Optex Systems Holdings Inc
Form 8-K/A
January 12, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

AMENDMENT NO. 1 TO FORM 8-K

CURRENT REPORT

Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): March 30, 2009

OPTEX SYSTEMS HOLDINGS, INC.
(Exact Name of Registrant as Specified in Charter)

Delaware (State or other jurisdiction of incorporation)	333-143215 (Commission File Number)	33-143215 (IRS Employer Identification No.)

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

Registrant’s telephone number, including area code: 972-238-0722

Sustut Exploration, Inc. 1420 5th Avenue #220
Seattle, Washington 98101
(Former name or former address, if changed since last report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

o Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

o Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 DFR 240.14a-12)

o Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

o Pre-commencement communications pursuant to Rule 13e-4 (c) under the Exchange Act (17 CFR 240.13e-4(c))

ITEM 1.01 Entry into Material Definitive Agreement.

On March 30, 2009, Optex Systems Holdings, Inc. (formerly known as Sustut Exploration, Inc., and the name was changed on March 26, 2009 pursuant to an amendment to the Articles of Incorporation, filed with the State of Delaware) entered into an Agreement and Plan of Reorganization (the "Reorganization Agreement") with Optex Systems, Inc., a privately-held Delaware corporation ("Optex Systems Inc., (Delaware)").

The parties closed the transaction on or about March 30, 2009.

Thus, a reorganization occurred whereby the then existing shareholders of Optex Systems Inc., (Delaware) exchanged their shares of common stock with the shares of common stock of Optex Systems Holdings as follows: (i) the outstanding 85,000,000 shares of Optex Systems Inc., (Delaware) common stock were exchanged by Optex Systems Holdings for 113,333,282 shares of Optex Systems Holdings common stock, (ii) the outstanding 1,027 shares of Optex Systems Inc., (Delaware) Series A preferred stock were exchanged by Optex Systems Holdings for 1,027 shares of Optex Systems Holdings Series A preferred stock and (iii) the 8,131,667 shares of Optex Systems Inc., (Delaware) common stock purchased in the private placement, which also occurred on March 30, 2009, were exchanged by Optex Systems Holdings for 8,131,667 shares of Optex Systems Holdings common stock. The per share price in the private placement was $0.15 per share of common stock, and the closing date was March 30, 2009. Optex Systems Inc., (Delaware) remains a wholly-owned subsidiary of Optex Systems Holdings.

At the time of the reorganization, 25,000,000 shares owned by Andrey Oks, the former CEO of Optex Systems Holdings, were cancelled. Immediately prior to the closing, 17,449,991 shares of Company common stock were outstanding. The 17,449,991 shares derives from the 17,999,995 shares outstanding as of December 31, 2008 plus the 26,999,996 shares issued in conjunct with the 2.5:1 forward stock split authorized by the Sustut Board and shareholders and effected on February 27, 2009 less retirement of Andrey Oks' 25,000,000 shares. The total outstanding common shares of Optex Systems Holdings subsequent to the closing of the reorganization is as follows:

Existing Sustut Shareholders	17,449,991
Optex Systems Inc., (Delaware) shares exchanged	113,333,282
Optex Systems Inc., (Delaware) Private Placement shares exchanged	8,131,667
Total Shares after reorganization	138,914,940

Optex Systems Holdings, Shareholders and Optex entered into this Agreement which provides, among other things, that (i) the outstanding 85,000,000 shares of Optex Common Stock be exchanged by Optex Systems Holdings for 113,333,282 shares of Optex Systems Holdings Common Stock, (ii) the outstanding 1,027 shares of Optex Series A Preferred Stock be exchanged by Optex Systems Holdings for 1,027 shares of Optex Systems Holdings Series A Preferred Stock and such additional items as more fully described in the Agreement and (iii) the 8,131,667 shares of Optex purchased in the private placement were exchanged by Optex Systems Holdings for 8,131,667 shares of Optex Systems Holdings Common Stock, as acknowledged by Optex Systems Holdings. Accordingly, following closing, Optex will be a wholly-owned subsidiary of the Optex Systems Holdings, and the Optex Systems Holdings will have a total of approximately 138,914,940 million common stock shares issued and outstanding, of which 17,449,991 million will be owned by persons who were previously shareholders of the Optex Systems Holdings and 121,464,949 will be owned by persons who were previously shareholders of Optex, and/or their nominees. Optex Systems Holdings will also have 1,027 shares of its Series A Preferred Stock outstanding which will be owned by persons who were previously creditors of Optex.

In addition, pursuant to the terms and conditions of the Reorganization Agreement upon Closing:

- The Optex Systems Holdings' board of directors was reconstituted to consist initially of Stanley Hirschman, Merrick Okamoto and Ronald Richards.

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- All prior officers of the Optex Systems Holdings resigned and the newly constituted board of directors appointed Stanley Hirschman as President, and appointed such other officers as it deemed necessary and in the best interests of the Optex Systems Holdings.

- Following closing, the Optex Systems Holdings shall complete the sale, transfer or other disposition of its pre-closing business operations, including all assets and liabilities related to such operations.

Item 2.01 Completion of Acquisition or Disposition of Assets .

Information regarding the principal terms of the reorganization and Optex Systems Holdings and Optex Systems Inc., (Delaware) are set forth below.

The Reorganization

Reorganization/Share Exchange

On March 30, 2009, the reorganization occurred whereby the then existing shareholders of Optex Systems Inc., (Delaware) exchanged their shares of common stock with the shares of common stock of Optex Systems Holdings as follows: (i) the outstanding 85,000,000 shares of Optex Systems Inc., (Delaware) common stock were exchanged by Optex Systems Holdings for 113,333,282 shares of Company common stock, (ii) the outstanding 1,027 shares of Optex Systems Inc., (Delaware) Series A preferred stock were exchanged by Optex Systems Holdings for 1,027 shares of Company Series A preferred stock and (iii) the 8,131,667 shares of Optex Systems Inc., (Delaware) common stock purchased in the private placement were exchanged by Optex Systems Holdings for 8,131,667 shares of Company common stock. Following the reorganization, Optex Systems Inc., (Delaware) remained a wholly-owned subsidiary of Optex Systems Holdings.

Shares outstanding of Optex Systems Holdings just prior to the close consisted of 17,449,991 shares of which 1,250,000 shares were issued on March 27, 2009 as payment for Investor Relations Services, of which 700,000 were surrendered to Optex Systems Holdings upon termination of one of the Investor Relations contracts in June 2009. See Note 11 – “Subsequent Events” for a further discussion of the termination of the relationship with one of Optex Systems Holdings’ investor relations firms and appointment of a replacement service provider.

Private Placement

Prior to the closing under the reorganization agreement, Optex Systems Inc., (Delaware) accepted subscriptions from accredited investors for a total 27.1 units, for $45,000 per unit, with each unit consisting of 300,000 shares of common stock of Optex Systems Inc., (Delaware) and warrants to purchase 300,000 shares of common Stock for $0.45 per share for a period of five years from the initial closing, which were issued by Optex Systems Inc., (Delaware) after the closing referenced above. Gross proceeds to Optex Systems Inc., (Delaware) were $1,219,750, and after deducting (i) a cash finder’s fee of $139,555, (ii) non-cash consideration of indebtedness owed to an investor of $146,250, and (iii) stock issuance costs of $59,416, the net proceeds were $874,529. The finder also received five year warrants to purchase 2.39 units, at an exercise price of $49,500 per unit.

Neither Optex Systems Holdings nor Optex Systems Inc., (Delaware) had any options or warrants to purchase shares of capital stock outstanding immediately prior to or following the reorganization, except for 8,941,667 warrants issued in the private placement. Immediately prior to the closing, Optex Systems Holdings adopted the 2009 Stock Option Plan providing for the issuance of up to 6,000,000 shares for the purpose of having shares available for the granting of options to officers, directors, employees and to independent contractors who provide services. Each share of stock entitles the holder to one vote on matters brought to a vote of the shareholders.

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All of the above equity transactions were made in reliance on Section 4(2) of the Securities Act, with the exception of the equity sale completed just prior to the closing of the reorganization agreement, which was exempt from registration pursuant to Regulation D and for which a Form D was filed by Optex Systems Inc., (Delaware) with the Commission on December 16, 2008.

Changes Resulting from the Reorganization. Registrant's business is now the business of Optex Systems Inc., (Delaware).

Optex Systems Holdings manufactures optical sighting systems and assemblies primarily for Department of Defense applications. Optical sighting systems are used to enable a soldier to have improved vision and in some cases, protected vision. One type of system would be a binocular which would have a special optical filter applied to the external lens which would block long wave length light (from a laser) from reaching the soldier's eyes. Another type of system would be a periscope where the soldier inside an armored vehicle needs to view the external environment outside of the tank. In this case, the visual path is reflected at two 90 degree angles enabling the soldier to be at a different plane than that of the external lens.

The following table describes the approximate percentage of revenue represented by the types of systems mentioned in the third and fourth sentences of the above paragraph. The table below reflects approximate product revenues and is a balanced overview of our business based on the percentages.

	% of Revenue
Howitzer Programs	11.0%
Periscope Programs	50.0%
Sighting Systems	20.0%
All Other	19.0%
Total	100.0%

Optex Systems Holdings' products consist primarily of build-to-customer print products that are delivered both directly to the armed services and to other defense prime contractors. Build-to-customer print products are those devices where the customer completes the design of the product and then brings these drawings to the supplier for production. In this case, the supplier would procure the piece parts from suppliers, build the final assembly, and then supply this product back to the original customer who designed it.

Our products are installed on a majority of types of U.S. military land vehicles, such as the Abrams and Bradley fighting vehicles, light armored and armored security vehicles and have been selected for installation on the Stryker family of vehicles. Optex Systems Holdings also manufactures and delivers numerous periscope configurations, rifle and surveillance sights and night vision optical assemblies. Approximately 30% of our current revenue is in support of Abrams vehicles, 5% in support of Stryker vehicles, and 25% in support of Bradley vehicles. The products that we produce can be used on other vehicles; however, they were originally designed for the Abrams, the Bradley, and the Stryker vehicles. In addition, some of the periscopes that we produce can be used on both the Bradley and the Styker vehicle. Finally, some customers combine their volumes for new vehicles with those requirements for replacement parts for vehicles coming back from the field. At this time, no vehicle generates more revenues than the Stryker vehicle other than the Abrams and Bradley vehicles.

Optex Systems Inc., (Delaware), and its Predecessor Optex Systems Inc., (Texas), have been in business since 1987. Optex Systems Holdings is located in Richardson, TX and is ISO 9001:2008 certified.

Following completion of the Reorganization, the Company has carried on Optex Systems Inc., (Delaware)'s business as its sole line of business. Optex Systems Holdings, Inc.'s offices are located at 1420 Presidential Drive, Richardson, TX 75081-2439, and its telephone number is (972) 238-1403.

Changes to the Board of Directors. In conjunction with closing under the terms of the reorganization agreement, the number of members of the Company's board of directors was increased to three and Stanley Hirschman, Ronald Richards and Merrick Okamoto were appointed to serve as Directors of the Company and Andrey Oks resigned. Ronald Richards was appointed as Chairman of the board of directors.

All of the Company's directors will hold office until the next annual meeting of the stockholders or until the election and qualification of their successors. The Company's officers are elected by the board of directors and serve at the discretion of the board of directors.

Name Change and Stock Option Plan. On or about March 26, 2009, the Registrant's board of directors and shareholders approved the change of the Registrant's name to "Optex Systems Holdings, Inc." and approved the 2009 Stock Option Plan.

2009 Stock Option Plan. The purpose of the Plan is to assist the Registrant in attracting and retaining highly competent employees and to act as an incentive in motivating selected officers and other employees of the Registrant and its subsidiaries, and directors and consultants of the Registrant and its subsidiaries, to achieve long-term corporate objectives. There are 6,000,000 shares of common stock reserved for issuance under this Plan. As of March 31, 2009, the Registrant had not issued any stock options under this Plan.

BUSINESS

Background

Prior History - Sustut Exploration, Inc.

Sustut was a Delaware corporation formed on April 11, 2006 to search for available properties in north central British Columbia. In May 2006, Sustut entered into an agreement which was negotiated at arms length with Richard Simpson to acquire a 100% interest in the WILLOW claim purported to be located in the Omineca Mining Division, NTS map sheet 94D/10E. The property could have been acquired from Simpson by paying a total of $75,000 in two option payments with the last option payment being due on May 15, 2008, however, Sustut did not make the required payments and did not acquire title to those property rights.

The mineral claim which was to be Sustut's primary business expired on May 15, 2008 leaving Sustut with no operating business of which to dispose. The Company does not believe it presently maintains any rights related to the Willowvale project and does not intend to pursue a mining or mineral business. In the event that Mr. Simpson seeks payment of any amount the Company does not intend to make any payment to exercise any option or extend the term of the rights, if any continue to exist.

Reorganization

On March 30, 2009, a reorganization occurred whereby the then existing shareholders of Optex, Inc., a Delaware corporation ("Optex Systems, Inc. (Delaware)") exchanged their shares of Optex Systems, Inc. (Delaware) common stock with the shares of common stock of Optex Systems Holdings as follows: (i) the outstanding 85,000,000 shares of Optex Systems, Inc. (Delaware) common stock were exchanged for 113,333,282 shares of Optex Systems Holdings common stock, (ii) the outstanding 1,027 shares of Optex Systems, Inc. (Delaware) Series A preferred stock were exchanged for 1,027 shares of Optex Systems Holdings Series A preferred stock and (iii) the 8,131,667 shares of Optex Systems, Inc. (Delaware) common stock purchased in the private placement were exchanged for 8,131,667 shares of Optex Systems Holdings common stock. Optex Systems, Inc. (Delaware) has remained a wholly-owned subsidiary of Company, and the Optex Systems, Inc. (Delaware) shareholders are now shareholders of Optex Systems Holdings. As a result of the reorganization, Sileas Corporation ("Sileas") beneficially owns approximately 73.52% of the issued and outstanding common stock of Optex Systems Holdings and Arland Holdings, Ltd. ("Arland") owns 5.89% of the issued and outstanding common stock of Optex Systems Holdings. Furthermore, at the time of the reorganization, Andrey Oks resigned as the sole officer and director of the Optex Systems Holdings. Additionally, Stanley Hirschman, Ronald Richards and Merrick Okamoto were appointed as its Directors, and Stanley Hirschman, Danny Schoening and Karen Hawkins were appointed as its President, COO and V.P. of Finance/Controller, respectively.

Prior to the closing under the reorganization agreement, Optex Systems, Inc. (Delaware) accepted subscriptions from accredited investors for a total 27.1 units, for $45,000 per unit, with each unit consisting of 300,000 shares of common stock of Optex Systems, Inc. (Delaware) and warrants to purchase 300,000 shares of common Stock for $0.45 per share for a period of five years from the initial closing, which were issued by Optex Systems, Inc. (Delaware) after the closing referenced above. Gross proceeds to Optex Systems, Inc. (Delaware) were $1,219,750, and after deducting (i) a cash finder's fee of $139,555, (ii) non-cash consideration of indebtedness owed to an investor of $146,250, and (iii) stock issuance costs of $59,416, the net proceeds were $874,529. The finder also received five year warrants to purchase 2.39 units, at an exercise price of $49,500 per unit.

Contracts

Each contract with Optex Systems Holdings' customers has specific quantities of material that need to be purchased, assembled, and finally shipped. Prior to bidding a contract, Optex Systems Holdings contacts potential sources of material and receives qualified quotations for this material. In some cases, the entire volume is given to a single supplier and in other cases, the volume might be split between several suppliers. If a contract has a single source supplier and that supplier fails to meet their obligations (e.g., quality, delivery), then Optex Systems Holdings would attempt to find an acceptable alternate supplier. Contractual deliverables would then be re-negotiated (e.g., specifications, delivery, price.). Currently, approximately 28% of our total material requirements are single sourced across 21 suppliers representing approximately 20% of our active supplier base. Single sourced component requirements span across all of our major product lines. Of these single sourced components, we have material contracts (purchase orders) with firm pricing and delivery schedules in place with each of the suppliers to supply the parts necessary to satisfy our current contractual needs.

We are subject to, and must comply ,with various governmental regulations that impact, among other things, our revenue, operating costs, profit margins and the internal organization and operation of our business. The most significant regulations affecting our U.S. government business are summarized in the table below:

Regulation	Summary
Federal Acquisition Regulation	The principal set of rules in the Federal Acquisition Regulation System. This system consists of sets of regulations issued by agencies of the Federal government of the United States to govern what is called the "acquisition process," which is the process through which the government purchases ("acquires") goods and services. That process consists of three phases: (1) need recognition and acquisition planning, (2) contract formation, and (3) contract administration. The Federal Acquisition Regulation System regulates the activities of government personnel in carrying out that process. It does not regulate the purchasing activities of private sector firms, except to the extent that parts of it are incorporated into government solicitations and contracts by reference.
International Traffic in Arms Regulations	United States government regulations that control the export and import of defense-related articles and services on the United States Munitions List. These regulations implement the provisions of the Arms Export Control Act.

Truth in Negotiations Act	A public law enacted for the purpose of providing for full and fair disclosure by contractors in the conduct of negotiations with the Government. The most significant provision included is the requirement that contractors submit certified cost and pricing data for negotiated procurements above a defined threshold, currently $650,000. Requires contractors to provide the Government with an extremely broad range of cost or pricing information relevant to the expected costs of contract performance. Requires contractors and subcontractors to submit cost or pricing data to Government and to certify that, to the best of their knowledge and belief, the data are current, accurate, and complete.

Optex Systems Holdings is responsible for full compliance with the Federal Acquisition Regulation. Upon award, the contract may identify certain regulations that Optex Systems Holdings needs to meet. For example, a contract may allow progress billing pursuant to specific Federal Acquisition Regulation clauses incorporated into the contract. Other contracts may call for specific first article acceptance and testing requirements. The Federal Acquisition Regulation will identify the specific regulations that Optex Systems Holdings must follow based on the type of contract awarded. The Federal Acquisition Regulation also contains guidelines and regulations for managing a contract after award, including conditions under which contracts may be terminated, in whole or in part, at the government's convenience or for default. These regulations also subject us to financial audits and other reviews by the government of our costs, performance, accounting and general business practices relating to our government contracts, which may result in adjustment of our contract-related costs and fees and, among other things and impose accounting rules that define allowable and unallowable costs governing our right to reimbursement under certain contracts. The full text of the Federal Acquisition Regulation System is located at the Library of Congress.

First Article Testing and Acceptance requirements are defined under the Federal Acquisitions Regulation, Part 9 – Contractor Qualification, Subpart 9.3 – First Article Testing and Approval. For example, first article testing on a Howitzer type product is very comprehensive and very time consuming. Each piece part of the assembly requires each dimension and material specification to be verified, and each product has in excess of 100 piece parts. Once the individual piece parts are verified to be compliant to the specification, the assembly processes are documented and verified. A sample of the production (typically 3 units) is verified to meet final performance specifications. Once the units meet the final performance specification, they are then exposed to a series of tests which simulate the lifetime use of the product in the field. This consists of exposing the units to thermal extremes, humidity, mechanical shock, vibration, and other physical exposure tests. Once completed, the units undergo a final verification that no damage has occurred as a result of the testing and that they continue to meet the performance specification. All of the information and data is recorded into a final first article inspection and test report and submitted to the customer along with the test units for final approval. First Article Acceptance and Testing is generally required on new contracts/product awards but may also be required on existing products or contracts where there has been a significant gap in production, or where the product has undergone significant manufacturing process, material, tooling, equipment or product configuration changes.

Optex Systems Holdings, Inc. is also subject to laws, regulations and executive orders restricting the use and dissemination of information classified for national security purposes and the exportation of certain products and technical data as covered by the International Traffic in Arms Regulation. In order to import or export items listed on the U.S. Munitions List, we are required to be registered with the Directorate of Defense Trade Controls office. The registration is valid for 1 year and the registration fees are established based on the number of license applications submitted the previous year. Optex Systems Holdings currently has an approved and current registration on file with the Directorate of Defense Trade Controls office. Once the registration is approved, each import/export license must be filed separately. License approval requires the company to provide proof of need, such as a valid contract or purchase order requirement for the specific product or technical data requested on the license and requires a detailed listing of the items requested for export/import, the end-user, the end-user statement, the value of the items, consignees/freight forwarders and a copy of a valid contract or purchase order from the end-user. The approval process for the license can vary from several weeks to six months or more. The licenses Optex Systems Holdings currently uses are the DSP-5 (permanent export) and DSP-73 (temporary export). The aforementioned licenses are all valid for 48 months from date of issue. Optex Systems Holdings currently has 7 active DSP-5's and 4 active DSP-73's. Licenses are subject to termination if a licensee is found to be in violation of the Arms Export Control Act or the International Traffic in Arms Regulations requirements. If a licensee is found to be in violation, in addition to a termination of its licenses, it can be subject to fines and penalties by the government.

Optex Systems Holdings' contracts may also be governed by the Truth in Negotiation Act requirements where certain of our contracts or proposals exceed the $650,000 threshold and/or are deemed as sole source, or non competitive awards, covered under this Act. These contracts require that Optex Systems Holdings provide a vast array of cost and pricing data in addition to certification that our pricing data and disclosure materials are current, accurate and complete upon conclusion of the negotiation. Due to the additional disclosure and certification requirements, if a post contract award audit were to uncover that the pricing data provided was in any way not current accurate or complete as of the certification date, Optex could be subjected to a defective pricing claim adjustment with accrued interest. Currently, Optex does not have any pending claims as a result of defective pricing as a result of these covered contracts. Additionally, as a result of this requirement, contract price negotiations may span from two to six months and will often result in undefinitized or not to exceed ceiling priced contracts subject to future downward negotiations and price adjustments. Currently, Optex Systems Holdings does not have any undefinitized contracts subject to further price negotiation.

Our failure to comply with applicable regulations, rules and approvals or misconduct by any of our employees could result in the imposition of fines and penalties, the loss of security clearances, the loss of our U.S. government contracts or our suspension or debarment from contracting with the U.S. government generally, any of which could have a material adverse effect our business, financial condition, results of operations and cash flows. We are currently in compliance with all applicable regulations and do not have any pending claims as a result of non compliance.

The material terms of our five largest contracts are as follows:

Customer	Customer PO/Contract	Contract Type	Contract Quantities Min Qty	Max Qty	Total Award Value	Progress Billable (1)	Order Period Expiration	Delivery Period
General Dynamics Land Systems	PCL860000 PCL860005 (Multiple Prime Contracts)	6 year blanket order with Fixed Qty Contract release which includes ability to in crease or decrease quantity on each release up to 20% from PO release quantity.	N/A	N/A	$ 14,813,100	Yes	Expired	Dec 2007 - Jan 2011
Tank-automotive and Armaments Command - ROCK ISLAND	W52H09-05-D-0260	5 Year Firm Fixed Price (3)	138	2,100	$ 7,261,716	Yes	30-Jun-2010	Oct 2007-Jan 2011
Tank-automotive and Armaments Command - ROCK ISLAND	W52H09-05-D-0248	5 Year Firm Fixed Price (3)	138	1,250	$ 5,006,119	Yes	30-Jun-2010	Apr 2007- Jul 2010

Tank-automotive and Armaments Command - ROCK ISLAND	W52H09-09-D-0128	Evaluated Pricing (3). Restricted Procurement between Optex Systems & Miller Holzwarth	250 each supplier	250 each supplier	$ 118,250(2)	Yes	31-Dec-2011	Initial award deliverable Aug - Sept 2009. Additional awards not to exceed aggregate 2000 units per month total units.
General Dynamics Land Systems	40050551 (Multiple Prime Contracts)	Firm Fixed Price and Fixed Quantity Purchase Order	N/A	N/A	$ 5,380,137	Yes	N/A	Jan 2011 - Feb 2013

(1) Payment terms on shipments are all net 30 days.

(2) Only first delivery order awarded. Maximum order value potential of up to $22 million with expected award value of $7.5 million. We estimate the maximum order potential at $22 million based on the government's estimated maximum order quantity for each periscope type times the Optex not to exceed price per unit for each of the solicited periscope assemblies. The $7.5 million expected value is derived based on the governments estimated quantity requirement for each periscope type across the contract period times Optex proposed not to exceed price per unit, assuming that the award is split equally between Optex and the other supplier.

(3) Indefinite Delivery/Indefinite Quantity type contract.

Organizational History

On October 14, 2008, in a transaction that was consummated via public auction, Optex Systems Inc., (Delaware) (Successor) purchased all of the assets of Optex Systems Inc., (Texas) (Predecessor) in exchange for $15 million of Irvine Sensors Corporation debt and the assumption of approximately $3.8 million of certain liabilities of Optex Systems Inc., (Texas). Optex Systems Inc., (Delaware) was formed by the Longview Fund, LP and Alpha Capital Antstalt, former secured creditors of Irvine Sensors Corporation, to consummate the transaction with Optex Systems Holdings, and subsequently, on February 20, 2009, Longview Fund conveyed its ownership interest in Optex Systems Holdings to Sileas, an entity owned by three of Optex Systems Holdings' officers (one of whom is also one of Optex Systems Holdings' three directors). On March 30, 2009, a reorganization occurred whereby Optex Systems Inc., (Delaware) became a wholly-owned subsidiary of Optex Systems Holdings.

Products

The Company's products are installed on a majority of types of U.S. military land vehicles, such as the Abrams and Bradley fighting vehicles, light armored and advanced security vehicles and have been selected for installation on the Future Combat Systems (FCS) Stryker vehicle. Optex Systems Holdings also manufactures and delivers numerous periscope configurations, rifle and surveillance sights and night vision optical assemblies. Optex Systems Holdings delivers its products both directly to the military services and to prime contractors.

Optex Systems Holdings delivers high volume products, under multi-year contracts, to large defense contractors and government customers. Optex Systems Holdings has a reputation for quality and credibility with its customers as a strategic supplier. Optex Systems Holdings also anticipates the opportunity to integrate some of its night vision and optical sights products into commercial applications.

Specific product lines include:

- Electronic sighting systems
- Mechanical sighting systems
- Laser protected glass periscopes
- Laser protected plastic periscopes
- Non-laser protected plastic periscopes
- Howitzer sighting systems
- Ship binoculars
- Replacement optics (e.g. filters, mirrors)

Location and Facility

We are located in Richardson, TX in a 49,000 square foot facility and currently has 107 full time employees. We operate with a single shift, and capacity could be expanded by adding a second shift. Our proprietary processes and methodologies provide barriers to entry by other competing suppliers. In many cases, we are the sole source provider or one of only two providers of a product. We have capabilities which include machining, bonding, painting, tracking, engraving and assembly and can perform both optical and environmental testing in-house. We lease our facility, and the lease currently expires on February 28, 2010. We are presently in negotiations with the landlord regarding a lease extension, and we are also exploring the possibility of moving to another location. Mixed use space, such as that leased by us (which is approximately 25% office space and 75% manufacturing space, in the case of us), is readily available in our general geographic area. (See subsequent events in Note 9 of Financial Statements)

Prior Operational/Financial Challenges; Recovery; and Future Growth Potential

While Optex Systems Inc., (Texas) (Predecessor) was a wholly-owned subsidiary of Irvine Sensors Corporation, Irvine Sensors Corporation faced certain business challenges and utilized the cash flow from Optex Systems Inc., (Texas) to meet its own funding needs. This left Optex Systems Inc., (Texas) with limited working capital to satisfy its own operating needs.

As of the year ended September 28, 2008, Optex Systems Inc., (Texas) (Predecessor) reported $4.3 million of liabilities attributable to corporate expenses allocated to Optex Systems Inc., (Texas) (Predecessor) through an intercompany payable account “Due to Parent”. These costs were for expenses incurred by Irvine Sensors Corporation on behalf of Optex Systems Inc., (Texas), including legal, audit, and consulting fees; insurance costs; and significant amounts of Irvine Sensors Corporation general overhead allocated to Optex Systems Inc., (Texas). The outstanding “Due to Parent” balance was not acquired by the company as part of the October 14, 2008 transaction. Therefore, this balance will have no impact on future operating results or liquidity. We anticipate incurring similar expenses for fiscal year 2009 as follows:

Accounting & Auditing Fees	$ 250,000
Legal Fees	60,000
Consulting Fees	60,000
Workers Comp & General Insurance	70,000
Total	$ 440,000

As a result of the purchase of Optex Systems, Inc. (Texas) on October 14, 2008, these general and administrative costs are incurred and paid directly by Optex Systems, Inc. (Delaware) for the 2009 fiscal year, and have been reflected in the financial statements to the extent incurred through December 28, 2008.

Since the buyout, the business outlook for Optex Systems Holdings has changed dramatically. Management has strengthened Optex Systems Holdings’ balance sheet and has increased operational efficiencies and productivity, as demonstrated by the significant $1.45 million reduction in operating loss to $(15,193) versus $(1,468,192) for the total for the periods September 29, 2008 through October 14, 2008 (Predecessor) and October 15, 2008 through June 28, 2009 (Successor) and the nine months ended June 28, 2008 (Predecessor), respectively. Management expects to achieve additional improvement in operations over time.

Virtually all of our contracts are prime or subcontracted directly with the Federal government and are subject to Federal Acquisition Regulation Subpart 49.5, “Contract Termination Clauses” and more specifically Federal Acquisition Regulation clauses 52.249-2 “Termination for Convenience of the Government (Fixed-Price)”, and 49.504 “Termination of fixed-price contracts for default”. These clauses are standard clauses on our prime military contracts and are generally “flowed down” to us as subcontractors on other military business. It has been our experience that the termination for convenience is rarely invoked, except where it has been mutually beneficial for both parties. We are currently not aware of any pending terminations for convenience or default on our existing contracts.

In the event a termination for convenience were to occur, these Federal Acquisition Regulation clause 52.249-2 provides for full recovery of all contractual costs and profits reasonably occurred up to and as a result of the terminated contract. In the event a termination for default were to occur, we could be liable for any excess cost incurred by the government to acquire replacement supplies from another supplier. We would not be liable for any excess costs if the failure to perform the contract arises from causes beyond the control and without the fault or negligence of the company as defined by Federal Acquisition Regulation clause 52.249-8. In addition, the U.S. government may require us to transfer title and deliver to it any completed supplies, partially completed supplies and materials, parts, tools, dies, jigs, fixtures, plans, drawings, information, and contract rights that we specifically produced or acquired for the terminated portion of this contract. The U.S. government is required to pay contract price for completed supplies delivered and accepted, and the parties are required to negotiate an agreed upon amount of payment for manufacturing materials delivered and accepted and for the protection and preservation of the property. Failure to agree on an amount for manufacturing materials is subject to the Federal Acquisition Regulation Disputes clause 52.233-1.

In some cases, we may receive orders subject to subsequent price negotiation on contracts exceeding the $650,000 federal government simplified acquisition threshold. These "undefinitized" contracts are considered firm contracts, but as Cost Accounting Standards Board covered contracts, they are subject to the Truth in Negotiations Act disclosure requirements and downward-only price negotiation. As of September 28, 2008 and September 30, 2007, approximately $4.0 million and $10.0 million of booked orders fell under this criterion, respectively. As of December 28, 2008 there were $5.0 million booked orders that fell under this criterion. Our experience has been that the historically negotiated price differentials have been immaterial and we do not anticipate any significant downward adjustments on these booked orders.

We are currently bidding on several substantial government contracts to expand sales and production beyond the current production and backlog. We are also exploring possibilities to adapt some of our products for commercial use in those markets that demonstrate potential for solid revenue growth.

Market Opportunity – U.S. Military

Our products are currently marketed to the military and related government markets. Since 1998, annual U.S. military spending has increased over 225% to over $600 billion. The trend of significant growth in government spending on the military and defense is very positive for Optex Systems Holdings and others in the defense industry sector. The data suggests that the market continues to be robust and Optex Systems Holdings believes the markets for new and replacement parts, such as those manufactured by Optex Systems Holdings, are significant.

The chart below was derived from public government spending sources and depicts total U.S. Military Spending from 1998 through 2008. Total military spending increased from $268.2 billion in 1998 to $607.3 billion in 2008 representing a total increase in military spending of 226% in the last 10 years. It is difficult to directly tie this spending to any specific military vehicles; however, Optex Systems Holdings serves the U.S. armed forces and state national guards. The purpose of including this chart is to provide the reader with trend data showing increased military spending by the government since 1998, which is a favorable trend for Optex Systems Holdings' overall business.

Source: Government Printing Office, U.S. Budget Historical Tables, FY 2008, Table 3.2 Outlays by function and subfunction, 1962-2012

The following factors are important to the U.S. military:

- Reliability – failure can cost lives

- Time delivery to schedule

- Cost effectiveness
- Armed forces need to be able to see to perform
- Mission critical products.

Optex Systems Holdings focuses on delivering products that satisfy these factors and believes it is well positioned to continue to service U.S. military needs.

Market Opportunity – Commercial

Optex Systems Holdings' products are currently sold exclusively to military and related government markets. We believe there may be opportunities to commercialize various products we presently manufacture to address other markets. Our initial focus will be directed in three product areas.

- Big Eye Binoculars – While the military application we produce is based on mature military designs, Optex Systems Holdings owns all castings, tooling and glass technology. These large fixed mount binoculars could be sold to Cruise Ships, Personal Yachts and Cities/Municipalities.
- Night Vision Sight – Optex Systems Holdings manufactured the Optical System for the NL-61 Night Vision Sight for the Ministry of Defense of Israel. This technology is based on the I Squared design and could be implemented for commercial applications.
- Infrared Imaging Equipment – Optex Systems Holdings manufactures and assembles Infrared Imaging Equipment for Textron and components for Raytheon's Thermal Imaging M36 Mount product. This equipment and technology has potential to be assembled for border patrol, police and security agencies.

Customer Base

Optex Systems Holdings serves customers in three primary categories: as prime contractor (Tank-automotive and Armaments Command , U.S. Army, Navy and Marine Corps), as subcontractor (General Dynamics, BAE, Raytheon and Northrop) and also as a supplier to foreign governments Israel, Australia and NAMSA). For reference, TACOM is Tank-automotive and Armaments Command, and NAMSA is the NATO Maintenance and Supply Agency, which is the main logistics agency of NATO. Although we do serve all three of these categories, at present, approximately 93% of the gross revenue from our business is derived from two customers, General Dynamics Land System Division and Tank-automotive and Armaments Command , with which we have approximately 50 discrete contracts that are utilized in vehicles, product lines and spare parts. Given the size of General Dynamics Land System Division and Tank-automotive and Armaments Command as well as the fact that the contracts are not interdependent, we are of the opinion that this provides us with a fairly well diversified revenue pool.

Marketing Plan

Potential Entrants – Low. In order to enter this market, potential competitors must overcome several barriers to entry. The first hurdle is that an entrant would need to prove the existence of a government approved accounting systems for larger contracts. Second, the entrant would need to develop the processes required to produce the product. Third, the entrant would then need to produce the product and then submit successful test requirements (many of which require lengthy government consultation for completion). Finally, in many cases the customer has an immediate need and therefore cannot wait for this qualification cycle and therefore must issue the contracts to existing suppliers.

Buyers – Medium. In most cases the buyers have two fairly strong suppliers. It is in their best interest to keep at least two, and therefore in some cases the contracts are split between suppliers. In the case of larger contracts, the customer can request an open book policy on costs and expects a reasonable margin to have been applied.

Substitutes – Low. Optex Systems Holdings has both new vehicle contracts and replacement part contracts for the exact same product. The US Government has declared that the Abrams/Bradley base vehicles will be the ground vehicle of choice out through 2040. The Bradley vehicle has been in service for 28 years, the Abrams for 27 years. Therefore it appears that the systems are capable of a life of approximately 30 years. In February 2008, the Army signed a 5 year multi-year contract for the delivery of improved Abrams and Bradleys. The contract is for up to 435 tanks and 540 Bradley vehicles. These are the only production tanks currently being procured by the government. This in conjunction with the 30 year life span supports their continued use through 2040. There are no replacement systems being proposed or funded at this time. The Abrams is the principal battle tank of the United States Army and Marine Corps, and the armies of Egypt, Kuwait, Saudi Arabia, and since 2007, Australia. The new contract terms allow efficiencies within the supply chain and a very long return on investment on new vehicle proposals.

Suppliers – Low to Medium. The suppliers of standard processes (e.g.: casting, machining, plating) have very little power. Given the current state of the economy, they need to be very competitive to gain and /or maintain contracts. Those suppliers of products that use Top Secret Clearance processes are slightly better off; however, there continues to be multiple avenues of supply and therefore moderate power.

Industry Competitors – Low. The current suppliers have been partitioned according to their processes and the products. Optex Systems Holdings and Miller-Holzwarth, Inc. both compete for plastic periscope products whereas Optex Systems Holdings and Seiler Instrument & Manufacturing Co., Inc., have competed on the higher level products. In the last 12-18 months, we have begun to challenge Seiler in areas where they have long held the dominant role. For example, while the existing Howitzer contracts are at low margins, the new bids will be at a much higher margin now that we have proven we can produce the product.

The second model is a two by two matrix for Products and Customers.

This Product/Customer matrix sets forth our four basic approaches:

1) Sell existing products to existing customers.

2) Sell existing products to new customers.

3) Develop new products to meet the needs of our existing customers.

4) Develop new products to meet the needs of new customers.

The product categories described in the above matrix are associated with the product lines set forth below:

Name	Product Line
M137, M187, M119 Aiming Device	Howitzer Sighting Systems
Aiming Circle	Howitzer Sighting Systems
Periscopes	Laser Protected Plastic Periscopes
Collimators	Electronic Sighting Systems
Back Up Sights	Mechanical Sighting Systems
ICWS	Laser Protected Glass Periscopes

Those “new customers” listed (BAE and Textron) are producers of armored vehicles. Optex Systems Holdings has provided them quotations for Laser Protected Plastic Periscopes and Mechanical Sighting Systems. Both of these companies have previously purchased products from Optex Systems Holdings. “New Customers” listed (L3 and ITT) are potential customers for night vision products.

Operations Plan

Our Operations Plan can be broken down into three distinct areas, Material Management, Manufacturing Space Planning and Efficient Scales of Economy.

Materials Management –

The largest portion of our costs are materials. We have completed the following activities in order to demonstrate continuous improvement:

- Successful Completion of ISO9001:2008 Certification

- Weekly Cycle Counts on Inventory Items

- Weekly Material Review Board Meeting on non-moving piece parts

- Kanban kitting on products with consistent ship weekly ship quantities

- Daily review of Yields and Product Velocity

- Bill of Material Reviews prior to Work Order Release

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Future continuous improvement opportunities include installation and training of Shop Floor Control module within the ERP system and organizational efficiencies of common procurement techniques among buyers.

Manufacturing Space Planning –

We currently lease approximately 49,000 square feet of manufacturing space. Given the ample building opportunities along with competitive lease rates, the objective is to maintain building and building-related costs consistent with prior historical norms on a percentage of sales basis.

Consistent with the space planning, we will drive economies of scale to reduce support costs on a percentage of sales perspective. These cost reductions can then be either brought directly to the bottom line or used for business investment.

This process is driven by the use of six sigma techniques and process standardization. Initial activities in this area have been the success of 5S projects in several production areas which has lead to improved output and customer approval on the aesthetics of the work environment. In addition to the 5S projects, we have used the Define, Measure, Analyze, Improve, Control Problem Solving technique to identify bottlenecks within the process flow and improve product yields. These successful techniques can then be duplicated across the production floor and drive operational improvements.

Intellectual Property

We utilize several highly specialized and unique processes in the manufacture of our products. While we believe that these trade secrets have value, it is probable that our future success will depend primarily on the innovation, technical expertise, manufacturing and marketing abilities of our personnel. We cannot assure you that we will be able to maintain the confidentiality of our trade secrets or that our non-disclosure agreements will provide meaningful protection of our trade secrets, know-how or other proprietary information in the event of any unauthorized use, misappropriation or other disclosure. The confidentiality agreements that are designed to protect our trade secrets could be breached, and we might not have adequate remedies for the breach. Additionally, our trade secrets and proprietary know-how might otherwise become known or be independently discovered by others. We do not possess any patents.

Our competitors, many of which have substantially greater resources, may have applied for or obtained, or may in the future apply for and obtain, patents that will prevent, limit or interfere with our ability to make and sell some of our products. Although we believe that our products do not infringe on the patents or other proprietary rights of third parties, we cannot assure you that third parties will not assert infringement claims against us or that such claims will not be successful.

Competition

The markets for our products are competitive. We compete primarily on the basis of our ability to design and engineer products to meet performance specifications set by our customers. Our customers include the military and government end users as well as prime contractors that purchase component parts or subassemblies, which they incorporate into their end products. Product pricing, quality, customer support, experience, reputation and financial stability are also important competitive factors.

There are a limited number of competitors in each of the markets for the various types of products that we design, manufacture and sell. At this time we consider our primary competitors to be Seiler Instruments, Miller-Holzwarth, Kent Periscopes, and EO System Co.

Our competitors are often well entrenched, particularly in the defense markets. Some of these competitors have substantially greater resources than we do. While we believe that the quality of our technologies and product offerings provides us with a competitive advantage over certain manufacturers, some of our competitors have significantly more financial and other resources than we do to spend on the research and development of their technologies and for funding the construction and operation of commercial scale plants.

We expect our competitors to continue to improve the design and performance of their products. We cannot assure investors that our competitors will not develop enhancements to, or future generations of, competitive products that will offer superior price or performance features, or that new technology or processes will not emerge that render our products less competitive or obsolete. Increased competitive pressure could lead to lower prices for our products, thereby adversely affecting our business, financial condition and results of operations. Also, competitive pressures may force us to implement new technologies at a substantial cost, and we may not be able to successfully develop or expend the financial resources necessary to acquire new technology. We cannot assure you that we will be able to compete successfully in the future.

External Growth Potential/Roll-Up Opportunities

We operate in a business environment which is highly fragmented with numerous private companies, many of which were established more than 20 years ago. We believe there may be opportunities to pursue mergers with these competitors. We are not aware of any previous attempts to consolidate companies with our defense manufacturing expertise.

The typical company we compete with has 50-100 employees and annual revenue of $20-$50 million dollars. Most of these private companies have never had the opportunity to enjoy the benefits of consolidation and the resulting economies of scale associated with a larger entity.

We plan to engage our competition on a selective basis, and to explore all opportunities to grow our operations through mergers and/or acquisitions. We have no acquisition agreements pending at this time and are not currently in discussions or negotiations with any third parties.

Employees

Optex Systems Holdings has 107 full time equivalent employees. Optex Systems Holdings uses a small temporary work force to handle peak loads. The full time employee count is 101 and the temporary employee head count is 6. To the best of its knowledge, Optex Systems Holdings is compliant with local prevailing wage, contractor licensing and insurance regulations, and has good relations with its employees.

Forward-Looking Statements

This Current Report on Form 8-K contains forward-looking statements. To the extent that any statements made in this Current Report on Form 8-K contain information that is not historical, these statements are essentially forward-looking. Forward-looking statements can be identified by the use of words such as “expects,” “plans,” “will,” “may,” “anticipates,” believes,” “should,” “intends,” “estimates,” and other words of similar meaning. These statements are subject to risks and uncertainties that cannot be predicted or quantified and, consequently, actual results may differ materially from those expressed or implied by such forward-looking statements. Such risks and uncertainties are outlined in “Risk Factors” and include, without limitation, the Company’s ability to raise additional capital to finance the Company’s activities; the effectiveness, profitability, and the marketability of its products; legal and regulatory risks associated with the Reorganization ; the future trading of the common stock of the Company; the ability of the Company to operate as a public company; the period of time for which the proceeds of the Private Placement will enable the Company to fund its operations; the Company’s ability to protect its proprietary information; general economic and business conditions; the volatility of the Company’s operating results and financial condition; the Company’s ability to attract or retain qualified senior management personnel and research and development staff; and other risks detailed from time to time in the Company’s filings with the SEC, or otherwise.

Information regarding market and industry statistics contained in this Report is included based on information available to the Company that it believes is accurate. It is generally based on industry and other publications that are not produced for purposes of securities offerings or economic analysis. The Company has not reviewed or included data from all sources, and cannot assure investors of the accuracy or completeness of the data included in this Report. Forecasts and other forward-looking information obtained from these sources are subject to the same qualifications and the additional uncertainties accompanying any estimates of future market size, revenue and market acceptance of products and services. The Company does not undertake any obligation to publicly update any forward-looking statements. As a result, investors should not place undue reliance on these forward-looking statements.

Management's Discussion and Analysis or Plan of Operations

All references to the "Company," "we," "our" and "us" for periods prior to the closing of the Reorganization refer to Optex, and references to the "Company," "we," "our" and "us" for periods subsequent to the closing of the Reorganization refer to the Registrant and its subsidiaries.

The following discussion highlights the principal factors that have affected our financial condition and results of operations as well as our liquidity and capital resources for the periods described. This discussion contains forward-looking statements. Please see "Special cautionary statement concerning forward-looking statements" and "Risk factors" for a discussion of the uncertainties, risks and assumptions associated with these forward-looking statements. The operating results for the periods presented were not significantly affected by inflation.

Background

Management's Discussion and Analysis or Plan of Operations

This management's discussion and analysis reflects information known to management as at December 28, 2008. This MD&A is intended to supplement and complement our audited financial statements and notes thereto for the year ended September 28, 2008 (Predecessor), prepared in accordance with U.S. generally accepted accounting principles (GAAP). You are encouraged to review our financial statements in conjunction with your review of this MD&A. The financial information in this MD&A has been prepared in accordance with GAAP, unless otherwise indicated. In addition, we use non-GAAP financial measures as supplemental indicators of our operating performance and financial position. We use these non-GAAP financial measures internally for comparing actual results from one period to another, as well as for planning purposes. We will also report non-GAAP financial results as supplemental information, as we believe their use provides more insight into our performance. When non-GAAP measures are used in this MD&A, they are clearly identified as a non-GAAP measure and reconciled to the most closely corresponding GAAP measure.

The following discussion highlights the principal factors that have affected our financial condition and results of operations as well as our liquidity and capital resources for the periods described. This discussion contains forward-looking statements. Please see "Special cautionary statement concerning forward-looking statements" and "Risk factors" for a discussion of the uncertainties, risks and assumptions associated with these forward-looking statements. The operating results for the periods presented were not significantly affected by inflation.

Background

On March 30, 2009, the reorganization was consummated pursuant to which the then existing shareholders of Optex Systems, Inc. (Delaware) exchanged their shares of common stock with the shares of common stock of Optex Systems Holdings as follows: (i) the outstanding 85,000,000 shares of Optex Systems, Inc. (Delaware) common stock were exchanged by Optex Systems Holdings for 113,333,282 shares of Company common stock, (ii) the outstanding 1,027 shares of Optex Systems, Inc. (Delaware) Series A preferred stock were exchanged by Optex Systems Holdings for 1,027 shares of Company Series A preferred stock, and (iii) the 8,131,667 shares of Optex Systems, Inc. (Delaware) common stock purchased in the private placement were exchanged by Optex Systems Holdings for 8,131,667 shares of Company common stock. Optex Systems, Inc. (Delaware) has remained a wholly-owned subsidiary of Optex Systems Holdings.

As a result of the reorganization, Optex Systems Holdings changed its name from Sustut Exploration Inc. to Optex Systems Holdings, Inc. and its year end from December 31 to a fiscal year ending on the Sunday nearest September 30.

Immediately prior to the closing under the reorganization agreement (and the shares included above), as of March 30, 2009, Optex Systems, Inc. (Delaware) accepted subscriptions from accredited investors for a total 27.1 units, for $45,000 per unit, with each unit consisting of 300,000 shares of common stock, no par value, of Optex Systems, Inc. (Delaware) and warrants to purchase 300,000 shares of common stock for $0.45 per share for a period of five (5) years from the initial closing, which were issued by Optex Systems, Inc. (Delaware) after the closing referenced above. Gross proceeds to Optex Systems, Inc. (Delaware) were $1,219,750, and after deducting (i) a cash finder's fee of $139,555, (ii) non-cash consideration of indebtedness owed to an investor of $146,250, and (iii) stock issuance costs of $59,416, the net proceeds were $874,529. The finder also received five year warrants to purchase 2.39 units, at an exercise price of $49,500 per unit. As described above, these 8,131,667 shares were exchanged for 8,131,667 shares of Optex Systems Holdings common stock in the reorganization.

Optex Systems, Inc. (Delaware) manufactures optical sighting systems and assemblies primarily for Department of Defense applications. Its products are installed on a majority of types of U.S. military land vehicles, such as the Abrams and Bradley fighting vehicles, light armored and armored security vehicles and have been selected for installation on the Stryker family of vehicles. Optex Systems, Inc. (Delaware) also manufactures and delivers numerous periscope configurations, rifle and surveillance sights and night vision optical assemblies. Optex Systems, Inc. (Delaware) products consist primarily of build-to-customer print products that are delivered both directly to the armed services and to other defense prime contractors. Less than 1% of today's revenue is resale of products "substantially manufactured by others". In this case, the product would likely be a simple replacement part of a larger system previously produced by Optex Systems, Inc. (Delaware).

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Optex Systems, Inc. (Delaware) delivers high volume products, under multi-year contracts, to large defense contractors. It has the reputation and credibility with those customers as a strategic supplier. Irvine Sensors Corporation ("Irvine Sensors Corporation") is predominately a research and design company with capabilities enabling only prototype or low quantity volumes. Optex Systems, Inc. (Delaware) is predominately a high volume manufacturing company. Therefore the systems and processes needed to meet customer's needs are quite different. While both companies serve the military market, the customers within these markets are different. For example, two of the largest customers for Optex are GDLS and TACOM. Irvine Sensors Corporation did not have any contracts or business relations with either of these two customers. Therefore the separation has allowed Optex Systems, Inc. (Delaware) to fully focus on high volume manufacturing and the use of the six sigma manufacturing methodology. This shift in priorities has allowed Optex Systems, Inc. (Delaware) to improve delivery performance and reduce operational costs.

Many of our contracts allow for government contract financing in the form of contract progress payments pursuant to Federal Acquisition Regulation 52.232-16. "Progress Payments". As a small business, and subject to certain limitations, this clause provides for government payment of up to 90% of incurred program costs prior to product delivery. To the extent our contracts allow for progress payments, we intend to utilize this benefit, thereby minimizing the working capital impact on Optex Systems Holdings for materials and labor required to complete the contracts.

Optex Systems Holdings also anticipates the opportunity to integrate some of its night vision and optical sights products into commercial applications. Optex Systems Holdings plans to carry on the business of Optex Systems, Inc. (Delaware) as its sole line of business, and all of Optex Systems Holdings' operations are expected to be conducted by and through Optex Systems, Inc. (Delaware).

The successful completion of the separation from Irvine Sensors Corporation, which was accomplished by Optex Systems, Inc. (Delaware)'s acquisition of all of the assets and assumption of certain liabilities of Optex Systems, Inc. (Texas), reduced the general and administrative costs allocated by Irvine Sensors Corporation. These costs represented services paid by Irvine Sensors Corporation for expenses incurred on Optex Systems, Inc. (Texas)' behalf such as legal, accounting and audit, consulting fees and insurance costs in addition to significant amounts of Irvine Sensors Corporation's general overhead allocated to Optex Systems, Inc. (Texas).

The estimated total General and Administrative expenses assuming Optex Systems, Inc (Texas) was operated under a stand-alone basis during the 2008 fiscal year are:

Accounting and Auditing Fees	$ 250,000
Legal Fees	60,000
Consulting Fees	60,000
Workers Comp and General Insurance	70,000
Total	$ 440,000

As a result of the purchase of Optex Systems, Inc. (Texas) on October 14, 2008, these general and administrative costs are incurred and paid directly by Optex Systems, Inc. (Delaware) for the 2009 fiscal year, and have been reflected in the financial statements to the extent incurred through December 28, 2008.

The liabilities not assumed relate to costs that would not have been incurred by Optex Systems, Inc. (Texas) if they were operated on a stand alone basis, including a note due to Timothy Looney. The 2007 promissory note had a principal amount of $2,000,000 together with accrued interest unpaid aggregating to approximately $2,300,000. The note was an amendment to Looney's earn-out agreement which was the consideration for Irvine Sensor's purchase of Optex Systems, Inc. (Texas).

The 2007 promissory note was not assumed by Optex Systems, Inc. (Delaware) in the October 2008 transaction. The note and accrued interest was reported on Optex Systems, Inc. (Texas) financial statements as of September 28, 2008 as a result of push down accounting for the acquisition of Optex Systems, Inc. (Texas) by Irvine Sensors. The note would not have been incurred by Optex Systems, Inc. (Texas) if operated as a stand alone entity because it relates to Irvine Sensor's consideration for its purchase of Optex Systems, Inc. (Texas). Therefore, we expect no similar impact to the future operating results or liquidity of the Company.

Additionally, as of September 28, 2008, Optex Systems, Inc. (Texas) reported $4.3 million of liabilities attributable to corporate expenses allocated to Optex Systems, Inc. (Texas) through an intercompany payable. The outstanding intercompany payable was not acquired by the company in the acquisition from Irvine Sensors.

Plan of Operation

Through a private placement offering completed prior to consummation of the reorganization agreement, Optex Systems, Inc. (Delaware) raised $1,219,750 ($874,529, net of finders fees, issuance costs and non cash consideration resulting from satisfaction of indebtedness owed to an investor) to fund operations. The proceeds have been used as follows:

Description	Offering
Additional Personnel	$ 150,000
Legal and Accounting Fees	$ 100,000
Investor Relations Fees	96,000
Working Capital	$ 528,529
Totals	$ 874,529

Results of Operations

Based on the current level of deliverable backlog, we expect the next three months' revenues to be consistent with the total for the periods September 29, 2008 through October 14, 2008 (Predecessor) and October 15, 2008 through December 28, 2008 (Successor). In addition, future business includes expected awards yet to be determined. Although the current range of products being manufactured is dependent on the receipt of continued and timely funding to existing programs, the most recent proposed federal budget is not expected to impact any of our existing programs in the near term.

The Revenue, Expenses and Income for the fourteen day period of Optex Systems, Inc. (Texas) prior to the acquisition by Optex Systems, Inc. (Delaware) are summarized below (in millions).

Optex Systems Inc. (Texas) (Predecessor)	
Revenue	$ 0.9
Cost of Sales	0.7
Gross Margin	0.2
General & Administrative	0.1

Operating Income	$	0.1
Net Income	$	0.1

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The table below summarizes our quarterly and year to date operating results in terms of both a GAAP net income measure and a non GAAP EBITDA measure. We use EBITDA as an additional measure for evaluating the performance of our business as "net income" includes the significant impact of noncash Intangible Amortization on our income performance. Consequently, in order to have a meaningful measure of our operating performance on a continuing basis, we need to evaluate an income measure which does not take into account this Intangible Amortization. We have summarized the quarterly revenue and margin below along with a reconciliation of the GAAP net loss to the non GAAP EBITDA calculation for comparative purposes below. We believe that including both measures allows the reader to have a "complete picture" of our overall performance.

	Predecessor - Fiscal Year 2008			
	Predecessor - Qtr 1 (Sept 29, 2008 through Oct 14, 2008)	Successor- Qtr 1 (Oct 15, 2008 through Dec 28, 2008)	3 months ended December 28, 2008	3 months ended December 30, 2007
Net Loss After Taxes - GAAP	$ (0.1)	$ 0.1	$ (0.0)	$ (0.7)
Add:				
Interest Expense		$ 0.1	$ 0.1	$ 0.1
Federal Income Taxes		0.2	0.2	-
Depreciation & Amortization		0.6	0.6	0.3
EBITDA - Non GAAP	$ (0.1)	$ 1.0	$ 0.9	$ (0.3)

We have experienced substantial improvement in our EBITDA as compared to our prior year performance. We have increased our EBITDA by $1.2 million in the three months ending December 28, 2008 as compared to the three months ending December 30, 2007 (Predecessor), primarily as a result of increased revenue and lower general and administrative costs. We expect this trend to continue over the next 12 months as our product mix shifts towards more profitable programs and we continue to pursue cost reductions in our production and general and administrative areas.

Product mix is dictated by customer contracted delivery dates and volume of each product to be delivered on such delivery dates. Shifts in gross margin from quarter to quarter are primarily attributable to the differing product mix recognized as revenues during each respective period. During the three months ended December 28, 2008, our revenues on legacy periscope programs increased significantly over the prior year. The legacy periscope contracts were awarded January 2003, and due to significant material price increases subsequent to the contract award date, we are experiencing a loss on these contracts. We have fully reserved for future contract losses on this program, thus deliveries against these programs yield a product margin of zero. During the first three months of fiscal year 2008, we recognized revenue of $1.5 million from these legacy periscope programs, with a remaining backlog of $5.1 million, $3.9 million of which should be recognized in fiscal year 2009 and the remaining $1.2 million in the first three quarters of fiscal year 2010. We expect our product margins on all periscopes to increase over the next 12 months as the legacy programs are completed and are replaced with new awards.

We are aggressively pursuing additional, potentially higher margin periscope business, and in May 2009, Optex Systems Holdings was awarded a multi-year Indefinite Delivery/Indefinite Quantity type contract accompanied by the first delivery order from TACOM. If all government forecasted delivery orders against this Indefinite Delivery/Indefinite Quantity contract are awarded and if we were to share equally with the other supplier in the awarded releases, the total value of the contract to us could be valued at approximately $7.5 million over the next three years. In June 2009, we received an additional $3.4 million dollar award from GDLS and in September 2009, an additional $1.9 million award to provide product beginning with delivery starting in 2011 at the completion of our current production contract.

As a result of the October 14, 2008 acquisition of the assets of Optex Systems, Inc. (Texas) (Predecessor), our amortizable intangible assets increased significantly over the prior year. The non cash amortization of intangible assets will have a negative impact on our Gross Margin for 2009 as compared to 2008. In fiscal 2009, intangible amortization expense will be $2 million and is scheduled to decline significantly to $1 million in fiscal 2010.

Backlog as of December 28, 2008 was $30.9 million as compared to a backlog of $44.2 million as of December 30, 2007. The following table depicts the current expected delivery by quarter of all contracts awarded as of March 30, 2009.

	2009			2010				2011				2012				2013
Program Backlog (000's)	Qtr 2	Qtr 3	Qtr 4	Qtr 1	Qtr 2	Qtr 3	Qtr 4	Qtr 1	Qtr 2	Qtr 3	Qtr 4	Qtr 1	Qtr 2	Qtr 3	Qtr 4	Qtr 1
Howitzer Programs	$ 0.2	$ 1.0	$ 0.8	$ 0.6	$ 1.7	$ 1.9	$ 2.6	$ 1.7	$ 0.1	-	-	-	-	-	-	-
Periscope Programs	4.4	2.6	2.1	1.9	2.0	2.5	1.5	0.5	0.3	0.2	-	-	0.1	0.1	-	-
Sighting Systems	0.6	1.3	1.0	0.6	-	-	-	-	-	-	-	-	-	-	-	-
All Other	0.6	2.3	1.4	0.6	0.5	0.4	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Total	$ 5.8	$ 7.2	$ 5.3	$ 3.7	$ 4.2	$ 4.8	$ 4.2	$ 2.3	$ 0.5	$ 0.3	$ 0.1	$ 0.1	$ 0.2	$ 0.2	$ 0.1	$ 0.1

Virtually all of our contracts are prime or subcontracted directly with the Federal government and, as such, are subject to Federal Acquisition Regulation Subpart 49.5, "Contract Termination Clauses" and more specifically Federal Acquisition Regulation clauses 52.249-2 "Termination for Convenience of the Government Fixed-Price)", and 49.504 "Termination of fixed-price contracts for default". These clauses are standard clauses on our prime military contracts and generally apply to us as subcontractors. It has been our experience that the termination for convenience is rarely invoked, except where it is mutually beneficial for both parties. We are currently not aware of any pending terminations for convenience or for default on our existing contracts.

By way of background, Federal Acquisition Regulation is the principal set of regulations that govern the acquisition process of government agencies and contracts with the U.S. government. In general, parts of the Federal Acquisition Regulation are incorporated into government solicitations and contracts by reference as terms and conditions effecting contract awards and pricing solicitations.

In the event a termination for convenience were to occur, these Federal Acquisition Regulation clause 52.249-2 provides for full recovery of all contractual costs and profits reasonably occurred up to and as a result of the terminated contract. In the event a termination for default were to occur, we could be liable for any excess cost incurred by the government to acquire supplies from another supplier similar to those terminated from us. We would not be liable for any excess costs if the failure to perform the contract arises from causes beyond the control and without the fault or negligence of the company as defined by Federal Acquisition Regulation clause 52.249-8. In addition, the Government may require us to transfer title and deliver to the Government any completed supplies, partially completed supplies and materials, parts, tools, dies, jigs, fixtures, plans, drawings, information, and contract rights that we have specifically produced or acquired for the terminated portion of this contract. The Government shall pay contract price for completed supplies delivered and accepted, and we and the Government would negotiate an agreed upon amount of payment for manufacturing materials delivered and accepted and for the protection and preservation of the property. Failure to agree on an amount for manufacturing materials is subject to the Federal Acquisition Regulation Disputes clause 52.233-1.

In some cases, we may receive an "undefinitized" (i.e., price, specifications and terms are not agreed upon before performance commenced) contract award for contracts that exceed the $650,000, which is the federal government simplified acquisition threshold. These contracts are considered firm contracts at an undefinitized, but not to exceed specified limits threshold. Cost Accounting Standards Board covered contracts are subject to the Truth in Negotiations Act disclosure requirements and downward only price negotiation. As of December 28, 2008, 16.6% of our outstanding backlog, or $5.0 million of booked orders, fell under this criterion. Our experience has been that the historically negotiated price differentials have been minimal (5% or less) and accordingly, we do not anticipate any significant downward adjustments on these booked orders.

Predecessor period of September 29, 2008 through October 14, 2008 and Successor period of October 15, 2008 through December 28, 2008 compared to the Predecessor three month period ended December 30, 2007.

Revenues: For the three months ended December 28, 2009 (Combined) revenues increased by 63.6% over the respective prior period (Predecessor) per the table below:

	Predecessor September 29, 2008 through October 14, 2008	Successor October 15, 2008 through December 28, 2008	Combined 3 mos. ended December 28, 2008	Predecessor 3 mos. ended December 30, 2007	Change
Revenue	$ 0.9	$ 6.4	$ 7.3	$ 4.4	$ 2.9
Percent increase					65.9%

The table below details the revenue changes by product line in the three months ended December 28, 2008.

Product Line	3 mos ended December 28, 2008 (Combined)	3 mos ended December 30, 2007 (Predecessor)	Change
Howitzer Programs	0.5	0.3	(0.2)
Periscope Programs	4.8	1.8	3.0
Sighting Systems	1.0	1.6	(0.6)
All Other	1.0	0.7	0.3
Total	7.3	4.4	2.9
Percent increase			65.9%

Revenues increased $3.0 million in periscopes during the three months ended December 28, 2008 as compared to the three months ended December 30, 2007. The significant increase in periscope sales is attributable to increased demand by GDLS and U.S. government accelerated schedules, whereby, in consideration for increased pricing of approximately $1.0 million, Optex Systems, Inc. (Delaware) agreed to accelerate the contract delivery schedule and deliver at higher volumes to support increased military service needs. Of the total periscope revenue increase, approximately 82% is attributable to increased product levels, as compared to 18% due to accelerated pricing. The ramp up included the addition direct labor headcount of approximately 8 employees, combined with dual sourcing of material on several key components needed to meet the increased production requirements. During the first three months of fiscal 2009, Optex had delivered approximately 23% of the accelerated units, with the remaining units to be delivered through the first quarter of 2010. Based on our current backlog demand, we expect the periscope revenues to decline after the first fiscal quarter of 2009 as the accelerated orders near completion; however we expect the revenue on periscopes to remain strong in 2010 as we continue to quote and receive awards for additional periscopes from multiple customers.

Revenues in the Howitzer programs declined slightly by ($0.2) million over the same period in the prior year due to technical issues experienced on the Howitzer product lines related to problems with the government technical data and drawing package affecting the manufacturability of the products and the functionality of the product during field use and testing. These issues were resolved subsequent to the second fiscal quarter of 2009 through Optex initiated engineering change proposals and customer changes to the statement of work and contract schedules modified accordingly to implement the required changes. With most of the technical and start up issues behind us on these programs, we expect to increase program deliveries on these programs starting with the third and fourth fiscal quarters of fiscal year 2009 continuing through 2010.

Sighting Systems revenues decreased ($0.6) million over the prior year due to the wind down and completion of a substantial Textron and Raytheon related M36 programs in 2008. There has been no follow on award to the programs subsequent to the program completion in April 2008.

Increases in the other products $0.3 million for the three months ending December 28, 2008 are a result of increased business in muzzle reference sensor assemblies from GDLS.

Currently we are experiencing losses on our Howitzer programs as a result of unanticipated manufacturing costs due to design and technical data package issues impacting the product manufacturability. These issues have resulted in increased labor and material costs due to higher scrap and extensive engineering costs incurred during the start up phase of the programs. In addition some of our older “legacy” periscope programs are experiencing losses due to significant material price increases since the initial 5 year contract award in 2004. As of December 28, 2008 Optex Systems Holdings has reserved $0.6 million in contract loss reserves on Howitzer programs and $0.1 million on periscope programs for a total of $0.7 million in contract loss reserves. The total remaining backlog on these loss programs as of December 28, 2008 is $15.7 million. We are expecting to ship $9.4 of the loss contract backlog in the remaining quarters of fiscal year 2009 and $4.5 million of the existing loss contract backlog in 2010, with the remaining $1.8 million expected to ship in the first quarter of 2011. As these losses have been previously recognized to the extent identified, future margins on these revenues are expected to be zero.

Currently we are not experiencing any negative impact due to changes in incremental funding commitments by federal agencies. There has been one delay in the award of the second delivery order for the U.S. government periscope contract subsequent to December 28, 2008, however as the contract is a dual award between Optex Systems Holdings and a competitor with no volume guaranteed to any single-source, we have not expended any resources in support of the yet to be awarded portion of the contract. We are anticipating a government award on the contract in the second quarter of 2010. However, delay of the government procurement is not expected to negatively impacted Optex Systems Holdings’ revenue in 2009, and due to other increased periscope orders from non U.S. government contracts further delays in the award on the prime government contract should not materially affect Optex Systems Holdings in the next 12 months.

Cost of Goods Sold. During the Predecessor period from September 29, 2008 through October 14, 2008, we recorded cost of goods sold of $0.7 million and during the Successor period from October 15 through December 28, 2008 we recorded cost of goods sold of $5.6 million for a total cost of goods sold during the three month period of $6.3 million as compared, to $3.8 million during the three months ended December 30, 2007, an increase of $2.5 million or 65.8%. This increase in cost of goods sold was primarily associated with increased revenue on our periscope product lines in support of higher backlog and accelerated delivery schedules and increased intangible amortization resulting from the acquisition of the assets of Optex Systems, Inc. (Texas) (Predecessor) on October 14, 2008. The gross margin during the Predecessor period beginning September 29, 2008 through October 14, 2008 was $0.1 million and the gross margin for the Successor period beginning October 15, 2008 through December 28, 2008 was $0.9 million for a total of $1.0 million or 13.7% of revenues as compared to a gross margin of $0.6 or 13.6% for the three months ended December 30, 2007. Product gross margins were up 0.5% to 20.1% for the three months ended December 28, 2008 versus 19.6% for the three months ended December 30, 2007 due to a shift in revenue mix toward more profitable periscopes programs in 2009 and completion of a less profitable sighting system in 2008. Cost of goods sold was also impacted by higher intangible amortization of $0.2 million, or 6.4% of revenues, in the period ended December 28, 2008 as compared to the three months ended December 30, 2007.

G&A Expenses. During the Predecessor period from September 29, 2008 through October 14, 2008 we recorded operating expense of $0.1 million and during the period from October 15, 2008 through December 28, 2008, we recorded operating expenses of $0.5 million for a total of $0.6 million for the three months ended December 30, 2008 as opposed to $1.2 million during the three months ended December 30, 2007, a decrease of $0.6 million or

50.0%. The components of the significant net decrease in general and administrative expenses as compared to the three months ended December 30, 2007 are outlined below.

- Elimination of corporate cost allocations from Irvine Sensors Corporation of $0.4 million and the Irvine Sensors Corporation Employee Stock Bonus Plan of $0.1 million as a result of the ownership change.
- Increased Amortization of Intangible Assets of $0.04 million as a result of the ownership change as of October 14, 2008.
- Decreased consulting and travel expenses of $0.04 million, primarily a result of the change in ownership.

Income (Loss) from Operations. During the Predecessor period from September 29, 2008 through October 14, 2008 we recorded income from operations of $0.1 million and for the Successor period from October 15, 2008 through December 28, 2008, we recorded income from operations of $0.2 million for a total operating income of $0.3 million during the three month period as opposed to a loss from operations of $(0.6) million during the three months ended December 30, 2007. This improvement was primarily due to increased sales revenue in the period ended December 28, 2008, combined with reduced general and administrative expenses driven by the elimination of Irvine Sensors Corporation corporate costs pushed down to us in the three months ended December 28, 2008. The current year loss from operations also includes $0.5 million of non cash amortization of intangible assets as a result of the October 14, 2008 acquisition transaction.

Net Income (Loss). During the Predecessor period from September 29, 2008 through October 14, 2008 we recorded net income of $0.07 million, and for the period beginning October 15, 2008 through December 28, 2008, we recorded a net loss of $(0.1) million for a total net loss of $(.03) million during the three months ended December 28, 2008, as compared to $(0.7) million for three months ended December 30, 2007, a decrease in net loss of $0.7 million or 97.1%. This decrease in net loss was principally the result of reduced operating expenses related to the elimination of corporate cost allocations from Irvine Sensors Corporation since the successor operating as a stand-alone entity did not incur these costs in the three months ended December 28, 2008 combined with increased revenue in the period ending December 28, 2008. Federal Income Tax expense increased by $0.3 million over the prior year period as a result of the increased profit before intangible amortization expense. The intangible amortization expense is amortized over five years for book purposes and is deductible over 15 years for income tax purposes. In 2008, there was no Federal Income Tax expense due to the loss from operations. Excluding the impact of the increased intangible expenses of $0.47 million, we would have recorded net income of $0.5 million for the three month period ending December 28, 2008.

Year Ended September 28, 2008 (Predecessor) Compared to Year Ended September 30, 2007 (Predecessor)

For the year ended September 28, 2008 revenues increased by 29.9% over the respective prior year per the table below:

	12 mos ended 9/28/2008	12 mos ended 9/30/2007	Change
Howitzer Programs	2.4	-	2.4
Periscope Programs	9.6	7.3	2.3
Sighting Systems	4.0	5.8	(1.8)
All Other	4.0	2.3	1.7
Total	20.0	15.4	4.6
Percent increase			29.9%

Revenues increased 29.9% or $4.6 million in the year ended September 28, 2008 from the prior year due to reaching full production on the M137 Howitzer program, $1.7 million combined with additional revenue of $0.7 million due to an equitable adjustment for start up costs on the M187 Howitzer program. In March 2008, The Department of the Army, TACOM-Rock Island awarded Optex Systems an equitable adjustment contract modification in support of the M187 Howitzer program. The equitable price adjustment had been requested by Optex Systems due to significant non-recurring incurred costs related to the start up on the program associated with deficiencies in the government provided design and technical data package provided during the original contract negotiation and award. These deficiencies caused significant cost overruns in materials, labor and other direct contract costs as a result of higher scrap, obsolete inventories, increased engineering effort, production delays and unabsorbed overhead costs incurred in 2007 and early 2008. The equitable adjustment totaled $1.6 million and was split between recovery of Optex program to date expended costs of $0.7 million and future price increases of $0.8 million. During the quarter ended March 30, 2008, Optex recognized $0.7 million in revenues directly attributable to the non recurring portion of the equitable adjustment for costs incurred thru March 2008, with the remaining $0.9 million adjustment to be recognized as a unit price increase on deliveries through 2010.

Periscope revenues increased $2.3 million due to increased production to meet higher delivery schedules from the U.S. Government and GDLS. Sighting system revenues declined $1.8 million due to completion of one of our major system contracts in the second quarter of 2008. Other products increased $1.7 million due to significantly increased revenues of Navy binoculars $0.8 million and increased deliveries for assorted optical spare parts and assemblies $0.9 million over the prior year.

Cost of Goods Sold. During the year ended September 28, 2008, we recorded cost of goods sold of $18.1 million as opposed to $17.4 million during the year ended September 30, 2007, an increase of $0.7 million or 4.5%. This increase in cost of goods sold was primarily due to increased revenues of $4.6 million. The margins on the increased revenue is significantly improved over the year ended September 30, 2007 due to equitable price adjustments and accelerated schedule consideration received in the year ended September 2008 on certain programs. Additionally, the gross margin for the year ended September 30, 2007 included significant contract loss reserves, excess and obsolescence and other non recurring inventory adjustments related to unrecoverable costs increases on fixed price contracts.

G&A Expenses. General and Administrative expenses were $5.0 million in the year ended 2008 versus $4.9 million in the year ended 2007, an increase $0.1 million or 2.0%. The significant components of the net increase are outlined below.

- Decrease in legal and accounting fees of $0.2 million as a result of reduced auditing expenses related to 2008 annual physical inventory and higher legal expenses in 2007 related to securing a $2 million note from Tim Looney.
- Salaries and wages and employee related costs changed by $0.0 in the year ended 2008 versus the year ended 2007. Salaries increased 4%, or $0.03 million in the year ended September 28, 2008 as compared to the year ended September 30, 2007. This increase was primarily due to personnel changes combined with annual salary and wage increases of approximately 3%. Employee benefits declined by 15% or $(0.03) million in the year ended September 28, 2008 due to personnel changes at the end of 2007 whereas two key executive employees received all accrued vacation as of their departure at the end September 2007.
- Consulting and contract service fees increased by $0.1 million in 2008 over 2007 due to services used in support of attaining ISO 9000 certification in 2008, in addition to executive services charged to Optex Systems Inc., (Texas) by Irvine Sensors Corporation for organizational oversight until replacements were secured for executives leaving Optex as of September 30, 2007.

Loss from Operations. During the year ended September 28, 2008, we recorded a loss of $(3.1) million as opposed to $(6.8) million during the year ended September 30, 2007, a decrease of $3.7 million or 54.4%. This decrease in the loss from operations was primarily due to the negotiation of several equitable price adjustments and other consideration on accelerated delivery schedules in the year ended September 28, 2008. Additionally, for the year ended September 30, 2007, non-recoverable cost increases on fixed price contracts resulted in significant contract loss and excess and obsolete inventory reserves as discussed above in cost of goods sold. These losses were partially offset in 2008 with equitable price adjustments negotiated with the customer.

Net Loss. During the year ended September 28, 2008, we recorded a net loss of $(4.8) million, as compared to $(6.8) million for year ended September 30, 2007, an improvement of $2.0 million or 29.4%. This decrease in net loss was principally the result of increased revenues and negotiated equitable and other price adjustments discussed above, partially offset by a $1.6 million adjustment for the impairment of goodwill, Goodwill was reviewed as of September 28, 2008 and adjusted based upon the most recent value of the company as determined by the sale to third party purchasers on October 14, 2008.

Liquidity and Capital Resources

In the year ended 2008, Optex Systems, Inc. (Texas) working capital was significantly constrained due a high level of loss programs and production increases across multiple programs which necessitated the need for investment in inventories and manpower resources required to meet the additional product demand. As Optex Systems, Inc. (Texas) was a wholly-owned subsidiary of Irvine Sensors Corporation, access to additional outside funding apart from government progress bills was severely limited. Further, Optex Systems, Inc. (Texas) had incurred significant costs on one of the Howitzer programs and was unable to recover these costs until fiscal 2009 due to progress billing limitations prior to first article inspection testing and approval which did not occur until August of 2009. During 2008, Optex Systems, Inc. (Texas) transferred $0.7 million in cash to Irvine Sensors in support of intercompany services provided by Irvine Sensors on behalf of Optex Systems, Inc. (Texas) that were outside our control, including: legal, accounting, and consulting fees; Irvine Sensors Corporation travel expenses; and insurance costs.

The estimated total General and Administrative expenses assuming Optex Systems, Inc. (Texas) was operated on a stand-alone basis during the 2008 fiscal year are:

	Year- Ended September 28, 2008
Accounting & Auditing Fees	$ 250,000
Legal Fees	60,000
Consulting Fees	60,000
Workers Comp & General Insurance	70,000
Total	$ 440,000

As a result of the purchase of Optex Systems, Inc. (Texas) on October 14, 2008, these general and administrative costs are incurred and paid directly by Optex Systems, Inc. (Delaware) for the 2009 fiscal year and have been reflected in the financial statements to the extent incurred through December 28, 2008.

Subsequent to the asset acquisition from Irvine Sensors on October 14, 2008 and the reverse merger and reorganization on March 30, 2009, Optex Systems Holdings has raised additional cash through a private equity sale that generated gross proceeds of $1.0 million. As a result of the new capital, Optex Systems Holdings will be able acquire the necessary inventory and personnel resources required to operate at the higher revenue levels, and improve the company’s working capital position.

We have historically met our liquidity requirements from a variety of sources, including government and customer funding through contract progress bills, short term loans, notes from related parties, and the sale of equity securities. Based upon our current working capital position and potential for expanded business revenues, we believe that our working capital is sufficient to fund our current operations for the next 12 months. However, based on our strategy and the anticipated growth in our business, we believe that our liquidity needs may increase in the future. The amount of such increase will depend on many factors, including the costs associated with the fulfillment of our projects, whether we upgrade our technology, and the amount of inventory required for our expanding business. If our liquidity needs do increase, we believe additional capital resources will be derived from a variety of sources including, but not limited to, cash flow from operations and further private placements of our common stock and/or debt, including receivables funding through a commercial lender.

Predecessor period of September 29, 2008 through October 14, 2008

Cash and Cash Equivalents. As of October 14, 2008, Optex Systems, Inc. (Texas) (Predecessor) had cash and cash equivalents of $0.3 million, an increase of $0.1 million from September 29, 2008. The slight increase in cash was primarily due to the timing of cash receipts on accounts receivable collections and supplier payments. The cash balance as of October 14, 2008 is included as “Cash Received through Optex Systems, Inc. (Texas) acquisition” as of October 15, 2008.

Net Cash Provided by Operating Activities. Net cash provided by operating activities totaled $0.1 million for the Predecessor period of September 29, 2008 through October 14, 2008. Cash provided by operating activities was primarily due to the timing of purchases and accounts receivable collections during the 15 day period prior to the acquisition of Optex Systems Inc, (Texas), by Optex Systems Inc., (Delaware). During this period, our net inventory increased by $0.9 million to support substantially increased production rates across all of our product lines and our accounts receivable decreased $(1.0) million due to timing of collections from one of our major customers in the second week of October 2008. Accounts payable and accrued expenses decreased by $(0.2) million due to the timing of cash disbursements prior to the acquisition.

Net Cash Used in Investing Activities. There was no net cash used in investing activities during the Predecessor period beginning September 29, 2008 and ending October 14, 2008. Optex Systems Holdings’ business is labor intensive and we purchase equipment as it becomes necessary.

Net Cash Provided by Financing Activities. There was no net cash provided by financing activities during the Predecessor period beginning September 29, 2008 and ending October 14, 2008.

Successor period of October 15, 2008 through December 28, 2008

Cash and Cash Equivalents. As of December 28, 2008, we had cash and cash equivalents of $0.5 million. During the Successor period of October 15, 2008 through December 28, 2008 we increased cash and cash equivalents by $0.2 million above the $0.3 million of cash received through the Optex Systems, Inc. (Texas) acquisition primarily due to timing of cash disbursements for accounts payable subsequent to the asset acquisition.

Net Cash (Used) Provided by Operating Activities. Net cash provided by operating activities during the Successor period beginning October 15, 2008 and ending December 28, 2009 totaled $0.4 million. The primary sources of cash during this period relate to the timing of purchases, accelerated collections on government contracts, and the timing of payments to vendors. Accelerated collections of government contracts was accomplished by offering nominal discounts for prompt payment. Federal Acquisition Regulation Clause 52.232-8 “Discounts for Prompt Payment” permits the offer of nominal discounts on payment terms for government contracts in order to expedite invoice payment. Because many of our programs incur significant, long lead times from material acquisition through production and shipment, it is the standard policy of Optex Systems, Inc. (Delaware) to offer a 0.5% discount for all government invoices paid in net 10 days or less. The normal payment terms on these contracts are net 30. The foregone revenues as a result of the discounted payments equate to less than 0.1% of total revenue reported during the same period. In the period beginning October 15, 2008 and ending December 28, 2008, our net inventory increased by $0.5 million to support substantially increased production rates across all of our product lines. A large portion of these inventories are progress billable costs and as such were billed to our customer as costs were incurred. As of December 28, 2008, our accounts receivable included approximately $0.6 million in unpaid outstanding progress bills related to these programs, which were paid in January 2009. We expect similar cash flows from operations until at least mid 2010 when our low margin legacy periscope programs are anticipated to end and are replaced with other significant programs as they reach level production rates.

Net Cash Provided by Investing Activities. In the Successor period beginning October 15, 2008 and ending December 28, 2008, net cash provided by investing activities totaled $0.24 million and consisted of cash acquired during the Optex Systems, Inc. (Delaware) Predecessor acquisition as of October 14, 2009 of $0.25 million and cash used to purchase equipment of $(0.01) million during the period.

Net Cash Used By Financing Activities. Net cash used by financing activities totaled $0.1 million during the period beginning October 15, 2008 through December 28, 2008, The change of $0.1 million is due to payments against an outstanding loan payable balance.

For the 12 months ended September 28, 2008 (Predecessor)

Cash and Cash Equivalents. As of September 28, 2008, the Predecessor had cash and cash equivalents of $0.2 million compared to $0.5 million in 2007. The decrease in cash and cash equivalents was primarily due to the timing of payments to suppliers against the open accounts payable balance versus collections of open accounts receivable balances as of year end.

Net Cash Used in Operating Activities. For the year ended September 28, 2008, the Predecessor used $0.6 million of net cash in operating activities, as compared to using $1.5 million of net cash in operating activities during 2007. The primary change was the timing of purchases, accelerated collections on government contracts, and the timing of payments to vendors. In the twelve months ending September, 28, 2008, the Predecessor's net inventory decreased by $1.7 million due to higher shipments in 2008 of inventories on hand as of the end of 2007. Accounts receivable declined by $0.4 million in 2008 primarily due to aggressive non US government collections and accelerated collections on government contracts. The accelerated collections of government contracts was accomplished by offering nominal discounts for prompt payment. Federal Acquisition Regulation Clause 52.232-8 "Discounts for Prompt Payment" permits the offer of nominal discounts on payment terms for government contracts in order to expedite invoice payment. Because many of our programs incur significant, long lead times from material acquisition through production and shipment, it is the standard policy to offer a 0.5% discount for all government invoices paid in net 10 days or less. The normal pay terms on these contracts is net 30. The foregone revenues as a result of the discounted payments equate to less than 0.1% of total revenue reported during the same period. Due to the increased revenues and collections, combined with reductions in inventory, the Predecessor was able to decrease the outstanding accounts payable and accrued expense balances by 30% or $1.1 million during 2008.

Net Cash Used in Investing Activities. Net cash used in investing activities totaled $0.1 million during the 12 months ended September 28, 2008, as compared to net cash used in investing activities of $0.06 million during the 12 months ended September 30, 2007 and consisted of equipment purchases. Optex Systems Holdings' business is labor intensive and the Predecessor purchased equipment as it became necessary.

Net Cash Provided By Financing Activities. Net cash provided by financing activities totaled $0.4 million during the 12 months ended September 28, 2008, as compared to net cash provided by financing activities of $2.0 million during the 12 months ended September 30, 2007. The Predecessor raised funds for working capital needs through short-term loans.

Critical Policies and Accounting Pronouncements

Stock-Based Compensation: In December 2004, the Financial Accounting Standards Board ("FASB") issued SFAS No. 123R, Share-Based Payment. SFAS No. 123R establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services. It also addresses transactions in which an entity incurs liabilities in exchange for goods or services that are based on the fair value of the entity's equity instruments or that may be settled by the issuance of those equity instruments. SFAS No. 123R focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions. SFAS No. 123R requires that the compensation cost relating to share-based payment transactions be recognized in the financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued.

The Company's accounting policy for equity instruments issued to consultants and vendors in exchange for goods and services follows the provisions of EITF 96-18, "Accounting for Equity Instruments That are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services" and EITF 00-18, "Accounting Recognition for Certain Transactions Involving Equity Instruments Granted to Other Than Employees." The measurement date for the fair value of the equity instruments issued is determined at the earlier of (i) the date at which a commitment for performance by the consultant or vendor is reached or (ii) the date at which the consultant or vendor's performance is complete. In the case of equity instruments issued to consultants, the fair value of the equity instrument is recognized over the term of the consulting agreement. Stock-based compensation related to non-employees is accounted for based on the fair value of the related stock or options or the fair value of the services, which ever is more readily determinable in accordance with SFAS 123R.

Revenue Recognition. The Company recognizes revenue based on the modified percentage of completion method utilizing the units-of-delivery method, in accordance with SOP 81-1:

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

Our contracts are fixed price production type contracts whereas a defined order quantity is delivered to the customer in a continuous or sequential production process in accordance with buyer specifications (build to print). Our deliveries against these contracts generally occur in monthly increments across fixed delivery periods spanning from 3 to 36 months.

Warranty Costs: Some of our customers require that we warranty the quality of our products to meet customer requirements and be free of defects for up to fifteen months subsequent to delivery. On certain product lines the warranty period has been extended to 24 months due to technical considerations incurred during the manufacture of such products. In the year ended September 28, 2008, the company incurred $227,000 of warranty expenses representing the estimated cost of repair or replacement for specific customer returned products still covered under warranty as of the return date and awaiting replacement, in addition to estimated future warranty costs for shipments occurring during the twelve months proceeding September 28, 2008. In the three months ended December 28, 2008, the company incurred $29,398 of warranty expense related to estimated warranties on product shipped during the first fiscal quarter of 2009. Future warranty costs were determined, based on estimated cost of replacement for expected returns based upon our most recent experience rate of defects as a percentage of sales. Prior to fiscal year 2008, all warranty expenses were incurred as product was replaced with no reserve for warranties against deliveries in the covered period.

On certain periscope product lines the warranty period has been extended from 15 to 24 months due to technical considerations incurred during the manufacture of such products. During June of 2008, Optex Systems Inc., (Delaware) experienced an internal control test failure related to the laser filters used on one of the periscope products. As a result of the internal test failure, Optex implemented a manufacturing process change to eliminate the potential for future failures. We believe the internal control test environment to be significantly more stringent than that which would occur under field conditions, however as a result of the internal test failure and manufacturing process change, we extended our warranty for all product shipped prior to the implemented change. As of the date of this report, Optex Systems Holdings has not received any warranty claims as a result of the condition.

Estimated Costs to Complete and Accrued Loss on Contracts. The Company reviews and reports on the performance of its contracts and production orders against the respective resource plans for such contracts/orders. These reviews are summarized in the form of estimates to complete and estimates at completion. Estimates at completion include the Company’s incurred costs to date against the contract/order plus management's current estimates of remaining amounts for direct labor, material, other direct costs and subcontract support and indirect overhead costs based on the completion status and future contractual requirements for each order. If an estimate at completion indicates a potential overrun (loss) against a fixed price contract/order, management generally seeks to reduce costs and /or revise the program plan in a manner consistent with customer objectives in order to eliminate or minimize any overrun and to secure necessary customer agreement to proposed revisions.

If an estimate at completion indicates a potential overrun against budgeted resources for a fixed price contract/order, management first attempts to implement lower cost solutions to still profitably meet the requirements of the fixed price contract. If such solutions do not appear practicable, management makes a determination whether to seek renegotiation of contract or order requirements from the customer. If neither cost reduction nor renegotiation appears probable, an accrual for the contract loss/overrun is recorded against earnings and the loss is recognized in the first period the loss is identified based on the most recent estimate at completion of the particular contract or product order.

Government Contracts: Virtually all of our contracts are prime or subcontracted directly with the Federal government and as such, are subject to Federal Acquisition Regulation Subpart 49.5, “Contract Termination Clauses” and more specifically Federal Acquisition Regulation clauses 52.249-2 “Termination for Convenience of the Government (Fixed-Price)”, and 49.504 “Termination of fixed-price contracts for default”.

Recent Accounting Pronouncements.

In June 2006, The FASB issued Interpretation No. 48 “Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109”. This Interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise’s financial statements in accordance with FASB No. 109, “Accounting for Income Taxes”. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The adoption of FIN 48 did not have a material impact on the Company's consolidated financial position, results of operations, or cash flows.

In September 2006, the FASB issued FASB No. 157, “Fair Value Measurements” which establishes a framework for measuring fair value, and expands disclosures about fair value measurements. While FASB No. 157 does not apply to transactions involving share-based payment covered by FASB No. 123, it establishes a theoretical framework for analyzing fair value measurements that is absent from FASB No. 123. We have relied on the theoretical framework established by FASB No. 157 in connection with certain valuation measurements that were made in the preparation of these financial statements. FASB No. 157 is effective for years beginning after November 15, 2007. Subsequent to the Standard’s issuance, the FASB issued an exposure draft that provides a one year deferral for implementation of the

Standard for non-financial assets and liabilities. The Company is currently evaluating the impact FASB No. 157 will have on its financial statements.

In February 2007, Statement of Financial Accounting Standards No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities-Including an Amendment of FASB Statement No. 115,” was issued. This standard allows a company to irrevocably elect fair value as the initial and subsequent measurement attribute for certain financial assets and financial liabilities on a contract-by-contract basis, with changes in fair value recognized in earnings. The provisions of this standard are effective as of the beginning of our fiscal year 2008, with early adoption permitted. The Company is currently evaluating what effect the adoption of FASB 159 will have on its financial statements.

In March 2007, the Financial Accounting Standards Board ratified “EITF” Issue No. 06-10, "Accounting for Collateral Assignment Split-Dollar Life Insurance Agreements”. EITF 06-10 provides guidance for determining a liability for the postretirement benefit obligation as well as recognition and measurement of the associated asset on the basis of the terms of the collateral assignment agreement. EITF 06-10 is effective for fiscal years beginning after December 15, 2007. The Company is currently evaluating the impact of EITF 06-10 on its financial statements, but does not expect it to have a material effect.

In December 2007, the FASB issued SFAS No. 141(R), Business Combinations and SFAS No. 160, Accounting and Reporting of Noncontrolling Interest in Consolidated Financial Statements, an amendment of ARB No. 51. These new standards will significantly change the accounting for and reporting of business combinations and non-controlling (minority) interests in consolidated financial statements. Statement Nos. 141(R) and 160 are required to be adopted simultaneously and are effective for the first annual reporting period beginning on or after December 15, 2008. Earlier adoption is prohibited. The Company is currently evaluating the impact of adopting SFAS Nos. 141(R) and SFAS 160 on its financial statements. See Note 14 to the financial statements for the year ended September 28, 2008 for adoption of SFAS 141R subsequent to September 30, 2008.

In December 2007, the SEC issued Staff Accounting Bulletin No. 110. SAB 110 permits companies to continue to use the simplified method, under certain circumstances, in estimating the expected term of “plain vanilla” options beyond December 31, 2007. SAB 110 updates guidance provided in SAB 107 that previously stated that the Staff would not expect a company to use the simplified method for share option grants after December 31, 2007. The Company does not have any outstanding stock options.

In March 2008, FASB issued Statement of Financial Accounting Standard (“SFAS”) No. 161, "Disclosures about Derivative Instruments and Hedging Activities—an amendment of FASB Statement No. 133”. SFAS 161 requires enhanced disclosures about an entity’s derivative and hedging activities. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008 with early application encouraged. As such, the Company is required to adopt these provisions at the beginning of the fiscal year ended September 30, 2009. The Company is currently evaluating the impact of SFAS 161 on its financial statements but does not expect it to have a material effect.

In May 2008, FASB issued SFAS No. 162, "The Hierarchy of Generally Accepted Accounting Principles”. SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (GAAP) in the United States. SFAS 162 is effective 60 days following the SEC’s approval of the Public Company Accounting Oversight Board amendments to AU Section 411, The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles. The Company is currently evaluating the impact of SFAS 162 on its consolidated financial statements but does not expect it to have a material effect.

In May 2008, FASB issued SFAS No. 163, "Accounting for Financial Guarantee Insurance Contracts—an interpretation of FASB Statement No. 60". SFAS 163 interprets Statement 60 and amends existing accounting pronouncements to clarify their application to the financial guarantee insurance contracts included within the scope of that Statement. SFAS 163 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and all interim periods within those fiscal years. As such, the Company is required to adopt these provisions at the beginning of the fiscal year ended September 30, 2011. The Company is currently evaluating the impact of SFAS 163 on its financial statements but does not expect it to have a material effect.

In June 2008, FASB issued FASB Staff Position EITF 03-6-1, “Determining Whether Instruments Granted in Share-Based Payment Transactions are Participating Securities”. FSP EITF 03-6-1 clarifies that share-based payment awards that entitle their holders to receive nonforfeitable dividends or dividend equivalents before vesting should be considered participating securities. We have granted and expect to continue to grant restricted stock that contain non-forfeitable rights to dividends and will be considered participating securities upon adoption of FSP EITF 03-6-1. As participating securities, we will be required to include these instruments in the calculation of our basic earnings per share ("EPS"), and we will need to calculate basic EPS using the "two-class method." Restricted stock is currently included in our dilutive EPS calculation using the treasury stock method. The two-class method of computing EPS is an earnings allocation formula that determines EPS for each class of common stock and participating security according to dividends declared (or accumulated) and participation rights in undistributed earnings. FSP EITF 03-6-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and all interim periods within those fiscal years. As such, the Company is required to adopt these provisions at the beginning of the fiscal year ending October 3, 2010. The Company does not expect adoption of FSP EITF 03-6-1 to have a material effect on the Company’s financial statements.

In May 2009, “FASB issued SFAS No. 165, "Subsequent Events". SFAS 165 establishes principles and requirements for the reporting of events or transactions that occur after the balance sheet date, but before financial statements are issued or are available to be issued. SFAS 165 is effective for financial statements issued for fiscal years and interim periods ending after June 15, 2009. As such, the Company adopted these provisions at the beginning of the interim period ended June 28, 2009. Adoption of SFAS 165 did not have a material effect on the Company’s financial statements.

In June 2009, FASB issued SFAS No. 168, " The FASB Accounting Standards Codification TM and the Hierarchy of Generally Accepted Accounting Principles - a replacement of FASB Statement No. 162". SFAS 168 replaces Statement 162 and to establish the FASB Accounting Standards CodificationTM (Codification) as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with GAAP. SFAS 168 is effective for financial statements issued for fiscal years and interim periods ending after September 15, 2009. As such, the Company is required to adopt these provisions at the beginning of the period ending September 27, 2009. The Company does not expect adoption of SFAS 168 to have a material effect its financial statements.

Cautionary Factors That May Affect Future Results

This Current Report on Form 8-K and other written reports and oral statements made from time to time by the Company may contain so-called “forward-looking statements,” all of which are subject to risks and uncertainties. You can identify these forward-looking statements by their use of words such as “expects,” “plans,” “will,” “estimates,” “forecasts,” “projects” and other words of similar meaning. You can identify them by the fact that they do not relate strictly to historical or current facts. These statements are likely to address the Company’s growth strategy, financial results and product and development programs. You must carefully consider any such statement and should understand that many factors could cause actual results to differ from the Company’s forward-looking statements. These factors include inaccurate assumptions and a broad variety of other risks and uncertainties, including some that are known and some that are not. No forward-looking statement can be guaranteed and actual future results may vary materially.

The Company does not assume the obligation to update any forward-looking statement. You should carefully evaluate such statements in light of factors described in the Company’s filings with the SEC, especially on Forms 10-K, 10-Q and 8-K. In various filings the Company has identified important factors that could cause actual results to differ from expected or historic results. You should understand that it is not possible to predict or identify all such factors. Consequently, you should not consider any such list to be a complete list of all potential risks or uncertainties.

RISK FACTORS

Investing in our common stock involves a high degree of risk. Prospective investors should carefully consider the risks described below, together with all of the other information included or referred to in this prospectus, before purchasing shares of our common stock. There are numerous and varied risks, known and unknown, that may prevent us from achieving our goals. The risks described below are not the only risks we will face. If any of these risks actually occurs, our business, financial condition or results of operations may be materially adversely affected. In such case, the trading price of our common stock could decline and investors in our common stock could lose all or part of their investment. The risks and uncertainties described below are not exclusive and are intended to reflect the material risks that are specific to us , material risks related to our industry and material risks related to companies that undertake a public offering or seek to maintain a class of securities that is registered or traded on any exchange or over-the-counter market.

Risks Related to our Business

We expect that we will need to raise additional capital in the future; additional funds may not be available on terms that are acceptable to us, or at all.

We anticipate we will have to raise additional capital in the future to service our debt and to finance our future working capital needs. We cannot assure you that any additional capital will be available on a timely basis, on acceptable terms, or at all. Future equity or debt financings may be difficult to obtain. If we are not able to obtain additional capital as may be required, our business, financial condition and results of operations could be materially and adversely affected.

We anticipate that our capital requirements will depend on many factors, including:

- our ability to fulfill backlog;
- our ability to procure additional production contracts;
- our ability to control costs;
- the timing of payments and reimbursements from government and other contracts, including but not limited to changes in federal government military spending and the federal government procurement process;
- increased sales and marketing expenses;
- technological advancements and competitors’ response to our products;
- capital improvements to new and existing facilities;
- our relationships with customers and suppliers; and

- general economic conditions including the effects of future economic slowdowns, acts of war or terrorism and the current international conflicts.

Even if available, financings can involve significant costs and expenses, such as legal and accounting fees, diversion of management's time and efforts, and substantial transaction costs. If adequate funds are not available on acceptable terms, or at all, we may be unable to finance our operations, develop or enhance our products, expand our sales and marketing programs, take advantage of future opportunities or respond to competitive pressures.

Current economic conditions may adversely affect our ability to continue operations.

Current economic conditions may cause a decline in business and consumer spending and capital market performance, which could adversely affect our business and financial performance. Our ability to raise funds, upon which we are fully dependent to continue to expand our operations, may be adversely affected by current and future economic conditions, such as a reduction in the availability of credit, financial market volatility and economic recession.

Our ability to fulfill our backlog may have an effect on our long term ability to procure contracts and fulfill current contracts.

Our ability to fulfill our backlog may be limited by our ability to devote sufficient financial and human capital resources and limited by available material supplies. If we do not fulfill our backlog in a timely manner, we may experience delays in product delivery which would postpone receipt of revenue from those delayed deliveries. Additionally, if we are consistently unable to fulfill our backlog, this may be a disincentive to customers to award large contracts to us in the future until they are comfortable that we can effectively manage our backlog.

Our historical operations depend on government contracts and subcontracts. We face risks related to contracting with the federal government, including federal budget issues and fixed price contracts.

Future general political and economic conditions, which cannot be accurately predicted, may directly and indirectly affect the quantity and allocation of expenditures by federal agencies. Even the timing of incremental funding commitments to existing, but partially funded, contracts can be affected by these factors. Therefore, cutbacks or re-allocations in the federal budget could have a material adverse impact on our results of operations. Obtaining government contracts may also involve long purchase and payment cycles, competitive bidding, qualification requirements, delays or changes in funding, budgetary constraints, political agendas, extensive specification development, price negotiations and milestone requirements. In addition, our government contracts are primarily fixed price contracts, which may prevent us from recovering costs incurred in excess of budgeted costs. Fixed price contracts require us to estimate the total project cost based on preliminary projections of the project's requirements. The financial viability of any given project depends in large part on our ability to estimate such costs accurately and complete the project on a timely basis. Some of those contracts are for products that are new to our business and are thus subject to unanticipated impacts to manufacturing costs. Given the current economic conditions, it is also possible that even if our estimates are reasonable at the time made, that prices of materials are subject to unanticipated adverse fluctuation. In the event our actual costs exceed fixed contractual costs of our product contracts, we will not be able to recover the excess costs which could have a material adverse effect on our business and results of operations. We examine these contracts on a regular basis and accrue for anticipated losses on these contracts, if necessary. As of September 27, 2009, we had approximately $1.3 million of loss provision accrued for these fixed price contracts.

Approximately 95% of our contracts contain contract termination clauses for convenience. In the event these clauses should be invoked by our customer, future revenues against these contracts could be affected, however these clauses allow for a full recovery of any incurred contract cost plus a reasonable fee up through and as a result of the contract termination. We are currently unaware of any pending terminations on our existing contracts. In some cases, contract awards may be issued that are subject to renegotiation at a date (up to 180 days) subsequent to the initial award date. Generally, these subsequent negotiations have had an immaterial impact (zero to 5%) on the contract price of the affected contracts. Currently, none of our awarded contracts are subject to renegotiation.

If we fail to scale our operations appropriately in response to growth and changes in demand, we may be unable to meet competitive challenges or exploit potential market opportunities, and our business could be materially and adversely affected.

Our past growth has placed, and any future growth in our historical business is expected to continue to place, a significant strain on our management personnel, infrastructure and resources. To implement our current business and product plans, we will need to continue to expand, train, manage and motivate our workforce, and expand our operational and financial systems, as well as our manufacturing and service capabilities. All of these endeavors will require substantial management effort and additional capital. If we are unable to effectively manage our expanding operations, we may be unable to scale our business quickly enough to meet competitive challenges or exploit potential market opportunities, and our current or future business could be materially and adversely affected.

We do not have long-term employment agreements with our key personnel, other than our Chief Operating Officer. If we are not able to retain our key personnel or attract additional key personnel as required, we may not be able to implement our business plan and our results of operations could be materially and adversely affected.

We depend to a large extent on the abilities and continued participation of our executive officers and other key employees. The loss of any key employee could have a material adverse effect on our business. We currently have only one employment agreement, with our Chief Operating Officer, and do not presently maintain "key man" insurance on any key employees. We believe that as our activities increase and change in character, additional, experienced personnel will be required to implement our business plan. Competition for such personnel is intense and we cannot assure you that they will be available when required, or that we will have the ability to attract and retain them. In addition, we do not presently have depth of staffing in our executive, operational and financial management. Until additional key personnel can be successfully integrated into our operations, the timing or success of which we cannot currently predict, our results of operations and ultimate success will be vulnerable to challenges associated with recruiting additional key personnel and difficulties associated with the loss of any key personnel in the future.

Our intangible assets or goodwill may suffer impairment in the future.

Goodwill represents the cost of acquired businesses in excess of fair value of the related net assets at acquisition. Valuation of intangible assets, such as goodwill, requires us to make significant estimates and assumptions including, but not limited to, estimating future cash flows from product sales, developing appropriate discount rates, maintaining customer relationships and renewing customer contracts, and approximating the useful lives of the intangible assets acquired. To the extent actual results differ from these estimates, our intangible assets or goodwill may suffer impairment in the future that will impact our results of operations. We reviewed the fair market value of our goodwill and intangible assets as of September 28, 2008, based on the fair market values established in connection with the acquisition by Optex Systems, Inc. (Delaware) of the assets of Optex Systems, Inc. (Texas) as of October 14, 2008, and as a result, determined that the current carrying value of goodwill had been impaired by $1.6 million. We intend to continue to monitor the value of our intangible assets and goodwill in order to identify any impairment that may occur in the future.

Certain of our products are dependent on specialized sources of supply that are potentially subject to disruption which could have a material, adverse impact on our business.

Optex Systems Holdings has selectively single-sourced some of our material components in order to mitigate excess procurement costs associated with significant tooling and startup costs. Furthermore, because of the nature of government contracts, we are often required to purchase selected items from Government approved suppliers, which may further limit our ability to utilize multiple supply sources for these key components.

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To the extent any of these single sourced or government approved suppliers should have disruptions in deliveries due to production, quality, or other issues, Optex Systems Holdings may also experience related production delays or unfavorable cost increases associated with retooling and qualifying alternate suppliers. The impact of delays resulting from disruptions in supply for these items could negatively impact our revenue, our customer reputation, and our results of operations. In addition, significant price increases from single-source suppliers could have a negative impact on our profitability to the extent that we are unable to recover these cost increases on our fixed price contracts.

Each contract has a specific quantity of material which needs to be purchased, assembled, and finally shipped. Prior to bidding a contract, Optex Systems Holdings contacts potential sources of material and receives qualified quotations for this material. In some cases, the entire volume is given to a single supplier and in other cases, the volume might be split between several suppliers. If a contract has a single source supplier and that supplier fails to meet their obligations (e.g., quality, delivery), then Optex Systems Holdings would find an alternate supplier and bring this information back to the final customer. Contractual deliverables would then be re-negotiated (e.g., specifications, delivery, price). Currently, approximately 28% of our total material requirements are single-sourced across 21 suppliers representing approximately 20% of our active supplier base. Single-sourced component requirements span across all of our major product lines. The vast majority of these single-sourced components could be provided by another supplier with minimal interruption in schedule (supply delay of 3 months or less) or increased costs. We do not believe these single sourced materials to pose any significant risk to Optex Systems Holdings as other suppliers are capable of satisfying the purchase requirements in a reasonable time period with minimal increases in cost. Of these single sourced components, we have contracts (purchase orders) with firm pricing and delivery schedules in place with each of the suppliers to supply parts in satisfaction of our current contractual needs.

We consider only those specialized single source suppliers where a disruption in the supply chain would result in a period of three months or longer for Optex Systems Holdings to identify and qualify a suitable replacement to present a material financial or schedule risk. In the table below we identify only those specialized single source suppliers and the product lines supported by those materials.

Product Line	Supplier	Supply Item	Risk	Purchase Orders
Periscopes	TSP Inc	Window used on all glass & plastic periscopes	Proprietary coatings would take in excess of 6 months to identify and qualify an alternative source	Current Firm Fixed Price & Quantity Purchase orders are in place with the supplier to meet all contractual requirements. Supplier is on schedule.
Periscopes	Spartec Polycast	Acrylic raw material used on plastic periscope assemblies	This material has quality characteristics which would take in excess of 6 months to identify and qualify an alternative source.	Current Firm Fixed Price & Quantity Purchase orders are in place with the supplier to meet all contractual requirements. Supplier is on schedule.
Howitzers	Danaher Controls	Counter Assembly for M137 & M187 Howitzer programs	Critical assembly would take in excess of 6 months to identify and qualify an alternative source. Currently, the only US Government approved supplier.	Current Firm Fixed Price & Quantity Purchase orders are in place with the supplier to meet all contractual requirements. Supplier is on schedule.

Other	SWS Trimac	Subcontracted Electron Beam Welding	Subcontracted welder that is the only qualified supplier for General Dynamics Land Systems muzzle reference system collimator assemblies. This operation would take in excess of 6 months to identify and qualify an alternative supplier.	Current Firm Fixed Price & Quantity Purchase orders are in place with the supplier to meet all contractual requirements. Supplier is on schedule.

The defense technology supply industry is subject to technological change and if we are not able to keep up with our competitors and/or they develop advanced technology as response to our products, we may be at a competitive disadvantage.

The market for our products is generally characterized by technological developments, evolving industry standards, changes in customer requirements, frequent new product introductions and enhancements, short product life cycles and severe price competition. Our competitors could also develop new, more advanced technologies in reaction to our products. Currently accepted industry standards may change. Our success depends substantially on our ability, on a cost-effective and timely basis, to continue to enhance our existing products and to develop and introduce new products that take advantage of technological advances and adhere to evolving industry standards. An unexpected change in one or more of the technologies related to our products, in market demand for products based on a particular technology or of accepted industry standards could materially and adversely affect our business. We may or may not be able to develop new products in a timely and satisfactory manner to address new industry standards and technological changes, or to respond to new product announcements by others. In addition, new products may or may not achieve market acceptance.

Unexpected warranty and product liability claims could adversely affect our business and results of operations.

The possibility of future product failures could cause us to incur substantial expense to repair or replace defective products. Some of our customers require that we warrant the quality of our products to meet customer requirements and be free of defects for up to fifteen months subsequent to delivery. Approximately 50% of our current contract deliveries are covered by these warranty clauses. We establish reserves for warranty claims based on our historical rate of less than one percent of returned shipments against these contracts. There can be no assurance that this reserve will be sufficient if we were to experience an unexpectedly high incidence of problems with our products. Significant increases in the incidence of such claims may adversely affect our sales and our reputation with consumers. Costs associated with warranty and product liability claims could materially affect our financial condition and results of operations.

We derive almost all of our revenue from two customers and the loss of either customer or both customers could have a material adverse effect on our revenues.

At present, we derive approximately 93% of the gross revenue from our business from two customers, with 46% from General Dynamics Land System Division and 47% from Tank-automotive and Armaments Command. Procuring new customers and contracts may partially mitigate this risk. A decision by either General Dynamics Land System Division or Tank-automotive and Armaments Command to cease issuing contracts could have a significant material impact on our business and results of operations. There can be no assurance that we could replace these customers on a timely basis or at all.

We have approximately 50 discrete contracts with General Dynamics Land System Division and Tank-automotive and Armaments Command. If they choose to terminate these contracts, Optex Systems Holdings is entitled to fully recover all contractual costs and reasonable profits incurred up to or as a result of the terminated contract.

We do not possess any patents and rely solely on trade secrets to protect our intellectual property.

We utilize several highly specialized and unique processes in the manufacture of our products, for which we rely solely on trade secrets to protect our innovations. We cannot assure you that we will be able to maintain the confidentiality of our trade secrets or that our non-disclosure agreements will provide meaningful protection of our trade secrets, know-how or other proprietary information in the event of any unauthorized use, misappropriation or other disclosure. The confidentiality agreements that are designed to protect our trade secrets could be breached, and we might not have adequate remedies for the breach.

It is also possible that our trade secrets will otherwise become known or independently developed by our competitors, many of which have substantially greater resources, and may have applied for or obtained, or may in the future apply for and obtain, patents that will prevent, limit or interfere with our ability to make and sell some of our products. Although based upon our general knowledge (and we have not conducted exhaustive patent searches), we believe that our products do not infringe on the patents or other proprietary rights of third parties; however, we cannot assure you that third parties will not assert infringement claims against us or that such claims will not be successful.

In the future, we may look to acquire other businesses in our industry and the acquisitions will require us to use substantial resources, among other things.

At some time in the future, we may decide to pursue a consolidation strategy with other businesses in our industry. In order to successfully acquire other businesses, we would be forced to spend significant resources in both acquisition and transactional costs, which could divert substantial resources in terms of both financial and personnel capital from our current operations. Additionally, we might assume liabilities of the acquired business, and the repayment of those liabilities could have a material adverse impact on our cash flow. Furthermore, when a new business is integrated into our ongoing business, it is possible that there would be a period of integration and adjustment required which could divert resources from ongoing business operations.

Conversion of our Series A preferred stock could cause substantial dilution to our existing common stock holders, and certain other rights of the preferred stock holders present other risks to our existing common stock holders.

As of September 27, 2009, we had 139,444,940 shares of our common stock issued and outstanding, as well as 1,027 shares of our Series A preferred stock issued and outstanding. The Series A preferred stock is convertible into 41,080,000 shares of our common stock, and upon conversion, the Series A preferred stock would represent 21.7% of our outstanding common stock. This would greatly dilute the holdings of our existing common stockholders. In addition, the preferred shareholders vote on a one-to-one basis with our common shareholders on an as converted basis.

Furthermore, in the event of a liquidation, the holders of our Series A preferred stock would receive priority liquidation payments before payments to common shareholders equal to the amount of the stated value of the preferred stock before any distributions would be made to our common shareholders. The total stated value of our preferred stock is $6,162,000, so the preferred shareholders would need to receive that amount before any distributions could be made to common shareholders. Our assets with liquidation value are exceeded by our liabilities on our balance sheet; therefore, upon a liquidation, there would be no assets remaining for distribution to common shareholders.

Lastly, the preferred shareholders have the right, by majority vote of the shares of preferred stock, to generally approve any issuances by us of equity and/or indebtedness, which is not ordinary course trade indebtedness. Therefore, the preferred shareholders can effectively bar us from entering into a transaction which they feel is not in their best interests even if the transaction would otherwise be in the best interests of Optex Systems

Holdings and its common shareholders.

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Risks Relating to the Reorganization

A director who is also an executive officer beneficially owns a substantial percentage of Optex Systems Holdings' outstanding common stock, which gives him control over certain major decisions on which Optex Systems Holdings' stockholders may vote, which may discourage an acquisition of Optex Systems Holdings ..

As a result of the reorganization, Sileas, which is owned by Optex Systems Holdings' three officers (one of whom is also one of Optex Systems Holdings' three directors), beneficially owns, in the aggregate, approximately 73.5% of Optex Systems Holdings' outstanding common stock. One director who is also an executive officer, Stanley Hirschman, owns the majority equity interest in Sileas. The interests of Optex Systems Holdings' management may differ from the interests of other stockholders. As Optex Systems Holdings' executive management has the right and ability to control virtually all corporate actions requiring stockholder approval, irrespective of how Optex Systems Holdings' other stockholders may vote, including the following actions:

- Confirming or defeating the election of directors;
- amending or preventing amendment of Optex Systems Holdings' certificate of incorporation or bylaws;
- effecting or preventing a reorganization, sale of assets or other corporate transaction; and controlling the outcome of any other matter submitted to the stockholders for vote.

Optex Systems Holdings' management's beneficial stock ownership may discourage a potential acquirer from seeking to acquire shares of Optex Systems Holdings' common stock or otherwise attempting to obtain control of Optex Systems Holdings, which in turn could reduce the stock price or prevent Optex Systems Holdings' stockholders from realizing a premium over Optex Systems Holdings' stock price.

If Sileas is unable to meet its obligations under the purchase money note to the party from which it purchased its stock holdings in Optex Systems Holdings, there could be a change in control in Optex Systems Holdings.

On February 20, 2009, Sileas purchased 100% of the equity and debt interest held by Longview, representing 90% of Optex Systems, Inc. (Delaware), in a private transaction. The purchase price for the acquisition of Longview's position was $13,524,405, and the consideration was paid in the form of a promissory note. The obligations of Sileas under the promissory note are secured by a security interest in Optex Systems Holdings' common and preferred stock owned by Sileas. As Sileas has no operations or business activities other than holding the purchased assets, Sileas is depending upon the value of its common stock and preferred stock holdings in Optex Systems Holdings to increase over time in order to pay its obligations under the promissory note. If the value of the holdings does not sufficiently increase, and Sileas is unable to meet its payment obligations, Longview could exercise its remedies with respect to its security interest and take control of the pledged stock, and thus there would be a change in control of Optex Systems Holdings, as Sileas is currently the majority owner of Optex Systems Holdings. There can be no guarantee that the investment objectives of Longview will be the same as those of Sileas or our other shareholders. In the event that control shifts to Longview from Sileas, Longview may vote its shares differently than Sileas would have voted under similar circumstances.

Public company compliance may make it more difficult to attract and retain officers and directors ..

The Sarbanes-Oxley Act of 2002 and new rules subsequently implemented by the SEC have required changes in corporate governance practices of public companies. As a public entity, Optex Systems Holdings expects these new rules and regulations to increase compliance costs in 2010 and beyond and to make certain activities more time consuming and costly. As a public entity, Optex Systems Holdings also expects that thes