

# NAPCO SECURITY SYSTEMS INC

## FORM 10-Q (Quarterly Report)

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Address	333 BAYVIEW AVE AMITYVILLE, NY 11701
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# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

## FORM 10-Q

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

**FOR THE QUARTERLY PERIOD ENDED: DECEMBER 31, 2008**

OR

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

**FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_.**

*Commission File number: 0-10004*

## NAPCO SECURITY TECHNOLOGIES, INC.

(Exact name of Registrant as specified in its charter)

Delaware	11-2277818
----- (State or other jurisdiction of incorporation of organization)	----- (IRS Employer Identification Number)
333 Bayview Avenue Amityville, New York	11701
----- (Address of principal executive offices)	----- (Zip Code)
(631) 842-9400	
----- (Registrant's telephone number including area code)	

### **NAPCO SECURITY SYSTEMS, INC.**

(Former name, former address and former fiscal year if  
changed from 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 and Exchange Act of 1934 during the preceding 12 months (or 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 is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition 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 in Rule 12b-2 of the Exchange Act):

Yes  No

Number of shares outstanding of each of the issuer's classes of common stock, as  
of: **FEBRUARY 9, 2009**

**COMMON STOCK, \$.01 PAR VALUE PER SHARE 19,095,713**

**PART I: FINANCIAL INFORMATION**

**ITEM 1. Financial Statements**

**NAPCO SECURITY TECHNOLOGIES, INC. AND SUBSIDIARIES  
INDEX - DECEMBER 31, 2008**

Condensed Consolidated Balance Sheets December 31, 2008 and June 30, 2008 3

Condensed Consolidated Statements of Income for the Three Months ended December 31, 2008 and 2007 4

Condensed Consolidated Statements of Income for the Six Months ended December 31, 2008 and 2007 5

Condensed Consolidated Statements of Cash Flows for the Six Months ended December 31, 2008 and 2007 6

**Notes to Condensed Consolidated Financial Statements 7**

**ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations 16**

**ITEM 3. Quantitative and Qualitative Disclosures About Market Risk 21**

**ITEM 4. Controls and Procedures 21**

**PART II: OTHER INFORMATION 22**

**SIGNATURE PAGE 23**

**PART I: FINANCIAL INFORMATION**

**ITEM 1. Financial Statements**

**NAPCO SECURITY TECHNOLOGIES, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS**

ASSETS	December 31, 2008 (unaudited)	June 30, 2008
	(in thousands, except share data)	
Current Assets:		
Cash and cash equivalents	\$ 5,631	\$ 2,765
Accounts receivable, net of reserves	22,997	25,823
Inventories	27,602	19,548
Prepaid expenses and other current assets	1,242	1,121
Deferred income taxes	790	769
	58,262	50,026
Total Current Assets		
Inventories - non-current, net	9,051	7,724
Property, plant and equipment, net	9,455	8,989
Intangible assets, net	16,238	--
Goodwill, net	10,609	9,686
Other assets	400	298
	104,015	76,723
Total Assets	\$ 104,015	\$ 76,723
LIABILITIES AND STOCKHOLDERS' EQUITY		
-----		
Current Liabilities:		
Current portion of long-term debt	\$ 3,572	\$ --
Accounts payable	5,714	4,857
Accrued expenses	1,387	1,333
Accrued salaries and wages	2,114	2,543
Accrued income taxes	12	--
	12,799	8,733
Total Current Liabilities		
Long-term debt	34,635	12,400
Accrued income taxes	305	294
Deferred income taxes	1,719	1,607
Minority interest in subsidiary	147	147
	49,605	23,181
Total Liabilities		
Commitments and Contingencies		
Stockholders' Equity:		
Common stock, par value \$.01 per share;		
40,000,000 shares authorized, 20,095,713		
and 20,092,473 shares issued and 19,095,713		
and 19,092,473 shares outstanding,		
respectively	201	201
Additional paid-in capital	13,638	13,424
Retained earnings	46,186	45,532
	60,025	59,157
Less: Treasury Stock, at cost (1,000,000 shares)	(5,615)	(5,615)
	54,410	53,542
Total stockholders' equity		
Total Liabilities and Stockholders' Equity	\$ 104,015	\$ 76,723

See accompanying notes to condensed consolidated financial statements.

**NAPCO SECURITY TECHNOLOGIES, INC AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME (unaudited)**

Three Months Ended  
December 31,

2008 2007

(in thousands, except share and per share data)

Net sales	\$ 19,079	\$ 16,166
Cost of sales	12,865	10,719
	-----	-----
Gross Profit	6,214	5,447
Selling, general and administrative expenses	5,448	4,162
	-----	-----
Operating Income	766	1,285
	-----	-----
Other expense:		
Interest expense, net	429	224
Other (income) expense, net	(54)	11
	-----	-----
Total Other expense	375	235
	-----	-----
Income Before Minority Interest and Provision for Income Taxes	391	1,050
Minority interest in loss of subsidiary	70	20
	-----	-----
Income Before Provision (Benefit) for Income Taxes	461	1,070
Provision (Benefit) for income taxes	129	(102)
	-----	-----
Net Income	\$ 332	\$ 1,172
	=====	=====
Earnings per share:		
Basic	\$ 0.02	\$ 0.06
	=====	=====
Diluted	\$ 0.02	\$ 0.06
	=====	=====
Weighted average number of shares outstanding:		
Basic	19,095,713	19,297,252
	=====	=====
Diluted	19,095,713	19,820,906

See accompanying notes to condensed consolidated financial statements.

**NAPCO SECURITY TECHNOLOGIES, INC AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME (unaudited)**

Six Months Ended  
December 31,

2008 2007

(in thousands, except share and per share data)

Net sales	\$	36,562	\$	30,042
Cost of sales		24,742		19,371
		-----		-----
Gross Profit		11,820		10,671
Selling, general and administrative expenses		10,224		8,583
		-----		-----
Operating Income		1,596		2,088
		-----		-----
Other expense:				
Interest expense, net		744		419
Other expense, net		25		18
		-----		-----
Total Other expense		769		437
		-----		-----
Income Before Minority Interest and Provision for Income Taxes		827		1,651
Minority interest in loss of subsidiary		112		59
		-----		-----
Income Before Provision for Income Taxes		939		1,710
Provision for income taxes		285		163
		-----		-----
Net Income	\$	654	\$	1,547
		=====		=====
Earnings per share:				
Basic	\$	0.03	\$	0.08
		=====		=====
Diluted	\$	0.03	\$	0.08
		=====		=====
Weighted average number of shares outstanding:				
Basic		19,095,537		19,432,471
		=====		=====
Diluted		19,206,453		19,985,412
		=====		=====

See accompanying notes to condensed consolidated financial statements.

**NAPCO SECURITY TECHNOLOGIES, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)**

	Six Months Ended December 31,	
	2008	2007
	(in thousands)	
Cash Flows from Operating Activities:		
Net income	\$ 654	\$ 1,547
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	888	561
Provision for (Recovery of) doubtful accounts	84	(35)
Change to inventory obsolescence reserve	(20)	--
Deferred income taxes	91	(340)
Non-cash stock based compensation expense	208	151
Changes in operating assets and liabilities, net of acquisition effects:		
Accounts receivable	4,578	4,363
Inventories	(2,621)	(4,431)
Prepaid expenses and other current assets	(9)	(72)
Other assets	65	(181)
Accounts payable, accrued expenses, accrued salaries and wages, and accrued income taxes	(766)	(275)
	3,152	1,288
Cash Flows Used in Investing Activities:		
Cash used in business acquisition, net of cash acquired of \$520	(24,581)	--
Purchases of property, plant and equipment	(326)	(447)
	(24,907)	(447)
Cash Flows from Financing Activities:		
Proceeds from exercise of employee stock options	6	2
Proceeds from acquisition financing	25,000	--
Proceeds from long-term debt borrowings	2,200	3,500
Principal payments on long-term debt	(2,393)	(2,000)
Cash paid for deferred financing costs	(192)	--
Cash paid for purchase of treasury stock	--	(3,120)
	24,621	(1,618)
Net increase (decrease) in Cash and Cash Equivalents	2,866	(777)
Cash and Cash Equivalents, Beginning of Period	2,765	1,748
Cash and Cash Equivalents, End of Period	\$ 5,631	\$ 971
Cash Paid During the Period for:		
Interest	\$ 624	\$ 377
Income taxes	\$ 125	\$ --
Non-cash Investing activities:		
Adjustment to Retained earnings relating to adoption of FIN 48	\$ --	\$ 485
Accrued Business Acquisition costs	\$ 295	\$ --
Debt assumed in the Acquisition	\$ 1,000	\$ --

See accompanying notes to condensed consolidated financial statements.

# NAPCO SECURITY TECHNOLOGIES, INC AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

### 1.) Summary of Significant Accounting Policies and Other Disclosures

The accompanying Condensed Consolidated Financial Statements are unaudited. In management's opinion, all adjustments (consisting of only normal recurring accruals) necessary for a fair presentation have been made. The results of operations for the period ended December 31, 2008 are not necessarily indicative of results that may be expected for any other interim period or for the full year.

The unaudited Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and related notes contained in the Company's Annual Report on Form 10-K for the year ended June 30, 2008. The accounting policies used in preparing these unaudited Condensed Consolidated Financial Statements are consistent with those described in the June 30, 2008 Consolidated Financial Statements. However, for interim financial statements, inventories are calculated using a gross profit percentage. In addition, the Condensed Consolidated Balance Sheet was derived from the audited financial statements but does not include all disclosures required by Generally Accepted Accounting Principles ("GAAP").

The consolidated financial statements include the accounts of Napco Security Technologies, Inc. and all of its wholly-owned subsidiaries, including those of Marks USA, a newly formed subsidiary which acquired substantially all of the assets and certain liabilities of G. Marks Hardware, Inc. ("Marks") acquired on August 18, 2008. The Company has also consolidated a 51%-owned joint venture. The 49% interest, held by a third party, is reflected as minority interest. All inter-company balances and transactions have been eliminated in consolidation.

The Company has made a number of estimates and assumptions relating to the assets and liabilities, the disclosure of contingent assets and liabilities and the reporting of revenues and expenses to prepare these financial statements in conformity with accounting principles generally accepted in the United States. Actual results could differ from those estimates.

#### **Seasonality**

The Company's fiscal year begins on July 1 and ends on June 30. Historically, the end users of Napco's products want to install its products prior to the summer; therefore sales of its products peak in the period April 1 through June 30, the Company's fiscal fourth quarter, and are reduced in the period July 1 through September 30, the Company's fiscal first quarter. To a lesser degree, sales in Europe are also adversely impacted in the Company's first fiscal quarter because of European vacation patterns, i.e., many distributors and installers are closed for the month of August. In addition, demand is affected by the housing and construction markets.

#### **Advertising and Promotional Costs**

Advertising and promotional costs are included in "Selling, General and Administrative" expenses in the condensed consolidated statements of income and are expensed as incurred. Advertising expense for the three months ended December 31, 2008 and 2007 was \$363,000 and \$206,000, respectively. Advertising expense for the six months ended December 31, 2008 and 2007 was \$664,000 and \$729,000, respectively.

#### **Research and Development Costs**

Research and development costs are included in "Cost of Sales" in the condensed consolidated statements of income and are expensed as incurred. Research and development expense for the three months ended December 31, 2008 and 2007 was \$1,318,000 and \$1,390,000, respectively. Research and development expense for the six months ended December 31, 2008 and 2007 was \$2,630,000 and \$2,722,000, respectively.

#### **Business Concentration and Credit Risk**

An entity is more vulnerable to concentrations of credit risk if it is exposed to risk of loss greater than it would have had if it mitigated its risk through diversification of customers. Such risks of loss manifest themselves differently, depending on the nature of the concentration, and vary in significance.

The Company had two customers with accounts receivable balances that aggregated 29% and 34% of the Company's accounts receivable at December 31, 2008 and June 30, 2008, respectively. Sales to neither of these customers exceeded 10% of net sales in any of the past three fiscal years.

## **Allowance for Doubtful Accounts**

In the ordinary course of business, the Company has established a reserve for doubtful accounts and customer deductions in the amount of \$450,000 and \$405,000 as of December 31, 2008 and June 30, 2008, respectively. The Company's reserve for doubtful accounts is a subjective critical estimate that has a direct impact on reported net earnings. This reserve is based upon the evaluation of accounts receivable agings, specific exposures and historical trends.

## **Stock Options**

During the three months ended December 31, 2008 the Company granted no stock options under its 2002 Employee Incentive Stock Option Plan. During the six months ended December 31, 2008 the Company granted 100,000 stock options under its 2002 Employee Incentive Stock Option Plan. These grants have an exercise price of \$4.25, a fair value of approximately \$198,000 and vest over a two-year period from the date of grant. There were no options granted under its 2000 Non-employee Incentive Stock Option Plan. During the three months ended December 31, 2008 there were no options exercised under either plan. During the six months ended December 31, 2008 there were 3,240 options exercised, with proceeds of approximately \$6,000, under the 2002 Employee Incentive Stock Option Plan and no exercises under the 2000 Non-employee Incentive Stock Option Plan.

## **Intangible Assets**

Under the Statement of Accounting Standards ("SFAS") No.142, "Goodwill and Other Intangible Assets", all goodwill and certain intangible assets determined to have indefinite lives will not be amortized but will be tested for impairment at least annually. Intangible assets other than goodwill will be amortized over their useful lives and reviewed for impairment at least annually or more often whenever there is an indication that the carrying amount may not be recovered.

The Company's acquisition of substantially all of the assets and certain liabilities of Marks included intangible assets with a fair value of \$16,440,000 on the date of acquisition. In accordance with the requirements of SFAS No. 141, "Business Combinations", the Company recorded the estimated value of \$9,800,000 related to the customer relationships, \$340,000 related to a non-compete agreement and \$6,300,000 related to the Marks trade name within intangible assets. The remaining excess of the purchase price of \$922,000 was assigned to Goodwill. In accordance with the provisions of SFAS No. 142, "Goodwill and Other Intangible Assets", the intangible assets will be amortized over their estimated useful lives of twenty years (customer relationships) and seven years (non-compete agreement). The Marks USA trade name was deemed to have an indefinite life. The goodwill recorded as a result of the acquisition is deductible for Federal and New York State income tax purposes over a period of 15 years.

## **Recent Accounting Pronouncements**

In March 2008, the Financial Accounting Standards Board ("FASB") issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities - an amendment of FASB Statement No. 133. This statement changes the disclosure requirements for derivative instruments and hedging activities. Entities are required to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under Statement 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS No. 161 is effective for fiscal years and interim periods beginning after November 15, 2008. The Company's adoption of SFAS No. 161 is not expected to have a material effect on its condensed consolidated financial statements.

In February 2008, the FASB issued FASB Staff Position ("FSP") No. FAS 157-1, "Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13." This FSP amends SFAS No. 157 to exclude certain leasing transactions accounted for under previously existing accounting guidance. However, this scope exception does not apply to assets acquired and liabilities assumed in a business combination, regardless of whether those assets and liabilities are related to leases.

In February 2008, the FASB issued FSP No. FAS 157-2, "Effective Date of FASB Statement No. 157". This FSP delays the effective date of SFAS No. 157, "Fair Value Measurements", for non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). This FSP defers the effective date of SFAS No. 157 to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years for items within the scope of this FSP.

In October 2008, the FASB issued FSP No. FAS 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active" ("FSP 157-3"). FSP 157-3 classified the application of SFAS No. 157 in an inactive market. It demonstrated how the fair value of a financial asset is determined when the market for that financial asset is inactive. FSP 157-3 was effective upon issuance, including prior periods for which financial statements had not been issued. The implementation of FSP 157-3 did not have a material effect on the Company's condensed consolidated financial statements.

In April 2008, the FASB issued FASB Staff Position SFAS 142-3, "Determination of the Useful Life of Intangible Assets" ("FSP SFAS 142-3"). FSP SFAS 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FASB Statement No. 142, Goodwill and Other Intangible Assets. The objective of this FSP is to improve the consistency between the useful life of a recognized intangible asset under Statement 142 and the period of expected cash flows used to measure the fair value of the asset under SFAS 141R, Business Combinations, and other U.S. GAAP principles. FSP SFAS 142-3 is effective for fiscal years beginning after December 31, 2008. The adoption of FSP SFAS 142-3 is effective July 1, 2009 and is not expected to have a material effect on the Company's condensed consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), "Business Combinations" ("SFAS No. 141(R)"). SFAS No. 141(R) replaces SFAS No. 141, "Business Combinations," however, it retains the fundamental requirements of the former Statement that the acquisition method of accounting (previously referred to as the purchase method) be used for all business combinations and for an acquirer to be identified for each business. SFAS No. 141(R) defines the acquirer as the entity that obtains control of one or more businesses in the business combination and establishes the acquisition date as the date that the acquirer achieves control. Among other requirements, SFAS No. 141(R) requires the acquiring entity in a business combination to recognize the identifiable assets acquired, liabilities assumed and any non-controlling interest in the acquiree at their acquisition-date fair values, with limited exceptions; acquisition-related costs generally will be expensed as incurred. SFAS No. 141(R) requires certain financial statement disclosures to enable users to evaluate and understand the nature and financial effects of the business combination. SFAS No. 141(R) must be applied prospectively to business combinations that are consummated beginning in the Company's fiscal 2010. The Company's adoption of SFAS No. 141(R) is not expected to have a material effect on its condensed consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, "Non-controlling Interests in Consolidated Financial Statements, an Amendment of ARB No. 51" ("SFAS No. 160") to establish accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. Among other requirements, SFAS No. 160 clarifies that a non-controlling interest in a subsidiary, which is sometimes referred to as minority interest, is to be reported as a separate component of equity in the consolidated financial statements. SFAS No. 160 also requires consolidated net income to include the amounts attributable to both the parent and the non-controlling interest and to disclose those amounts on the face of the consolidated statement of income. SFAS No. 160 must be applied prospectively for fiscal years, and interim periods within those fiscal years, beginning in the Company's fiscal 2010, except for the presentation and disclosure requirements, which will be applied retrospectively for all periods. The Company's adoption of SFAS No. 160 is not expected to have a material effect on its condensed consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities". SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. Most of the provisions of this Statement apply only to entities that elect the fair value option. However, the amendment to SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities", applies to all entities with available-for-sale and trading securities. Some requirements apply differently to entities that do not report net income. SFAS No. 159 became effective for the Company in its fiscal year ending June 30, 2009. The Company's adoption of SFAS No. 159 did not have a material effect on its condensed consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements". SFAS No. 157 provides guidance for using fair value to measure assets and liabilities. In addition, this statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. Where applicable, this statement simplifies and codifies related guidance within generally accepted accounting principles. SFAS No. 157 became effective for the Company in its fiscal year ending June 30, 2009. The Company's adoption of SFAS No. 157 did not have a material effect on its condensed consolidated financial statements.

## Reclassification.

Certain expenses in Cost of sales for fiscal 2008 have been reclassified to Selling, general and administrative expenses to conform with the current years presentation.

### 2.) Stock-based Compensation

The Company has established two share incentive programs as discussed in more detail in the Consolidated Financial Statements and related notes contained in the Company's annual report on Form 10-K for the year ended June 30, 2008. The Company accounts for its stock options and share units granted in accordance with SFAS No. 123(R), "Share-Based Payment" ("SFAS No. 123(R)") which requires that all stock-based compensation must be recognized as an expense in the financial statements and that cost be measured at the fair market value of the award. SFAS No. 123(R) also requires that excess tax benefits related to stock option exercises be reflected as financing cash inflows instead of operating cash inflows. Stock-based compensation costs of \$89,000 and \$93,000 were recognized in three months ended December 31, 2008 and 2007, respectively. Stock-based compensation costs of \$208,000 and \$151,000 were recognized in six months ended December 31, 2008 and 2007, respectively. Unearned stock-based compensation cost was \$443,000 as of December 31, 2008.

The fair values of stock options granted during the six months ended December 31, 2008 were estimated on the date of grant using the Black-Scholes option-pricing model that used the following weighted average assumptions:

Expected life in years	5
Risk-free interest rates	3.07%
Volatility	49.86%
Dividend yield	0%

### 3.) Inventories

For interim financial statements, inventories are calculated using a gross profit percentage. The Company regularly reviews parts and finished goods inventories on hand and, when necessary, records a reserve for excess or obsolete inventories. As of December 31, 2008 and June 30, 2008, the balance in this reserve amounted to \$1,432,000 and \$1,200,000, respectively. The Company also regularly reviews the period over which its inventories will be converted to sales. Any inventories expected to convert to sales beyond 12 months from the balance sheet date are classified as non-current.

Inventories, net of reserves consist of the following (in thousands):	December 31, 2008	June 30, 2008
	-----	-----
Component parts	\$ 17,370	\$ 12,924
Work-in-process	5,529	4,114
Finished product	13,754	10,234
	-----	-----
	\$ 36,653	\$ 27,272
	=====	=====
Classification of inventories, net of reserves:		
Current	\$ 27,602	\$ 19,548
Non-current	9,051	7,724
	-----	-----
	\$ 36,653	\$ 27,272
	=====	=====

### 4.) Earnings Per Common Share

The Company follows the provisions of SFAS No. 128, "Earnings Per Share". In accordance with SFAS No. 128, earnings per common share amounts ("Basic EPS") were computed by dividing earnings by the weighted average number of common shares outstanding for the period. Earnings per common share amounts, assuming dilution ("Diluted EPS"), were computed by reflecting the potential dilution from the exercise of stock options. SFAS No. 128 requires the presentation of both Basic EPS and Diluted EPS on the face of the condensed consolidated statements of income.

A reconciliation between the numerators and denominators of the Basic and Diluted EPS computations for earnings is as follows (in thousands except per share data):

	Three months ended December 31, 2008		
	Net Income (numerator)	Shares (denominator)	Per Share Amounts
-----			
Basic EPS			
-----			
Net income, as reported	\$ 332	19,096	\$ 0.02
Effect of dilutive securities			
-----			
Employee Stock Options	\$ --	--	\$ -
-----			
Diluted EPS			
-----			
Net income, as reported and assumed option exercises	\$ 332	19,096	\$ 0.02
	=====	=====	=====

1,420,000 options to purchase shares of common stock in the three months ended December 31, 2008 were excluded in the computation of Diluted EPS because the exercise prices were in excess of the average market price for this period and their inclusion would be anti-dilutive.

	Three months ended December 31, 2007		
	Net Income (numerator)	Shares (denominator)	Per Share Amounts
-----			
Basic EPS			
-----			
Net income, as reported	\$ 1,172	19,298	\$ 0.06
Effect of dilutive securities			
-----			
Employee Stock Options	\$ -	523	\$ -
-----			
Diluted EPS			
-----			
Net income, as reported and assumed option exercises	\$ 1,172	19,821	\$ 0.06
	=====	=====	=====

194,000 options to purchase shares of common stock in the three months ended December 31, 2007 were excluded in the computation of Diluted EPS because the exercise prices were in excess of the average market price for this period and their inclusion would be anti-dilutive.

	Six months ended December 31, 2008		
	Net Income (numerator)	Shares (denominator)	Per Share Amounts
-----			
Basic EPS			
-----			
Net income, as reported	\$ 654	19,096	\$ 0.03
Effect of dilutive securities			
-----			
Employee Stock Options	\$ --	110	\$ --
-----			
Diluted EPS			
-----			
Net income, as reported and assumed option exercises	\$ 654	19,206	\$ 0.03
	=====	=====	=====

795,000 options to purchase shares of common stock in the three months ended December 31, 2008 were excluded in the computation of Diluted EPS because the exercise prices were in excess of the average market price for this period and their inclusion would be anti-dilutive.

	Six months ended December 31, 2007		
	Net Income (numerator)	Shares (denominator)	Per Share Amounts
-----			
Basic EPS			
-----			
Net income, as reported	\$ 1,547	19,432	\$ 0.08
Effect of dilutive securities			

----- Employee Stock Options	\$	-	553	\$	-
	-----		-----	-----	-----
Diluted EPS					
-----					
Net income, as reported and assumed option exercises	\$	1,547	19,985	\$	0.08
	=====	=====	=====	=====	=====

115,000 options to purchase shares of common stock in the three months ended December 31, 2007 were excluded in the computation of Diluted EPS because the exercise prices were in excess of the average market price for this period and their inclusion would be anti-dilutive.

Option activity during the six months ended December 31, 2008 is summarized as follows:

	Options	Weighted Average Exercise Price
	-----	-----
Outstanding at July 1, 2008	1,323,480	\$ 2.89
Granted	100,000	4.25
Cancelled	--	--
Exercised	(3,240)	(1.90)
	-----	
Outstanding at December 31, 2008	1,420,240	2.99
	=====	
Exercisable at December 31, 2008	1,187,248	
	=====	

## 5.) Acquisition of Business

On August 18, 2008, the Company acquired substantially all of the assets and business of G. Marks Hardware, Inc. ("Marks") for \$25.2 million, the repayment of \$1 million of bank debt and the assumption of current liabilities as described more fully in the Asset Purchase Agreement. As such, the operations of Marks have been included in the Company's Statement of Income for the period August 18, 2008 to December 31, 2008. The Marks business involves the manufacturing and distribution of door-locking devices. The Company completed this acquisition at a price in excess of the value of the net identifiable assets because it believes that the combination of the two companies offers the potential for manufacturing and operational synergies as the Company combines the Marks operations and production into its own door-locking operations and production structure. The Company funded the acquisition with a term loan from its lenders as described in Note 6.

The acquisition described above was accounted for as a purchase and was valued based on management's estimate of the fair value of the assets acquired and liabilities assumed. The estimates of fair value are preliminary and subject to adjustment for a period of up to one year from the date of acquisition. Based on the Company's evaluation, the allocation of the purchase price for the acquisition was as follows (in thousands):

Assets Acquired:	
Cash	\$ 520
Accounts receivable	1,836
Inventory	6,740
Prepaid expenses and other current assets	112
Property and equipment	801
Goodwill	922
Intangible assets	16,440
	-----
	27,371
	-----
Less: Liabilities Assumed:	
Line of credit borrowings outstanding	1,000
Accounts payable	637
Accrued expenses	339
	-----
	1,976
	-----
Total consideration (including acquisition Costs of \$222)	\$ 25,395
	=====

In accordance with the requirements of SFAS No. 141, "Business Combinations", the Company recorded the estimated value of \$9,800,000 related to the customer relationships, \$340,000 related to a non-compete agreement and \$6,300,000 related to the Marks trade name within intangible assets and the excess of the purchase price over the fair value of the acquired assets of \$922,000 was assigned to Goodwill. In accordance with the provisions of SFAS No. 142, "Goodwill and Other Intangible Assets", the intangible assets will be amortized over their estimated useful lives of twenty years (customer relationships) and seven years (non-compete agreement). The weighted average amortization period of these assets is 19.6 years. The Marks trade name was deemed to have an indefinite life. The goodwill recorded as a result of the acquisition is deductible for Federal and New York State income tax purposes over a period of 15 years.

Unaudited pro-forma consolidated financial information is presented below as if the acquisition had occurred as of the first day of the earliest period presented. Results have been adjusted to account for: (1) the initial \$25,000,000 cash borrowing and related interest expense under the term loan, (2) cash used to repay \$1,000,000 in assumed bank debt at closing of the purchase transaction, (3) deferred financing costs and related amortization associated with the term loan, (4) additional salary and employee stock option expense for employees not previously included in salary expense, and (5) amortization expense of acquired intangible assets. The pro-forma information presented below does not purport to present what actual results would have been if the acquisition had occurred at the beginning of such periods, nor does the information project results for any future period. The unaudited pro-forma consolidated financial information should be read in conjunction with the historical financial information included in other reports and documents filed with the United States Securities and Exchange Commission.

The unaudited pro-forma consolidated financial information for the three and six months ended December 31, 2008 and 2007 is as follows:

	Three months ended December 31,		Six months ended December 31,	
	2008	2007	2008	2007
	(in thousands, except per share data)		(in thousands, except per share data)	
Pro-forma:				
Net sales	\$ 19,079	\$ 22,455	\$ 39,081	\$ 42,732
Net income	\$ 332	\$ 1,285	\$ 748	\$ 1,852
Net income per share:				
Basic	\$ 0.02	\$ 0.07	\$ 0.04	\$ 0.10
Diluted	\$ 0.02	\$ 0.06	\$ 0.04	\$ 0.09
Weighted average number of shares:				
Basic	19,095,713	19,297,252	19,095,537	19,432,471
Diluted	19,095,713	19,820,906	19,206,453	19,985,412

## 6.) Long Term Debt

On August 18, 2008, the Company and its banks amended and restated the existing \$25,000,000 revolving credit agreement. The amended facility was \$50,000,000 and provides for a \$25,000,000 revolving credit line as well as a \$25,000,000 term portion of which the entire \$25,000,000 was utilized to finance the asset purchase agreement as described in Note 5. The amended revolving credit agreement and term loan was amended in November 2008 to \$20,000,000 and is secured by all the accounts receivable, inventory, the Company's headquarters in Amityville, New York and certain other assets of Napco Security Technologies, Inc. and the common stock of three of the Company's subsidiaries. The agreements bear interest at either the Prime Rate or an alternate rate based on LIBOR as described in the agreement. The August amendment extended the revolving credit agreement to August 2012. Any outstanding borrowings are to be repaid or refinanced on or before that time. As of December 31, 2008 there was \$14,100,000 outstanding under the revolving credit facility with an interest rate of 3.5% and \$24,107,000 outstanding under the term loan with an interest rate of 3.3%. The term loan is being repaid in 19 quarterly installments of \$893,000 each, commencing in December 2008, and a final payment of \$8,033,000 due in August 2013. The agreements contain various restrictions and covenants including, among others, restrictions on payment of dividends, restrictions on borrowings and compliance with certain financial ratios, as defined in the agreement. As of December 31, 2008 the Company was not in compliance with the covenants relating to the ratio of Funded Debt to EBITDA, Debt Service Coverage Ratio and a Modified Quick Ratio for which it has received the appropriate waivers from its banks. The Company and its banks are currently renegotiating certain terms and conditions of its \$20,000,000 revolving line of credit and its \$25,000,000 term loan and expects to have amended facilities in place during the quarter ended March 31, 2009.

## 7.) Geographical Data

The Company is engaged in one major line of business: the development, manufacture, and distribution of security alarm products and door security devices for commercial and residential use. Sales to unaffiliated customers are primarily shipped from the United States. The Company has customers worldwide with major concentrations in North America, Europe, and South America.

The Company observes the provisions of SFAS No. 131. The following represents selected consolidated geographical data for the three and six months ended December 31, 2008 and 2007 (in thousands):

	Three Months ended December 31,		Six Months ended December 31,	
	2008	2007	2008	2007
Sales to external customers(1):				
Domestic	\$ 17,124	\$ 13,394	\$ 32,551	\$ 24,967
Foreign	1,955	2,772	4,011	5,075
Total Net Sales	\$ 19,079	\$ 16,166	\$ 36,562	\$ 30,042
As of				
	December 31, 2008	June 30, 2008		
Identifiable assets:				
United States	\$ 76,544	\$ 50,056		
Dominican Republic (2)	22,277	19,841		
Other foreign countries	5,194	6,826		
Total Identifiable Assets	\$ 104,015	\$ 76,723		

(1) All of the Company's sales occur in the United States and are shipped primarily from the Company's facilities in the United States and United Kingdom. There were no sales into any one foreign country in excess of 10% of Net Sales.

(2) Consists primarily of inventories (\$17,318,000 and \$14,754,000) and fixed assets (\$4,850,000 and \$4,970,000) located at the Company's principal manufacturing facility in the Dominican Republic as of December 31, 2008 and June 30, 2008, respectively.

## 8.) Commitments and Contingencies

In the normal course of business, the Company is a party to claims and/or litigation. Management believes that the settlement of such claims and/or litigation, considered in the aggregate, will not have a material adverse effect on the Company's financial position and results of operations. In August 2008, the Company entered into a lease for the building where Marks has maintained its operations. The lease provides for an annual base rent of \$288,750 plus maintenance and real estate taxes, expires in August 2009 and provides for two annual extensions thereafter at similar terms and conditions. The Company intends to move the Marks operations into its facilities after constructing extensions of approximately 35,000 square feet. To date, the Company does not have estimates for the cost of this move or the related construction and may defer construction depending on economic conditions. The Marks business involves the manufacturing and distribution of door-locking devices.

## 9.) Income Taxes

The provision for income taxes represents Federal, foreign, and state and local income taxes. The effective rate differs from statutory rates due to the effect of state and local income taxes, tax rates in foreign jurisdictions and certain nondeductible expenses. Our effective tax rate will change from quarter to quarter based on recurring and non-recurring factors including, but not limited to, the geographical mix of earnings, enacted tax legislation, and state and local income taxes. In addition, changes in judgment from the evaluation of new information resulting in the recognition, de-recognition or re-measurement of a tax position taken in a prior annual period are recognized separately in the quarter of the change.

The Company does not expect that our unrecognized tax benefits will significantly change within the next twelve months. We file a consolidated U.S. income tax return and tax returns in certain state and local and foreign jurisdictions. There are no current tax examinations in progress. Accordingly, as of December 31, 2008, we remain subject to examination in all tax jurisdictions for all relevant jurisdictional statutes.

The Company adopted the provisions of FIN 48 as of July 1, 2007. The Company has identified its U.S. Federal income tax return and its State return in New York as its major tax jurisdictions. During the three and six months ending December 31, 2008 the Company increased its reserve for uncertain income tax positions by \$5,000 and \$11,000, respectively. As a result, as of December 31, 2008 the Company has a long-term accrued income tax liability of \$305,000.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

### Management's Discussion and Analysis of Financial Condition and Results of Operations

This Quarterly Report on Form 10-Q and the information incorporated by reference may include "Forward-Looking Statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Exchange Act of 1934. The Company intends the Forward-Looking Statements to be covered by the Safe Harbor Provisions for Forward-Looking Statements. All statements regarding the Company's expected financial position and operating results, its business strategy, its financing plans and the outcome of any contingencies are Forward-Looking Statements. The Forward-Looking Statements are based on current estimates and projections about our industry and our business. Words such as "anticipates," "expects," "intends," "plans," "believes," "seeks," "estimates," or variations of such words and similar expressions are intended to identify such Forward-Looking Statements. The Forward-Looking Statements are subject to risks and uncertainties that could cause actual results to differ materially from those set forth or implied by any Forward-Looking Statements. For example, the Company is highly dependent on its Chief Executive Officer for strategic planning. If he is unable to perform his services for any significant period of time, the Company's ability to continue growing could be adversely affected. In addition, factors that could cause actual results to differ materially from the Forward-Looking Statements include, but are not limited to, adverse tax consequences of offshore operations, significant fluctuations in the exchange rate between the Dominican Peso and the U.S. Dollar, distribution problems, unforeseen environmental liabilities, the uncertain military, political and economic conditions in the world and the successful integration of Marks into our existing operations.

### Overview

The Company is a diversified manufacturer of security products, encompassing intrusion and fire alarms, building access control systems and electronic locking devices. These products are used for commercial, residential, institutional, industrial and governmental applications, and are sold worldwide principally to independent distributors, dealers and installers of security equipment. International sales accounted for approximately 11% and 17% of our revenues for the six months ended December 31, 2008 and 2007, respectively.

The Company owns and operates manufacturing facilities in Amityville, New York and the Dominican Republic. A significant portion of our operating costs are fixed, and do not fluctuate with changes in production levels or utilization of our manufacturing capacity. As production levels rise and factory utilization increases, the fixed costs are spread over increased output, which should improve profit margins. Conversely, when production levels decline our fixed costs are spread over reduced levels, thereby decreasing margins.

On August 18, 2008, the Company acquired substantially all of the assets and business of G. Marks Hardware, Inc. ("Marks") for \$25.2 million, the repayment of \$1 million of bank debt and the assumption of certain current liabilities. The Company also entered into a lease for the building where Marks has maintained its operations. The lease provides for an annual base rent of \$288,750 plus maintenance and real estate taxes, expires in August 2009 and provides for two annual extensions thereafter. The Company intends to move the Marks operations into its facilities after constructing extensions of approximately 35,000 square feet during fiscal 2010. To date, the Company does not have estimates for the cost of this move or the related construction and may defer construction depending on economic conditions. The Marks business involves the manufacturing and distribution of door-locking devices.

The security products market is characterized by constant incremental innovation in product design and manufacturing technologies. Generally, the Company devotes 7-8% of revenues to research and development (R&D) on an annual basis. Products resulting from our R&D investments in fiscal 2008 did not contribute materially to revenue during this fiscal year, but should benefit the Company over future years. In general, the new products introduced by the Company are initially shipped in limited quantities, and increase over time. Prices and manufacturing costs tend to decline over time as products and technologies mature.

### Economic and Other Factors

Since October 2008, the U.S. and international financial markets have taken a significant loss and continue to be very volatile. In the event that the downturn in the U.S. or international financial markets is prolonged, our revenue levels could be materially adversely affected. If the current worldwide economic downturn continues, many of our current or potential future customers may experience serious cash flow problems and as a result may, modify, delay or cancel purchases of our products. Additionally, customers may not be able to pay, or may delay payment of, accounts receivable that are owed to us. Furthermore, the current downturn and market instability makes it difficult for us to forecast our revenues.

## **Seasonality**

The Company's fiscal year begins on July 1 and ends on June 30. Historically, the end users of Napco's products want to install its products prior to the summer; therefore sales of its products peak in the period April 1 through June 30, the Company's fiscal fourth quarter, and are reduced in the period July 1 through September 30, the Company's fiscal first quarter. To a lesser degree, sales in Europe are also adversely impacted in the Company's first fiscal quarter because of European vacation patterns, i.e., many distributors and installers are closed for the month of August. In addition, demand is affected by the housing and construction markets.

## **Critical Accounting Policies and Estimates**

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in conformity with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses reported in those financial statements. These judgments can be subjective and complex, and consequently actual results could differ from those estimates. Our most critical accounting policies relate to revenue recognition; concentration of credit risk; inventories; intangible assets; goodwill; and income taxes.

### **Revenue Recognition**

Revenues from merchandise sales are recorded at the time the product is shipped or delivered to the customer pursuant to the terms of sale. We report our sales levels on a net sales basis, which is computed by deducting from gross sales the amount of actual returns received and an amount established for anticipated returns and other allowances.

Our sales return accrual is a subjective critical estimate that has a direct impact on reported net sales and income. This accrual is calculated based on a history of gross sales and actual sales returns, as well as management's estimate of anticipated returns and allowances. As a percentage of gross sales, sales returns, rebates and allowances were 8% and 6% for the six months ended December 31, 2008 and 2007, respectively.

### **Concentration of Credit Risk**

An entity is more vulnerable to concentrations of credit risk if it is exposed to risk of loss greater than it would have had if it mitigated its risk through diversification of customers. Such risks of loss manifest themselves differently, depending on the nature of the concentration, and vary in significance.

The Company had two customers with accounts receivable balances that aggregated 29% and 34% of the Company's accounts receivable at December 31, 2008 and June 30, 2008, respectively. Sales to neither of these customers exceeded 10% of net sales in any of the past three fiscal years.

In the ordinary course of business, we have established a reserve for doubtful accounts and customer deductions in the amount of \$450,000 and \$405,000 as of December 31, 2008 and June 30, 2008, respectively. Our reserve for doubtful accounts is a subjective critical estimate that has a direct impact on reported net earnings. This reserve is based upon the evaluation of accounts receivable agings, specific exposures and historical trends.

### **Inventories**

Inventories are valued at the lower of cost or fair market value, with cost being determined on the first-in, first-out (FIFO) method. The reported net value of inventory includes finished saleable products, work-in-process and raw materials that will be sold or used in future periods. Inventory costs include raw materials, direct labor and overhead. The Company's overhead expenses are applied based, in part, upon estimates of the proportion of those expenses that are related to procuring and storing raw materials as compared to the manufacture and assembly of finished products. These proportions, the method of their application, and the resulting overhead included in ending inventory, are based in part on subjective estimates and approximations and actual results could differ from those estimates.

In addition, the Company records an inventory obsolescence reserve, which represents the difference between the cost of the inventory and its estimated market value, based on various product sales projections. The balance in this reserve was \$1,432,000 and \$1,200,000 as of December 31, 2008 and June 30, 2008, respectively. This reserve is calculated using an estimated obsolescence percentage applied to the inventory based on age, historical trends, requirements to support forecasted sales, and the ability to find alternate applications of its raw materials and to convert finished product into alternate versions of the same product to better match customer demand. There is inherent professional judgment and subjectivity made by both production and engineering members of management in determining the estimated obsolescence percentage. In addition, and as necessary, the Company may establish specific reserves for future known or anticipated events.

The Company also regularly reviews the period over which its inventories will be converted to sales. Any inventories expected to convert to sales beyond 12 months from the balance sheet date are classified as non-current.

### **Goodwill and Other Intangible Assets**

The Company accounts for Goodwill in accordance with Statement of Financial Accounting Standards (SFAS) No. 141, Business Combinations and SFAS No. 142, Goodwill and Other Intangible Assets. These statements established accounting and reporting standards for acquired goodwill and other intangible assets. Specifically, the standards address how acquired intangible assets should be accounted for both at the time of acquisition and after they have been recognized in the financial statements. In accordance with SFAS No. 142, intangible assets, including purchased goodwill, must be evaluated for impairment. Those intangible assets that are classified as goodwill or as other intangibles with indefinite lives are not amortized.

Impairment testing is performed in two steps: (i) the Company determines impairment by comparing the fair value of a reporting unit with its carrying value, and (ii) if there is an impairment, the Company measures the amount of impairment loss by comparing the implied fair value of goodwill with the carrying amount of that goodwill. At the conclusion of fiscal 2008, the Company performed its annual impairment evaluation required by this standard and determined that its goodwill is not impaired.

The Company's acquisition of substantially all of the assets and certain liabilities of Marks included intangible assets with a fair value of \$16,440,000 on the date of acquisition. In accordance with the requirements of SFAS No. 141, "Business Combinations", the Company recorded the estimated value of \$9,800,000 related to the customer relationships, \$340,000 related to a non-compete agreement and \$6,300,000 related to the Marks trade name within intangible assets and Goodwill of \$922,000 subject to further adjustment. In accordance with the provisions of SFAS No. 142, "Goodwill and Other Intangible Assets", the intangible assets will be amortized over their estimated useful lives of twenty years (customer relationships) and seven years (non-compete agreement). The Marks USA trade name was deemed to have an indefinite life. The goodwill recorded as a result of the acquisition is deductible for Federal and New York State income tax purposes over a period of 15 years.

### **Income Taxes**

The provision for income taxes represents Federal, foreign, and state and local income taxes. The effective rate differs from statutory rates due to the effect of state and local income taxes, tax rates in foreign jurisdictions and certain nondeductible expenses. Our effective tax rate will change from quarter to quarter based on recurring and non-recurring factors including, but not limited to, the geographical mix of earnings, enacted tax legislation, and state and local income taxes. In addition, changes in judgment from the evaluation of new information resulting in the recognition, de-recognition or re-measurement of a tax position taken in a prior annual period are recognized separately in the quarter of the change.

We do not expect that our unrecognized tax benefits will significantly change within the next twelve months. We file a consolidated U.S. income tax return and tax returns in certain state and local and foreign jurisdictions. There are no current tax examinations in progress. Accordingly, as of December 31, 2008, we remain subject to examination in all tax jurisdictions for all relevant jurisdictional statutes.

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	Three months ended December 31, (dollars in thousands)			Six months ended December 31, (dollars in thousands)		
	2008	2007	% Increase/ (decrease)	2008	2007	% Increase/ (decrease)
Net sales	\$ 19,079	\$ 16,166	18.0%	\$ 36,562	\$ 30,042	21.7%
Gross profit	6,214	5,447	14.1%	11,820	10,671	10.8%
Gross profit as a % of net sales	32.6%	33.7%	(1.1)%	32.3%	35.5%	(3.2)%
Selling, general and administrative	5,448	4,162	30.9%	10,224	8,583	19.1%
Selling, general and administrative as a percentage of net sales	28.6%	25.7%	(2.9)%	28.0%	28.6%	(0.6)%
Operating income	766	1,285	(40.0)%	1,596	2,088	(23.6)%
Interest expense, net	429	224	91.5%	744	419	77.6%
Other (income) expense	(54)	11	(590.9)%	25	18	38.9%
Minority interest in net loss of subsidiary	70	20	350.0%	112	59	89.8%
Provision (Benefit) for income taxes	129	(102)	226.5%	285	163	74.8%
Net income	332	1,172	(71.7)%	654	1,547	(57.7)%

Sales for the three months ended December 31, 2008 increased by approximately 18% to \$19,079,000 as compared to \$16,166,000 for the same period a year ago. Sales for the six months ended December 31, 2008 increased by approximately 22% to \$36,562,000 as compared to \$30,042,000 for the same period a year ago. The increase in sales for the three and six months ended December 31, 2008 was primarily the result of the net sales added from the Marks acquisition as well as increased sales of the Company's door-locking and access control products as partially offset by a decrease in the Company's intrusion products.

Gross profit for the three months ended December 31, 2008 increased to \$6,214,000 or 32.6% of sales as compared to \$5,447,000 or 33.7% of sales for the same period a year ago. Gross profit for the six months ended December 31, 2008 increased to \$11,820,000 or 32.3% of sales as compared to \$10,671,000 or 35.5% of sales for the same period a year ago. The increase in Gross profit in dollars for the three and six months was primarily due to the addition of the Gross profit of Marks (\$1,557,000 and \$2,614,000, respectively) resulting from the acquisition on August 18, 2008 as partially offset by an increase in certain overhead expenses in Cost of sales. The decrease in gross profit as a percentage of sales declined primarily from the increase in certain overhead expenses as well as a decrease in production of the Company's non-Marks product lines, resulting in lower overhead absorption.

Selling, general and administrative expenses for the three months ended December 31, 2008 increased by \$1,286,000 to \$5,448,000, or 28.6% of sales, as compared to \$4,162,000, or 25.7% of sales a year ago. Selling, general and administrative expenses for the six months ended December 31, 2008 increased by \$1,641,000 to \$10,224,000, or 28.0% of sales, as compared to \$8,583,000, or 28.6% of sales a year ago. The increase in dollars for the three and six months ended December 31, 2008 was due primarily to the additional expenses relating to Marks (\$1,137,000 and \$1,591,000, respectively). The three months ended December 31, 2008 also included an increase in tradeshow expenses due to a major tradeshow occurring in October 2008 (\$199,000). This tradeshow occurred in September 2007 and was therefore included in Selling, general and administrative expense for the first quarter of fiscal 2008.

Interest expense, net for the three months ended December 31, 2008 increased by \$205,000 to \$429,000 as compared to \$224,000 for the same period a year ago. Interest expense, net for the six months ended December 31, 2008 increased by \$325,000 to \$744,000 as compared to \$419,000 for the same period a year ago. The increase in interest expense for the three and six months resulted primarily from the increase in the Company's average outstanding debt, which was due to the \$25,000,000 term loan utilized for the Marks acquisition in August 2008.

The Company's provision for income taxes for the three months ended December 31, 2008 increased by \$231,000 to a provision of \$129,000 as compared to a benefit of \$102,000 for the same period a year ago. The Company's provision for income taxes for the six months ended December 31, 2008 increased by \$122,000 to \$285,000 as compared to \$163,000 for the same period a year ago. The increase in provision for income taxes for the three and six months resulted primarily from the Company's corporate restructuring during the quarter ended December 31, 2007. As a result, the Company's effective rate for income tax was 28.0% and 30.4% for the three and six months ended December 31, 2008, respectively as compared to (9.5)% and 9.5% for the same periods a year ago.

Net income decreased by \$840,000 to \$332,000 or \$0.02 per diluted share for the three months ended December 31, 2008 as compared to \$1,172,000 or \$0.06 per diluted share for the same period a year ago. Net income decreased by \$893,000 to \$654,000 or \$0.03 per diluted share for the six months ended December 31, 2008 as compared to \$1,547,000 or \$0.08 per diluted share for the same period a year ago. The decrease for the three and six months ended December 31, 2008 was primarily due to the decrease in net sales and gross profit in the Company's intrusion product lines.

### **Liquidity and Capital Resources**

During the six months ended December 31, 2008 the Company utilized all of its cash from operations and additional borrowings to complete the Marks acquisition (\$26,173,000, which includes payment of the \$1,000,000 of assumed debt), purchase inventory (\$2,621,000) and property, plant and equipment (\$326,000). The Company's management believes that current working capital, cash flows from operations and its revolving credit agreement will be sufficient to fund the Company's operations through at least the next twelve months. The Company and its banks are currently renegotiating certain terms and conditions of its \$20,000,000 revolving line of credit and its \$25,000,000 term loan and expects to have amended facilities in place during the quarter ended March 31, 2009.

Accounts Receivable at December 31, 2008 decreased \$2,826,000 to \$22,997,000 as compared to \$25,823,000 at June 30, 2008. This decrease is primarily the result of the lower sales volume during the quarter ended December 31, 2008 as compared to the quarter ended June 30, 2008, which is typically the Company's highest, as partially offset by Marks acquisition (\$2,628,000) .

Inventories at December 31, 2008 increased by \$9,381,000 to \$36,653,000 as compared to \$27,272,000 at June 30, 2008. This increase was primarily the result of the Marks acquisition (\$5,401,000) as well as the Company level-loading its production schedule in anticipation of its historical sales cycle where a larger portion of the Company's sales occur in the latter fiscal quarters as compared to the earlier quarters. The Company initiated several steps in order to reduce inventory levels in fiscal 2008 and expects to continue them in fiscal 2009 in the Company's non-Marks inventory.

On August 18, 2008, the Company and its banks amended and restated the existing \$25,000,000 revolving credit agreement. The amended facility is \$50,000,000 and provides for a \$25,000,000 revolving credit line as well as a \$25,000,000 term portion of which the entire \$25,000,000 was utilized to finance the asset purchase agreement as described in Note 5. The amended revolving credit agreement and term loan was amended to \$20,000,000 in November 2008 and is secured by all the accounts receivable, inventory, the Company's headquarters in Amityville, New York and certain other assets of Napco Security Technologies, Inc. and the common stock of three of the Company's subsidiaries. The agreements bear interest at either the Prime Rate or an alternate rate based on LIBOR as described in the agreement. The August amendment extended the revolving credit agreement to August 2012. Any outstanding borrowings are to be repaid or refinanced on or before that time. As of December 31, 2008 there was \$14,100,000 outstanding under the revolving credit facility with an interest rate of 3.5% and \$24,107,000 outstanding under the term loan with an interest rate of 3.3%. The term loan is to be repaid in 19 quarterly installments of \$893,000 each commencing in December 2008 and a final payment of \$8,033,000 due in August 2013. The agreements contain various restrictions and covenants including, among others, restrictions on payment of dividends, restrictions on borrowings and compliance with certain financial ratios, as defined in the agreement. As of December 31, 2008 the Company was not in compliance with the covenants relating to the ratio of Funded Debt to EBITDA, Debt Service Coverage Ratio and a Modified Quick Ratio for which it has received the appropriate waivers from its banks.

As of December 31, 2008 the Company had no material commitments for capital expenditures or inventory purchases other than purchase orders issued in the normal course of business.

### **ITEM 3: Quantitative and Qualitative Disclosures About Market Risk**

The Company's principal financial instrument is long-term debt (consisting of a revolving credit facility and term loan) that provides for interest at the prime rate or an alternate rate based on LIBOR as described in the agreement. The Company is affected by market risk exposure primarily through the effect of changes in interest rates on amounts payable by the Company under this credit facility. At December 31, 2008, an aggregate principal amount of approximately \$38,207,000 was outstanding under the Company's credit facility with a weighted average interest rate of approximately 3.3%. If principal amounts outstanding under the Company's credit facility remained at this level for an entire year and the prime rate increased or decreased, respectively, by 1% the Company would pay or save, respectively, an additional \$382,000 in interest that year.

A significant number of foreign sales transactions by the Company are denominated in U.S. dollars. As such, the Company has shifted foreign currency exposure onto many of its foreign customers. As a result, if exchange rates move against foreign customers, the Company could experience difficulty collecting unsecured accounts receivable, the cancellation of existing orders or the loss of future orders. The foregoing could materially adversely affect the Company's business, financial condition and results of operations. In addition, the Company transacts certain sales in Europe in British Pounds Sterling, therefore exposing itself to a certain amount of foreign currency risk. Management believes that the amount of this exposure is immaterial. We are also exposed to foreign currency risk relative to expenses incurred in Dominican Pesos ("RD\$"), the local currency of the Company's production facility in the Dominican Republic. The result of a 10% strengthening in the U.S. dollar to our RD\$ expenses would result in an annual decrease in income from operations of approximately \$314,000.

### **ITEM 4: Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management to allow timely decisions regarding required disclosure. Management necessarily applied its judgment in assessing the costs and benefits of such controls and procedures, which, by their nature, can provide only reasonable assurance regarding management's control objectives.

At the conclusion of the period ended December 31, 2008, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective in alerting them in a timely manner to information relating to the Company required to be disclosed in this report except as follows:

Management's review over its internal controls at the conclusion of fiscal 2008 identified conditions which they deemed to be material weaknesses, (as defined by standards established by the SEC and the Public Company Accounting Oversight Board) with respect to certain of our inventory valuation methods both at year-end and relating to the Gross profit method used to calculate Gross profit and Inventories for interim reporting purposes. Management has informed its independent auditors and the Audit Committee that it has corrected its method of calculating its gross profit and inventory for interim reporting by including a more comprehensive review of changes within the business and accounting for those changes where appropriate. The Company has also initiated a review of the ways in which we can more accurately cost its inventory for year-end reporting and will continue to monitor the effectiveness of these actions and will make any other changes or take such additional actions as management determines to be appropriate. Management expects to complete the actions relating to the year-end inventory valuation during fiscal 2009.

The Company has excluded from this assessment the internal control over financial reporting of Marks USA, which was acquired in August 2008. Total assets and total net sales subject to Marks USA internal control over financial reporting, represented 25% and 22%, respectively, of the Company's consolidated total assets and net sales for the six months ended December 31, 2008.

During the second quarter of fiscal 2009, there were no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting except for the procedure described above which has corrected the weakness relating to interim Gross profit and inventory calculations.

## PART II: OTHER INFORMATION

### Item 1A. Risk Factors

Information regarding the Company's Risk Factors are set forth in the Company's Annual Report on Form 10-K for the year ended June 30, 2008. There have been no material changes in the risk factors previously disclosed in the Company's Form 10-K for the year ended June 30, 2008 during the three months ended December 31, 2008 except as follows:

#### **Our Business Could Be Materially Adversely Affected as a Result of General Economic and Market Conditions**

We are subject to the effects of general economic and market conditions. If these conditions deteriorate, our business, results of operations or financial condition could be materially adversely affected. In addition, since October 2008, the U.S. and international financial markets have taken a significant loss and continue to be very volatile. In the event that the downturn in the U.S. or international financial markets is prolonged, our revenue levels could be materially adversely affected. If the current worldwide economic downturn continues, many of our current or potential future customers may experience serious cash flow problems and as a result may, modify, delay or cancel purchases of our products. Additionally, customers may not be able to pay, or may delay payment of, accounts receivable that are owed to us. Furthermore, the current downturn and market instability makes it difficult for us to forecast our revenues.

#### **Our Business Could Be Materially Adversely Affected by the Integration of Marks into Our Existing Operations**

Our business is dependent on the orderly, effective integration of the acquired Marks business, technologies, product lines and employees into our organization. If this integration is unsuccessful, our business may be materially adversely affected.

### Item 4. Submission of Matters to a Vote of Security Holders

- (a) The annual meeting of stockholders ("the Annual Meeting") was held on December 9, 2008.
- (b) At the Annual Meeting, two directors were re-elected as directors through 2011: Andrew J. Wilder - 14,010,972 votes "for", 2,731,469 votes "withheld", and Arnold Blumenthal - 14,589,134 votes "for", 2,153,307 votes "withheld"
- (c) At the Annual Meeting, the proposal to amend the Company's Amended and Restated Certificate of Incorporation to change the name of the Company to Napco Security Technologies, Inc. was approved: 16,501,708 votes "for", 195,885 votes "against", 44,848 votes "abstained"

### Item 6. Exhibits

- 30.1 First Amendment to Credit Agreement and Waiver dated as of November 14, 2008.
- 30.2 Second Amendment and Waivers to Amended and Restated Credit Agreement dated as of January 29, 2009.
- 30.3 Certificate of Amendment of Certificate of Incorporation of Napco Security Systems, Inc.
- 30.4 Certificate of Incorporation as Amended of Napco Security Technologies, Inc.
- 31.1 Certification Pursuant to Rule 13a-14(a)/15d-14(a) of Richard L. Soloway, Chairman of the Board and President
- 31.2 Certification Pursuant to Rule 13a-14(a)/15d-14(a) of Kevin S. Buchel, Senior Vice President of Operations and Finance
- 32.1 Section 1350 Certifications

**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.

February 9, 2009

**NAPCO SECURITY TECHNOLOGIES, INC**  
(Registrant)

By: /S/ RICHARD L. SOLOWAY

-----  
*Richard L. Soloway*  
*Chairman of the Board of Directors, President and Secretary*  
*(Chief Executive Officer)*

By: /S/ KEVIN S. BUCHEL

-----  
*Kevin S. Buchel*  
*Senior Vice President of Operations and Finance and Treasurer*  
*(Principal Financial and Accounting Officer)*

**EXHIBIT 26.1**

**FIRST AMENDMENT TO CREDIT AGREEMENT  
AND WAIVER**

FIRST AMENDMENT TO AMENDED AND RESTATED CREDIT AGREEMENT and WAIVER dated as of August 18, 2008 (the "First Amendment") by and among NAPCO SECURITY SYSTEMS, INC., a Delaware corporation (the "Borrower"), CAPITAL ONE, N.A. a national banking association, HSBC Bank USA, National Association, a national banking association, collectively, the "Lenders") and HSBC BANK, USA, National Association, a national banking association, as administrative agent and collateral agent for the Lenders hereunder (in such capacities, the "Administrative Agent" and the "Collateral Agent", respectively and each an "Agent").

**RECITALS**

The Borrower, the Lenders, and the Administrative Agent entered into an Amended and Restated Credit Agreement dated as of August 18, 2008, (the "Credit Agreement"), pursuant to which certain financial accommodations were made available to the Borrower.

The Borrower has requested that the Lenders and the Administrative Agent modify certain of the terms set forth in the Credit Agreement and further waive another term of the Credit Agreement for a certain period and the Lenders and the Administrative Agent are willing to modify such terms and waive such term but only upon and subject to the following terms and conditions.

NOW THEREFORE, in consideration of the premises and mutual covenants and promises exchanged herein, the parties hereto mutually agree as follows:

Section 1. Definitions. Except as otherwise defined in this First Amendment, terms defined in the Credit Agreement are used herein as defined therein.

Section 2. Amendment. Subject to the satisfaction of the conditions precedent specified in Section 4 below:

(A) Section 1.1 of the Credit Agreement is hereby amended by deleting the definition of "Revolving Credit Commitment" and substituting the following therefor:

"Revolving Credit Commitment": as to any Revolving Lender at any time, its obligation to make Revolving Credit Loans, issue or participate in Letters of Credit issued for the account of the Borrower and/or make or participate in Swing Line Loans to the Borrower in an aggregate amount not to exceed at any time outstanding the amount set forth opposite such Lender's name in Schedule I hereto under the heading "Revolving Credit Commitment," as such amount may be reduced from time to time pursuant to subsection 2.4 and the other applicable provisions hereof.

(B) Schedule I referenced in the definition of Revolving Credit Commitment is hereby amended by deleting same and substituting Schedule I-1 attached hereto for same.

(C) Section 6.3 of the Credit Agreement is hereby amended by deleting same and substituting the following therefor:

"6.3 Post Closing Obligations. By January 15, 2009 (or September 18, 2008 in the case of subsection (h) hereof) the Borrower will deliver to the Administrative Agent the following in form and content reasonably satisfactory to the Administrative Agent and the Required Lenders in each case, at the Borrower's sole cost and expense:

- (a) An environment report (Phase II) on the Borrower's real property located at 333 Bayview Avenue, Amityville, New York (the "Mortgaged Property");
- (b) A mortgage and security agreement on the Administrative Agent's standard form or other form acceptable to the Administrative Agent and its counsel, (the "Mortgage") encumbering the land and improvements upon the Mortgaged Property securing the \$5,000,000 in principal amount of the obligations under this Agreement together with Hazardous Material Guaranty and Indemnification Agreement on the standard form of the Administrative Agent or on a form acceptable to the Administrative Agent and its counsel from the Borrower and its Domestic Subsidiaries with respect to the real property encumbered by such Mortgage;
- (c) An updated survey of the Mortgage Property guaranteed to the Administrative Agent together with certificates of occupancy/completion for all improvements requiring same and satisfactory violation, flood, lien and judgment searches;

(d) Title insurance (including such endorsements as the Administrative Agent shall require) insuring the Mortgage as a first mortgage lien upon the Mortgaged Property subject only to those exceptions permitted by the Administrative Agent and its counsel;

(e) Paid certificates of insurance evidencing hazard, business interruption, explosion, flood (if necessary) and general liability coverage in such amounts and on such forms as shall be satisfactory to the Administrative Agent and its counsel;

(f) Evidence that all fees, taxes, premiums and amounts owed in connection with the recording of the Mortgage and the issuance of the Title Insurance Policy, including the Administrative Agent's fees and expenses, have been paid in full;

(g) Supplements to the Loan Documents perfecting the Collateral Agent's liens in the Mark's patents and trademarks, if any;

(h) A pledge security agreement on the Agent's standard form granting a security interest in the shares of Napco Group Europe Limited (48,750 shares), Alarm Lock systems, Inc. (100 shares) and Napco Americas (65 shares) (the "Pledged Stock") together with legal opinions from counsel relating to the effectiveness of such security interests in such stock satisfactory to the Administrative Agent and the Required Lenders and undated stock powers or similar instruments duly executed by each pledgor for such pledged shares.

Section 3. Waiver. Non-compliance by the Borrower with the covenant contained in Section 8.1 (a) (i) of the Credit Agreement requiring the ratio of Consolidated Funded Debt to consolidated EBITDA to be no greater than 3.5 to 1.0 to the extent of non-compliance for the period ended 12/30/08 solely to the extent such ratio was 5.17 to 1.0 instead of the required ratio.

Section 4. Conditions Precedent. The amendments to the Credit Agreement set forth in Section 2 hereof and the waiver set forth in Section 3 hereof shall become effective, on the date of this First Amendment, upon the execution and delivery of this First Amendment by the Borrower, the Administrative Agent and each of the Lenders and the satisfaction of the following conditions:

(A) Certified Copies and Other Documents. The Administrative Agent shall have received certificates of an officer of the Borrower dated the date of this First Amendment certifying (y) no changes in the certificate of incorporation or by-laws from the date of the Agreement or attaching copies of any amendments,  
(z) the incumbency and specimen signatures of the officers of the Borrower executing any documents delivered to the Administrative Agent or a Lender by the Borrower in connection herewith.

(B) Approval of the Administrative Agent and Agent's Counsel. All other documents and legal matters in connection with the transactions contemplated by this First Amendment shall be satisfactory in form and substance to the Administrative Agent and its counsel.

Section 5. Representations and Warranties. The Borrower represents and warrants to the Lenders that the representations and warranties set forth in the Credit Agreement and in the other Loan Documents are true and complete on the date of this First Amendment and as if made on and as of the date hereof (or, if such representation or warranty is expressly stated to have been made as of a specific date, as of such specific date).

Section 6. Borrower's Acknowledgments. The Borrower acknowledges and agrees that the Borrower has no claims, counterclaims, offsets, or defenses to the Loan Documents and the performance of the Borrower's obligations thereunder or if the Borrower did have any such claims, counterclaims, offsets or defenses to the Loan Documents or any transaction related to the Loan Documents, the same are hereby waived, relinquished and released in consideration of execution and delivery of this Second Amendment.

Section 7. Acknowledgement of Guarantors. The Guarantors acknowledge and consent to all of the terms and conditions of this First Amendment and agree that this First Amendment and all documents executed in connection herewith do not operate to reduce or discharge the Guarantors' obligations under the Credit Agreement or the other Loan Documents. The Guarantors further acknowledge and agree that the Guarantors have no claims, counterclaims, offsets, or defenses to the Loan Documents and the performance of the Guarantors' obligations thereunder or if the Guarantors did have any such claims, counterclaims, offsets or defenses to the Loan Documents or any transaction related to the Loan Documents, the same are hereby waived, relinquished and released in consideration of execution and delivery of this First Amendment.

Section 8. Continuing Effect; No Further Waiver. Except as expressly set forth in this First Amendment, all of the terms and provisions of the Loan Documents are ratified and confirmed, and are and shall remain in full force and effect and the Borrower shall continue to be bound by all of such terms and provisions. The Waiver provided for herein is limited as specified herein and shall not constitute any other waiver of the Loan Documents. The Borrower acknowledges and agrees that nothing in this Waiver shall constitute an indication of the Lenders' willingness to consent to any other amendment or waiver of any other provision of the Credit Agreement or a waiver of any Default or Event of Default not referenced in this Waiver or for any other time period.

Section 9. Governing Law; Execution in Counterparts. This First Amendment may be executed in any number of counterparts, all of which taken together shall constitute one and the same amendatory instrument and any of the parties hereto may execute this First Amendment by signing any such counterpart. This First Amendment shall be governed by, and construed in accordance with, the internal laws of the State of New York (without regard to New York conflicts of laws principles).

Section 10. Expenses, etc. The Borrower agrees to pay or reimburse the Administrative Agent for all reasonable out-of-pocket costs and expenses of the Administrative Agent (including, without limitation, the reasonable fees and expenses of Certilman, Balin, Adler & Hyman, LLP in connection with the negotiation, preparation, execution and delivery of this Second Amendment and the transactions contemplated hereby.

Section 11. Effective Date. This First Amendment is dated for convenience as of November 14, 2008 and shall be effective as of such date, on the delivery of an executed counterpart to the Borrower upon satisfaction of the conditions precedent contained in Section 4 hereof.

**[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK]**

IN WITNESS WHEREOF, the parties hereto have caused this First Amendment to Credit Agreement to be duly executed and delivered by their duly authorized officers, all as of the day and year first above written.

**Borrower:**

**NAPCO SECURITY SYSTEMS, INC.**

By: /s/KEVIN S. BUCHEL

-----  
Kevin S. Buchel  
Senior Vice President of  
Operations and Finance

**Guarantors:**

**ALARM LOCK SYSTEMS, INC.**

By: /s/KEVIN S. BUCHEL

-----  
Name: Kevin S. Buchel  
Title: Senior Vice President

**CONTINENTAL INSTRUMENTS, LLC**

By: /s/KEVIN S. BUCHEL

-----  
Name: Kevin S. Buchel  
Title: Manager

**Lenders:**

**CAPITAL ONE, N.A.**

By: /s/LUCILLE MCARDLE  
Name: Lucille McArdle  
Title: Vice President

**HSBC BANK USA, NATIONAL ASSOCIATION,  
as Administrative Agent and as a Lender**

By: /s/GARY SARRO

-----  
Name: Gary Sarro  
Title: First Vice President

**SCHEDULE I**  
**To the Amended and Restated Credit Agreement**

**COMMITMENTS**

Revolving Credit Commitment	
Revolving Lender	Revolving Credit Commitment
HSBC BANK USA, NATIONAL ASSOCIATION	\$12,000,000
CAPITAL ONE, N.A.	\$ 8,000,000
Total	\$20,000,000

  

Term Commitment	
Term Lender	Term Commitment
HSBC BANK USA, NATIONAL ASSOCIATION	\$15,000,000
CAPITAL ONE, N.A.	\$10,000,000
Total	\$25,000,000

**EXHIBIT 26.2**

February 6, 2009

Napco Security Technologies, Inc.  
f/k/a Napco Security Systems, Inc.  
333 Bayview Avenue  
Amityville, New York

Re: Amended and Restated Credit Agreement dated August 18, 2008

Ladies and Gentlemen:

We refer to the referenced agreement between you and the undersigned Lenders and Administrative Agent as most recently amended by a Second Amendment and Waivers dated as of January 29, 2009 (collectively, the "Credit Agreement"). Capitalized terms used herein without definition have the meanings ascribed in the Credit Agreement.

Section 8.1 (a) (i) of the Credit Agreement required maintenance of a ratio of Consolidated Funded Debt to Consolidated EBITDA of not more than 3.5 to 1.0 for the Trailing four quarter period which was not maintained as at December 31, 2008.

Section 8.1 (b) of the Credit Agreement required the Borrower and its Consolidated Subsidiaries to maintain a minimum Debt Service Coverage Ratio of at least 1.25 to 1.0 for the Trailing four quarter period which was not maintained as at December 31, 2008.

Section 8.1 (c) of the Credit Agreement required the Borrower and its Consolidated Subsidiaries to maintain a Modified Quick Ratio of at least 1.15 to 1.0 for the Trailing four quarter period which was not maintained as at December 31, 2008.

The Banks hereby waive non-compliance with the foregoing covenants for the above-referenced period as follows:

(1) Section 8.1 (a) (i) of the Credit Agreement requiring the ratio of Consolidated Funded Debt to Consolidated EBITDA to be no greater than 3.5 to 1.0 to the extent of non-compliance for the Trailing four quarter period ended 12/31/08 solely to the extent such ratio was 6.29 to 1.0 instead of the required ratio (For purposes of calculating Consolidated EBITDA, the definition has been expanded as follows: "Consolidated EBITDA": for any period of four consecutive fiscal quarters, the sum of (i) Trailing Consolidated Net Income for such period, plus non-recurring and non-cash losses (net of tax for such period) minus non-recurring and non-cash gains (net of taxes for such period), (ii) Trailing Consolidated Interest Expense for such period and (iii) the Trailing amount of taxes, depreciation and amortization deducted from earnings in determining such Consolidated Net Income. FOR PURPOSES OF THIS CALCULATION, THE FIRST POST-ACQUISITION QUARTER OF MARKS CONSOLIDATED EBITDA FOR THE THREE MONTHS ENDED DECEMBER 31, 2008 WILL BE ADDED TO THE PRE-ACQUISITION CONSOLIDATED EBITDA OF MARKS FOR THE THREE QUARTERS ENDED JULY 31, 2008;

(2) Section 8.1 (b) of the Credit Agreement requiring the Debt Service Coverage Ratio of the Borrower and its Consolidated Subsidiaries to be at least 1.25 to 1.0 to the extent of non compliance for the Trailing four quarter period ended 12/31/08 solely to the extent such ratio was 1.08 to 1.0 instead of the required ratio (For purposes of defining Consolidated Cash Flow, the definition has been expanded as follows: "Consolidated Cash Flow": for any period of four consecutive fiscal quarters, net income, plus, without duplication, depreciation plus amortization of intangibles, minus capital expenditures, plus non-recurring and non-cash losses (net of tax) minus non-recurring and non-cash gains (net of taxes), in each case, of the Borrower and its Consolidated Subsidiaries with all accounting terms defined in accordance with GAAP, based upon receipt of the quarterly and/or annual financial statements. For the avoidance of doubt, non-recurring and non-cash losses must occur together to be added to the equation, and non-recurring and non-cash gains must occur together to be subtracted from the equation. FOR PURPOSES OF THIS CALCULATION, THE FIRST POST-ACQUISITION QUARTER OF MARKS CONSOLIDATED CASH FLOW FOR THE THREE MONTHS ENDED DECEMBER 31, 2008 WILL BE ADDED TO THE PRE-ACQUISITION CONSOLIDATED CASH FLOW OF MARKS FOR THE THREE QUARTERS ENDED JULY 31, 2008); and

(3) Section 8.1 (c) of the Credit Agreement requiring the Modified Quick Ratio of the Borrower and its Consolidated Subsidiaries to be at least 1.15 to 1.0 to the extent of non compliance for the Trailing Four Quarter period ended 12/31/08 solely to the extent such ratio was 1.06 to 1.0 instead of the required ratio.

The waivers described above are effective only in this instance for the purpose given, are limited to the circumstances and conditions set forth herein, and shall not be deemed to be a continuing or further waiver of these or any other covenants, terms or provisions of the Credit Agreement. The waivers described above will expire by their terms on March 15, 2009 unless reaffirmed on or prior to such date by the Required Lenders. No waiver of any single breach or default under the Credit Agreement shall be deemed to be a waiver of any other breach or default thereunder. It is understood that all covenants, terms and conditions of the Credit Agreement remain unmodified and in full force and effect.

In consideration of the grant of the above waivers, Borrower agrees that effective as of the date hereof the definitions of "Consolidated EBITDA", "Consolidated Cash Flow" and "LIBOR Rate" set forth in the Credit Agreement are modified to read as follows:

"Consolidated EBITDA": for any period of four consecutive fiscal quarters, the sum of (i) Trailing Consolidated Net Income for such period, plus non-recurring and non-cash losses (net of tax for such period) minus non-recurring and non-cash gains (net of taxes for such period), (ii) Trailing Consolidated Interest Expense for such period and (iii) the Trailing amount of taxes, depreciation and amortization deducted from earnings in determining such Consolidated Net Income.) FOR PURPOSES OF THIS CALCULATION, CONSOLIDATED EBITDA WILL INCLUDE MARKS CONSOLIDATED EBITDA PRIOR TO THE ACQUISITION DATE TO THE EXTENT NECESSARY TO REFLECT A FULL 4 QUARTERS OF MARKS USA CONSOLIDATED EBITDA.

"Consolidated Cash Flow": for any period of four consecutive fiscal quarters, net income, plus, without duplication, depreciation plus amortization of intangibles, minus capital expenditures, plus non-recurring and non-cash losses (net of tax) minus non-recurring and non-cash gains (net of taxes), in each case, of the Borrower and its Consolidated Subsidiaries with all accounting terms defined in accordance with GAAP, based upon receipt of the quarterly and/or annual financial statements. For the avoidance of doubt, non-recurring and non-cash losses must occur together to be added to the equation, and non-recurring and non-cash gains must occur together to be subtracted from the equation. FOR PURPOSES OF THIS CALCULATION, CONSOLIDATED CASH FLOW WILL INCLUDE MARKS CONSOLIDATED CASH FLOW PRIOR TO THE ACQUISITION DATE TO THE EXTENT NECESSARY TO REFLECT A FULL 4 QUARTERS OF MARKS CONSOLIDATED CASH FLOW.

"LIBOR Rate": with respect to any Eurodollar Loan for any Interest Period, the greater of (i) 2% per annum or (ii) the rate per annum (rounded upward, if necessary, to the nearest 1/32 of one percent) as determined on the basis of the offered rates for deposits in U.S. dollars, for a period of time comparable to such Interest Period which appears on the Telerate page 3750 as of 11:00 a.m. London time on the day that is two (2) London Banking Days preceding the first day of such Eurodollar Loan; provided, however, if the rate described above does not appear on the Telerate System on any applicable interest determination date, the rate shall be the rate (rounded upwards as described above, if necessary) for deposits in dollars for a period substantially equal to the Interest Period on the Reuter Page "LIBO" (or such other page as may replace the LIBO Page on that service for the purpose of displaying such rates), as of 11:00 a.m. (London Time), on the day that is two London Banking days prior to the beginning of such Interest Period. "Banking Day" shall mean, in respect of any city, any date on which commercial banks are open for business in that city.

Please indicate your consent and agreement to the amendment set forth in the last paragraph above by signing and dating a copy of this letter.

Very truly yours,

**CAPITAL ONE, N.A.**

By: /s/STEVEN RATNER

-----  
Name: Steven Ratner  
Title: Senior Vice President

**HSBC BANK USA, NATIONAL  
ASSOCIATION, as Administrative  
Agent and as a Lender**

By: /s/GARY SARRO

-----  
Name: Gary Sarro  
Title: First Vice President

The Borrower and Guarantors under the Credit Agreement acknowledge and consent to the amendment of the definition of LIBOR Rate set forth above.

**Borrower:**

**NAPCO SECURITY TECHNOLOGIES, INC.  
f/k/a Napco Security Systems, Inc.**

By: /s/KEVIN S. BUCHEL

-----  
Kevin S. Buchel  
Senior Vice President of  
Operations and Finance

**Guarantors:**  
**ALARM LOCK SYSTEMS, INC.**

*By: /s/KEVIN S. BUCHEL*

-----  
*Name: Kevin S. Buchel*

*Title: Senior Vice President*

**CONTINENTAL INSTRUMENTS, LLC**

*By: /s/KEVIN S. BUCHEL*

-----  
*Name: Kevin S. Buchel*

*Title : Manager*

**EXHIBIT 26.3**

**CERTIFICATE OF AMENDMENT OF  
CERTIFICATE OF INCORPORATION OF  
NAPCO SECURITY SYSTEMS, INC.**

NAPCO SECURITY SYSTEMS, INC., a corporation organized and existing under and by virtue of the General Corporation Law of the State of Delaware, DOES HEREBY CERTIFY:

FIRST: That at a meeting of the Board of Directors of NAPCO SECURITY SYSTEMS, INC. resolutions were duly adopted setting forth a proposed amendment to the Certificate of Incorporation of said Corporation, declaring said amendment to be advisable and directing that said amendment be considered at the 2008 Annual Meeting of Stockholders. The resolution setting forth the proposed amendment is as follows:

RESOLVED, that Article First of the Amended and Restated Certificate of Incorporation of the Company be, and hereby is, amended to read in its entirety as follows:

"First: The name of the corporation (the "Company") is NAPCO Security Technologies, Inc."

SECOND: That thereafter, pursuant to resolution of its Board of Directors, the 2008 Annual Meeting of Stockholders was duly called and held upon notice in accordance with Section 222 of the General Corporation Law of the State of Delaware, at which meeting the necessary number of shares as required by statute were voted in favor of the amendment.

THIRD: That said amendment was duly adopted in accordance with the provisions of Section 242 of the General Corporation Law of the State of Delaware.

IN WITNESS WHEREOF, said Corporation has caused this Certificate to be signed this 9th day of December, 2008.

**NAPCO SECURITY SYSTEMS, INC.**

By: */s/ Kevin S. Buchel*  
-----  
*Kevin S. Buchel*  
*Senior Vice President*

**EXHIBIT 26.4**

**CERTIFICATE OF INCORPORATION, AS AMENDED OF  
NAPCO SECURITY TECHNOLOGIES, INC.**

**FIRST:** The name of the corporation (hereinafter called the "Company") is **NAPCO SECURITY TECHNOLOGIES, INC.**

**SECOND:** The registered office of the Company is to be located at No. 100 West Tenth Street, in the City of Wilmington, in the County of New Castle, in the State of Delaware. The name of its registered agent at that address is The Corporation Trust Company.

**THIRD:** The purpose of the Company is to engage in any lawful act or activity for which corporations may be organized under the General Corporation Law of the State of Delaware.

**FOURTH:** The total number of shares of Common Stock which the Corporation is authorized to issue is forty million (40,000,000), and the par value of each such share is one cent (\$.01), amounting in the aggregate to \$400,000.

**FIFTH:** In furtherance and not in limitation of the powers conferred by statute, the board of directors is expressly authorized to make, alter or repeal the by-laws of the Company. In addition, to the powers and authorities hereinbefore or by statute expressly conferred upon them, the directors are hereby empowered to exercise all such powers and do all such acts and things as may be exercised or done by the corporation; subject, nevertheless, to the provisions of the statutes of Delaware, of this certificate, and to any by-laws from time to time made by the stockholders; provided, however, that no by-law so made shall invalidate any prior act of the directors which would have been valid if such by-law had not been made.

**SIXTH:** Whenever a compromise or arrangement is proposed between the Company and its creditors or any class of them and/or between the Company and its stockholders or any class of them, any court of equitable jurisdiction within the State of Delaware may, on the application in a summary way of the Company or of any creditor or stockholder thereof, or on the application of any receiver or receivers appointed for the Company under the provisions of Section 291 of Title 8 of the Delaware Code or on the application of trustees in dissolution or of any receiver or receivers appointed for the Company under the provisions of Section 279 of Title 8 of the Delaware Code, order a meeting of the creditors or class of creditors, and/or of the stockholders or class of stockholders of the Company, as the case may be, to be summoned in such manner as the said court directs. If a majority in number representing three-fourths in value of the creditors or class of creditors, and/or of the stockholders or class of stockholders of the Company, as the case may be, agrees to any compromise or arrangement and to any reorganization of the Company as a consequence of such compromise or arrangement, the said compromise or arrangement and the said reorganization shall, if sanctioned by the court to which the said application has been made, be binding on all the creditors or class of creditors, and/or on all the stockholders or class of stockholders of the Company, as the case may be, and also on the Company.

**SEVENTH:** Meetings of stockholders may be held outside the State of Delaware, if the by-laws so provide. The books of the corporation may be kept (subject to any provision contained in the statutes) outside the State of Delaware at such place or places as may be designated from time to time by the Board of Directors or in the by-laws of the corporation. Elections of directors need not be by ballot unless the by-laws of the corporation shall so provide.

**EIGHTH:** The Company shall, to the fullest extent permitted by the General Corporation Law of the State of Delaware, indemnify any and all persons whom it shall have power to indemnify from and against any and all expenses, liabilities or other matters.

**NINTH:** The name and mailing address of the incorporator is as follows:

Name:  
-----

Michael J. Fuchs

Mailing Address:  
-----

430 Park Avenue  
New York, New York 10022

TENTH: To the fullest extent permitted by the Delaware General Corporation Law now in effect and as amended from time to time, a director of the Corporation shall not be liable to the Corporation or its stockholders for monetary damages for breach of fiduciary duty resulting from actions or omissions while serving as a director.

ELEVENTH: The number of directors which shall constitute the whole Board of Directors shall be not less than three (3) and shall be fixed from time to time exclusively by the Board of Directors pursuant to a resolution adopted by a majority of the total number of authorized directors (whether or not there exist any vacancies in the previously authorized directorships at the time any such resolution is presented to the Board of Directors for adoption). At the Annual Meeting of Stockholders at which this Article is adopted, the directors shall be divided into three classes, designated Class I, Class II, and Class III (which at all times shall be as nearly equal in number as possible), with the term of office of Class III directors to expire at the 1999 Annual Meeting of Stockholders, the term of office of Class II directors to expire at the 2000 Annual Meeting of Stockholders, and the term of office of Class I directors to expire at the 2001 Annual Meeting of Stockholders. At each annual meeting of stockholders following such initial classification and election, directors elected to succeed those directors whose terms expire shall be elected for a term of office to expire at the third succeeding annual meeting of stockholders after their election. Subject to the rights of the holders of any class or series of the Voting Stock then outstanding, newly created directorships resulting from any increase in the authorized number of directors or any vacancies on the Board of Directors resulting from death, resignation, retirement, disqualification, removal from office or other cause may be filled by a majority vote of the directors then in office, though less than a quorum, and directors so chosen shall hold office for a term expiring at the annual meeting of stockholders at which the term of office of the class to which they have been elected expires. No decrease in the number of authorized directors constituting the entire Board of Directors shall shorten the term of any incumbent director.

**EXHIBIT 31.1**

**SECTION 302 CERTIFICATION**

I, Richard Soloway, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Napco Security Technologies, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report, based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

*Date: February 9, 2009*

*/S/RICHARD SOLOWAY*

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*Richard Soloway*  
*Chief Executive Officer*  
*(Principal Executive Officer)*

**EXHIBIT 31.2**

**SECTION 302 CERTIFICATION**

I, Kevin S. Buchel, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Napco Security Technologies, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report, based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

*Date: February 9, 2009*

*/S/KEVIN S. BUCHEL*

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*Kevin S. Buchel*  
*Chief Financial Officer*  
*(Principal Financial Officer)*

**EXHIBIT 32.1**

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Napco Security Technologies, Inc. (the "Company") on Form 10-Q for the period ending December 31, 2008 filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, RICHARD L. SOLOWAY, Chief Executive Officer of the Company, certify, that to the best of my knowledge, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

*Dated: February 9, 2009*

*/S/ RICHARD L. SOLOWAY*

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*Richard L. Soloway, Chief Executive Officer*

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Napco Security Technologies, Inc. (the "Company") on Form 10-Q for the period ending December 31, 2008 filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, KEVIN S. BUCHEL, Chief Financial Officer of the Company, certify, that to the best of my knowledge, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

*Dated: February 9, 2009*

*/S/ KEVIN S. BUCHEL*

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*Kevin S. Buchel, Chief Financial Officer*

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.