limitations by relying primarily on our U.S. GAAP results and using Adjusted EBITDA from continuing operations only supplementally. Adjusted EBITDA from continuing operations is calculated as follows for the periods presented:

|  | <b>Three-Month Periods Ended</b> |                          |
|--|----------------------------------|--------------------------|
|  | <b>April 1,<br/>2012</b>         | <b>April 3,<br/>2011</b> |
| Net income (loss) attributable to Ultralife          | \$ (1,502)                       | \$ (5,690)               |
| Add: interest expense, net                           | 103                              | 155                      |
| Add: income tax provision                            | 91                               | 58                       |
| Add: depreciation and amortization of financing fees | 880                              | 923                      |
| Add: amortization of intangible assets               | 125                              | 157                      |
| Add: stock-based compensation expense                | 341                              | 284                      |
| Add (Less): loss (gain) from discontinued operations | 71                               | 1,853                    |
| Adjusted EBITDA                                      | \$ 109                           | \$ (2,260)               |

**Liquidity and Capital Resources**

The following cash flow information is being presented net of continuing and discontinued operations.

As of April 1, 2012, cash and cash equivalents totaled \$4,136, a decrease of \$1,184 from December 31, 2011. During the three-month period ended April 1, 2012, we used \$1,200 of cash from operating activities as compared to the generation of \$2,066 for the three-month period ended April 3, 2011. The use of cash from operating activities in 2012 resulted mainly from our net loss of \$1,502 and use of approximately \$1,087 of cash for working capital due mainly to decreases in the balances of accounts receivable, accounts payable, and inventories.

We used \$209 in cash for investing activities during the first three months of 2012 compared with \$527 in cash used for investing activities in the same period in 2011. In the first three months of 2012, we spent \$209 to purchase plant, property and equipment. In the first three months of 2011, we spent \$492 to purchase plant, property and equipment and \$50 was used in connection with the contingent purchase price payout related to RPS Power Systems, Inc. In addition, we received \$15 in cash proceeds from dispositions of property, plant and equipment.

During the three-month period ended April 1, 2012, we generated \$118 in funds from financing activities compared to the generation of \$1,665 in funds in the same period of 2011. The financing activities in the first three months of 2012 included a \$19 inflow from borrowings on the revolver portion of our primary credit facility, and an inflow of \$99 from stock option exercises. The financing activities in the first three months of 2011 included a \$1,654 inflow from borrowings on the revolver portion of our primary credit facilities, and an inflow of \$53 from stock option exercises, partially offset by an outflow of \$42 for principal payments on debt and capital lease obligations.

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Inventory turnover for the first three months of 2012 was an annualized rate of approximately 3.0 turns per year, unchanged from the 3.0 turns for the full year of 2011.

As of April 1, 2012, we had made commitments to purchase approximately \$560 of production machinery and equipment, which we expect to fund through operating cash flows or the use of debt.

*Debt Commitments*

On February 17, 2010, we entered into a new senior secured asset based revolving credit facility ( *Credit Facility* ) of up to \$35,000 with RBS Business Capital, a division of RBS Asset Finance, Inc. ( *RBS* ). The proceeds from the Credit Facility can be used for general working capital purposes, general corporate purposes, and letter of credit foreign exchange support. The Credit Facility has a maturity date of February 17, 2013 ( *Maturity Date* ). The Credit Facility is secured by substantially all of our assets. At closing, we paid RBS a facility fee of \$263.

On February 18, 2010, we drew down \$9,870 from the Credit Facility to repay all outstanding amounts due under our previous credit facility with JP Morgan Chase Bank, N.A. and Manufacturers and Traders Trust Company. Our available borrowing under the Credit Facility fluctuates from time to time based upon amounts of eligible accounts receivable and eligible inventory. Available borrowings under the Credit Facility equals the lesser of (1) \$35,000 or (2) 85% of eligible accounts receivable plus the lesser of (a) up to 70% of the book value of our eligible inventory or (b) 85% of the appraised net orderly liquidation value of our eligible inventory. The borrowing base under the Credit Facility is further reduced by (1) the face amount of any letters of credit outstanding, (2) any liabilities under hedging contracts with RBS and (3) the value of any reserves as deemed appropriate by RBS. We are required to have at least \$3,000 available under the Credit Facility at all times.

On January 19, 2011, we entered into a First Amendment to the Credit Agreement ( *First Amendment* ) with RBS. The First Amendment amended the Credit Facility as follows:

(i) Included foreign (non-U.S.) accounts subject to credit insurance payable to RBS under the definition of eligible accounts receivable under the Credit Facility (for the determination of available borrowings - formerly, such accounts were not eligible without arranging letter of credit facilities satisfactory to RBS).

(ii) Decreased the interest rate that will accrue on outstanding indebtedness, as set forth in the following table:

| Excess Availability                                     | LIBOR Rate Plus |
|---|-----------------|
| Greater than \$10,000                                   | 3.00%           |
| Greater than \$6,000 but less than or equal to \$10,000 | 3.25%           |
| Greater than \$3,000 but less than or equal to \$6,000  | 3.50%           |

Interest currently accrues on outstanding indebtedness under the Credit Facility at LIBOR plus 3.00%. We have the ability, in certain circumstances, to fix the interest rate for up to 90 days from the date of borrowing.

In addition to paying interest on the outstanding principal under the Credit Facility, we are required to pay an unused line fee of 0.50% on the unused portion of the \$35,000 Credit Facility. We must also pay customary letter of credit fees equal to the LIBOR rate and the applicable margin and any other customary fees or expenses of the issuing bank. Interest that accrues under the Credit Facility is to be paid monthly with all outstanding principal, interest and applicable fees due on the Maturity Date.

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We are required to maintain a fixed charge coverage ratio of 1.20 to 1.00 or greater at all times as of and after March 28, 2010. As of April 1, 2012, our fixed charge coverage ratio was 3.50 to 1.00. Accordingly, we were in compliance with the financial covenants of the Credit Facility. All borrowings under the Credit Facility are subject to the satisfaction of customary conditions, including the absence of an event of default and accuracy of our representations and warranties. The Credit Facility also includes customary representations and warranties, affirmative covenants and events of default. If an event of default occurs, RBS would be entitled to take various actions, including accelerating the amount due under the Credit Facility, and all actions permitted to be taken by a secured creditor.

As of April 1, 2012, we had \$19 outstanding under the Credit Facility. At April 1, 2012, the interest rate on the asset based revolver component of the Credit Facility was 3.24%. As of April 1, 2012, the revolver arrangement had approximately \$13,369 of additional borrowing capacity, including outstanding letters of credit. At April 1, 2012, we had \$413 of outstanding letters of credit under the Credit Facility.

### *Equity Transactions*

In some of our recent acquisitions, we utilized securities as consideration in these transactions in part to reduce the need to draw on the liquidity provided by our cash and cash equivalents and revolving credit facility.

See Note 7 in the Notes to Condensed Consolidated Financial Statements for additional information.

### *Other Matters*

We periodically explore various sources of liquidity to ensure financing flexibility, including leasing alternatives, issuing new or refinancing existing debt, and raising equity through private or public offerings. Although we stay abreast of such financing alternatives, we believe we have the ability during the next 12 months to finance our operations primarily through internally generated funds or through the use of additional financing that currently is available to us. In the event that we are unable to finance our operations with internally generated funds or through the use of additional financing from our Credit Facility, we may need to seek additional credit or access the capital markets for additional funds. We can provide no assurance that we would be successful in this regard.

With respect to our battery products, we typically offer warranties against any defects due to product malfunction or workmanship for a period up to one year from the date of purchase. With respect to our communications accessory products, we typically offer a three-year warranty. We provide for a reserve for these potential warranty expenses, which is based on an analysis of historical warranty issues. There is no assurance that future warranty claims will be consistent with past history, and in the event we experience a significant increase in warranty claims, there is no assurance that our reserves would be sufficient. This could have a material adverse effect on our business, financial condition and results of operations.

### Critical Accounting Policies

Management exercises judgment in making important decisions pertaining to choosing and applying accounting policies and methodologies in many areas. Not only are these decisions necessary to comply with U.S. generally accepted accounting principles, but they also reflect management's view of the most appropriate manner in which to record and report our overall financial performance. All accounting policies are important, and all policies described in Note 1 ( Summary of Operations and Significant Accounting Policies ) to our Consolidated Financial Statements in our 2011 Annual Report on Form 10-K should be reviewed for a greater understanding of how our financial performance is recorded and reported.

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During the first three months of 2012, there were no significant changes in the manner in which our significant accounting policies were applied or in which related assumptions and estimates were developed.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

During the three months ended April 3, 2012, there were no material changes to our quantitative and qualitative disclosures about market risk as presented in Item 7A of Part II of our Annual Report on Form 10-K for the year ended December 31, 2011.

Item 4. CONTROLS AND PROCEDURES

*Evaluation Of Disclosure Controls And Procedures*

Our president and chief executive officer (principal executive officer) and our chief financial officer and treasurer (principal financial officer) have evaluated our disclosure controls and procedures (as defined in Securities Exchange Act Rules 13a-15(e)) as of the end of the period covered by this quarterly report. Based on this evaluation, our president and chief executive officer and chief financial officer and treasurer concluded that our disclosure controls and procedures were effective as of such date.

*Changes In Internal Control Over Financial Reporting*

There has been no change in our internal control over financial reporting (as defined in Securities Exchange Act Rule 13a-15(f)) that occurred during the fiscal quarter covered by this quarterly report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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**PART II OTHER INFORMATION**

Item 1. Legal Proceedings

We are subject to legal proceedings and claims that arise in the normal course of business. We believe that the final disposition of such matters will not have a material adverse effect on our financial position, results of operations or cash flows.

*Arista Power Litigation*

On September 23, 2011, we initiated an action against Arista Power, Inc. (Arista) and our former senior sales and engineering employee, David Modeen, in the State of New York Supreme Court, County of Wayne (Index No. 73379). In our Complaint, we allege that Arista recruited all but one of the members of its executive team from us, subsequently changed its business to compete directly with us by using our confidential information, and during the summer of 2011, recruited Modeen to become an Arista employee. We allege that, as a result of actions by Arista and Modeen: (i) Modeen has breached the terms of his Employee Confidentiality, Non-Disclosure, Non-Compete, Non-Disparagement and Assignment Agreement with us; (ii) Modeen has breached certain agreements, duties and obligations he owed us, including to protect and refrain from disclosing our trade secrets and confidential and proprietary information; (iii) Arista's employment of Modeen will inevitably lead to the disclosure and use of our trade secrets by Arista, in violation of Modeen's duties and obligations to us; (iv) Arista unlawfully induced Modeen to breach his agreements with and duties and obligations to us; and (v) Arista's recruitment and employment of Modeen has breached a subcontract between Arista and us. We seek damages as determined at trial and preliminary and permanent injunctive relief. The defendants have answered the allegations set forth in the Complaint, without asserting any counterclaims. Discovery has commenced and is ongoing.

On December 5, 2011, Arista served us with a Complaint it filed on November 29, 2011 in the State of New York Supreme Court, County of Monroe (Index No. 11-13896) against us, our officers, several of our directors, and an employee. In its Complaint, Arista alleges that we and our named defendants have violated the terms of a Confidentiality Agreement with Arista and have unfairly competed against Arista by unlawfully appropriating Arista's trade secrets and that as a result of such activity, Arista has incurred damages in excess of \$60,000. Arista seeks damages, an accounting, and preliminary and permanent injunctive relief.

On December 21, 2011, we and our officers, directors and employee named in Arista's Complaint filed a motion to dismiss Arista's Complaint against our officers, directors and employee as Arista's Complaint fails to state any cause of action against any of them and to dismiss the claim of fraud against our officers, directors and employee. Subsequently, Arista filed an Amended Complaint alleging essentially the same causes of action but adding additional factual allegations against us and our officers, directors and employee. In addition, Arista filed a motion to disqualify our outside legal counsel representing us and our officers, directors and employee in both Arista's Complaint and our Complaint against Arista. In response, we and our officers, directors and employee filed a new motion to dismiss Arista's Complaint against us in its entirety and seeking dismissal of the fraud claim against us. Arista's motion to disqualify our outside legal counsel was denied on February 10, 2012. On March 9, 2012, the Court issued its decision on our motion to dismiss, granting the motion to the extent of dismissing some claims against us, but denying the motion to dismiss the individuals from the lawsuit at this preliminary stage. On April 19, 2012, an Answer was filed on behalf of us, our officers, directors and employee.

We initiated the September 23, 2011 Complaint against Arista Power to protect our customers, employees and shareholders from the unauthorized use and theft of our investments in intellectual property, trade secrets and confidential information by Arista and its employees. Protecting our collective intellectual property and know-how, developed at great cost to us to form our competitive position in the marketplace and create value for our shareholders, is a fundamental responsibility of all our employees.

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We believe the November 29, 2011 Arista Complaint is retaliatory and without merit. Our development of the foundation for the new product concept for which Arista claims we allegedly used its trade secrets commenced in 2008, long prior to the departure of those individuals who now constitute the executive team of Arista. Furthermore, we believe the purported damage of \$60,000 being claimed by Arista is based solely on the reduction in its market capitalization between November 2009 and the filing date of the Complaint. This market value loss is totally unrelated to any actions on account of us, and claims for recovery of this or any other amount are legally and factually baseless.

Accordingly, we will vigorously pursue our complaint against Arista and defend what we believe to be a meritless action on the part of Arista Power.

Item 6. Exhibits

Exhibit

| Index    | Description of Document  | Incorporated By Reference from:  |
|----------|--|--|
| 10.1     | Amendment No. 4 to Ultralife Corporation Amended and Restated Long-Term Incentive Plan | Exhibit 4.5 of the Registration Statement on Form S-8 filed on January 30, 2012, File No. 333-179235 |
| 31.1     | Rule 13a-14(a) / 15d-14(a) CEO Certifications  | Filed herewith   |
| 31.2     | Rule 13a-14(a) / 15d-14(a) CFO Certifications  | Filed herewith   |
| 32       | Section 1350 Certifications  | Filed herewith   |
| *101.INS | XBRL Instance Document   |  |
| *101.SCH | XBRL Taxonomy Extension Schema Document  |  |
| *101.CAL | XBRL Taxonomy Calculation Linkbase Document  |  |
| *101.LAB | XBRL Taxonomy Label Linkbase Document  |  |
| *101.PRE | XBRL Taxonomy Presentation Linkbase Document   |  |
| *101.DEF | XBRL Taxonomy Definition Document  |  |

Management contract or compensatory plan or arrangement.

\* Pursuant to Rule 406T of Regulation S-T, the information in this exhibit is deemed not filed or part of a registration statement or prospectus for purposes of Section 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is otherwise not subject to liability under these sections.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**ULTRALIFE CORPORATION**

(Registrant)

Date: May 10, 2012

By: /s/ Michael D. Popielec  
Michael D. Popielec  
President and Chief Executive Officer

(Principal Executive Officer)

Date: May 10, 2012

By: /s/ Philip A. Fain  
Philip A. Fain  
Chief Financial Officer and Treasurer

(Principal Financial Officer and Principal Accounting Officer)

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Index to Exhibits

|         |  |
|---------|--|
| 31.1    | Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2    | Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32      | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002   |
| 101.INS | XBRL Instance Document   |
| 101.SCH | XBRL Taxonomy Extension Schema Document  |
| 101.CAL | XBRL Taxonomy Calculation Linkbase Document  |
| 101.LAB | XBRL Taxonomy Label Linkbase Document  |
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