

SURGE COMPONENTS INC
Form 10-K
February 28, 2019

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended **November 30, 2018**

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

For the transition period from _____ to _____

Commission File No. 000-27688

SURGE COMPONENTS, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

11-2602030
(I.R.S. Employer
Identification No.)

95 East Jefryn Boulevard

11729

Deer Park, New York

(Address of principal executive offices) (Zip Code)

(631) 595-1818

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Exchange Act:

| Title of Each Class to be so Registered: | Name of each exchange on which registered |
|--|---|
| None | None |

Securities registered under Section 12(g) of the Act:

Common Stock, Par Value \$0.001

Preferred Stock Purchase Rights

(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes No

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in the definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or amendment to this Form 10-K.

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

| | |
|-------------------------|---------------------------|
| Large Accelerated Filer | Accelerated Filer |
| Non-accelerated Filer | Smaller reporting company |
| | Emerging growth company |

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of May 31, 2018, the aggregate market value of the issued and outstanding common stock held by non-affiliates of the registrant, based upon the closing price of the common stock, was approximately \$3.9 million.

The registrant's common stock outstanding as of February 26, 2019, was 5,262,128 shares of common stock.

SURGE COMPONENTS, INC.

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FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements. All statements other than statements of historical facts contained in this report, including statements regarding our future results of operations and financial position, business strategy and plans and objectives of management for future operations, are forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements.

In some cases, forward-looking statements can be identified by terms such as “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “could,” “intends,” “target,” “projects,” “contemplates,” “believes,” “estimates,” “predicts,” “potential” or “contingent,” and the negative of these terms or other similar words. These statements are only predictions. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our business, financial condition and results of operations. We discuss many of the risks in greater detail under the heading “Risk Factors.” Also, these forward-looking statements represent our estimates and assumptions only as of the date of the filing of this report. Except as required by law, we assume no obligation to update any forward-looking statements after the date of the filing of this report.

This report also contains estimates and other statistical data made by independent parties and by us relating to market size and growth and other industry data. This data involves a number of assumptions and limitations, and investors are cautioned not to give undue weight to such estimates. We have not independently verified the statistical and other industry data generated by independent parties and contained in this report and, accordingly, we cannot guarantee their accuracy or completeness. In addition, projections, assumptions and estimates of our future performance and the future performance of the industries in which we operate are subject to a high degree of uncertainty and risk due to a variety of factors, including those described in “Risk Factors” and elsewhere in this report. These and other factors could cause results to differ materially from those expressed in the estimates made by the independent parties and by us.

PART I

Item 1. Business.

References to “we,” “us,” “our”, “our company” and “the company” refer to Surge Components, Inc. (“Surge” or the “Company”) and, unless the context indicates otherwise, includes Surge’s wholly-owned subsidiaries, Challenge/Surge, Inc. (“Challenge”), and Surge Components, Limited (“Surge Limited”).

We were incorporated under the laws of the State of New York on November 24, 1981, and re-incorporated in Nevada on August 26, 2010. In February 2019, we converted into a Delaware corporation. We completed an initial public offering of our securities in 1984 and a second offering in August 1996. Our principal executive offices are located at 95 East Jefryn Boulevard, Deer Park, New York 11729 and our telephone number is (631) 595-1818.

We are a supplier of electronic products and components. These products include capacitors, which are electrical energy storage devices, and discrete components, such as semiconductor rectifiers, transistors and diodes, which are single function low power semiconductor products that are packaged alone as compared to integrated circuits such as microprocessors. The products that we sell are typically utilized in the electronic circuitry of diverse products, including, but not limited to, automobiles, telecomm, audio, cellular telephones, computers, consumer electronics, garage door openers, household appliances, power supplies and security equipment. The products that we sell are sold to both original equipment manufacturers, commonly referred to as OEMs, who incorporate them into their products, and to distributors of the lines of products we sell, who resell these products within their customer base. Surge sells its products through three of the top four distributors for electronic components in the world and also supplies its products to subcontractors who manufacture for their customers. These channels open doors to Surge at customers which Surge may not have access to otherwise. The products that we sell are manufactured predominantly in Asia by approximately sixteen independent manufacturers. We only have one binding long-term supply agreement with one of our manufacturers, Lelon Electronics. We have an agreement to act as the exclusive sales agent utilizing independent sales representative organizations in North America to sell and market the products for one of such manufacturers, Lelon Electronics. When we act as a sales agent, we receive a commission from our supplier who sold the product to the customer that we introduced to our supplier. The amount of the commission is determined on a sale by sale basis depending on the profit margin of the product. Commission revenue totaled \$48,730 and \$244,631 for the fiscal years ended November 30, 2018 (“Fiscal 2018”) and November 30, 2017 (“Fiscal 2017”), respectively.

Challenge is engaged in the sale of electronic components. In 1999, Challenge began as a division to sell audible components. We have been able to increase the types of products that we sell because some of our suppliers introduced new products, and we also located other products from new suppliers. Our core products include buzzers, speakers, microphones, resonators, alarms, chimes, filters, and discriminators. We now also work with our suppliers to have our suppliers customize many of the products we sell for many customers through the customers’ own designs

and those that we work with our suppliers to have our suppliers redesign for them at our suppliers' factories. We have an engineer on our staff who works with our suppliers on such redesigns and assists with the introduction of new product lines. We are continually looking to expand the line of products that we sell. We sell these products through independent representatives that earn a commission on the products we sell. We are also working with local, regional, and national distributors to sell these products to local accounts in every state.

In order for us to grow, we will depend on, among other things, the continued growth of the electronics and semiconductor industries, our ability to withstand intense price competition, our ability to obtain new clients, our ability to retain and attract sales and other personnel in order to expand our marketing capabilities, our ability to secure adequate sources of products, which are in demand on commercially reasonable terms, our success in managing growth, including monitoring an expanded level of operations.

Industry Background

The United States electronics distribution industry is composed of manufacturers, national and international distributors, as well as regional and local distributors. Electronics distributors market numerous products, including active components (such as transistors, microprocessors, integrated circuits and semiconductors), passive components (such as capacitors and audibles), and electro mechanical, interconnect (such as connectors and wire) and computer products. Surge focuses its efforts on the sale of capacitors, discrete components, and audible products.

The electronics industry has been characterized by intense price cutting and rapid technological changes and development, which could materially adversely affect our future operating results. In addition, the industry has been affected historically by periodic economic downturns, which have had an adverse economic effect upon manufacturers and end-users of the products that we sell, as well as distributors. Furthermore, the life-cycle of existing electronic products and the timing of new product development and introduction can affect the demand for electronic components, including the products that we sell. Accordingly, any downturn in the electronics industry in general could adversely affect our business and results of operations. Due to rising transportation and employment costs in Asia, we have seen some U.S. manufacturers start moving their manufacturing facilities to Mexico to reduce transportation costs and bring manufacturing much closer to home. At this time, however, none of our customers has moved its manufacturing facilities to Mexico.

Products

Surge supplies a wide variety of electronic components (some of which bear our private “Surge” label) which can be broadly divided into two categories—capacitors and discrete components. For Fiscal 2018 and Fiscal 2017, capacitors accounted for approximately 51% and 50% of Surge’s sales, respectively, of which approximately 75% for each year was Lelon capacitors (discussed below). Discrete components accounted for Surge’s remaining sales in Fiscal 2018 and Fiscal 2017. Capacitors and discrete components can be categorized based on various factors, including function, construction, fabrication and capacity.

We sell, under the name of the manufacturer, Lelon Electronics, aluminum electrolytic capacitors, which are capacitors that store and release energy into a circuit incrementally and are used in various applications, including but not limited to, computers, appliances, automotive, lighting, telecommunications devices and various consumer products. Our sales of products under the Lelon Electronics name accounted for approximately 46% of our total sales (and approximately 75% of our capacitor sales as noted above) in Fiscal 2018.

The principal products sold by Surge under the Surge name (except with respect to capacitors, which the Company also sells under the Lelon Electronics name as noted above) or by Challenge are set forth below.

Capacitors

A capacitor is an electrical energy storage device used in the electronics industry for varied applications, principally as elements of resonant circuits, coupling and bypass applications, blockage of DC current, frequency determining and timing elements, filters and delay-line components. All products are available in traditional leaded as well as surface mount (chip) packages. The product line of capacitors we sell includes:

Aluminum Electrolytic Capacitors- These capacitors, which are Surge's principal product, are storage devices used in power applications to store and release energy as the electronic circuitry demands. They are commonly used in power supplies and can be found in a wide range of consumer electronics products. Our supplier has one of the largest facilities for these products in Taiwan and China. These facilities are fully certified for the International Quality Standard ISO 9001 and QS9000, and TS16949, which means that they meet the strictest requirements established by the automotive industry and adopted throughout the world to ensure that the facility's manufacturing processes, equipment and associated quality control systems will satisfy specific customer requirements. This system is also intended and designed to facilitate clear and thorough record keeping of all quality control and testing information and to ensure clear communication from one department to another about the information (i.e., quality control, production or engineering). This certification permits us to monitor quality control/manufacturing process information and to respond to any customer questions.

Ceramic Capacitors- These capacitors are the least expensive, and are widely used in the electronics industry. They are commonly used to bypass or filter semiconductors in resonant circuits and are found predominantly in a wide range of low cost products including computer, telecom, appliances, games and toys.

Mylar Film Capacitors- These capacitors are frequently used for noise suppression and filtering. They are commonly used in telecommunication and computer products. Surge's suppliers in China have facilities fully certified for all of the above mentioned quality certifications.

Discrete Components

Discrete components, such as semiconductor rectifiers, transistors and diodes, are packaged individually to perform a single or limited function, in contrast to integrated circuits, such as microprocessors and other "chips", which contain from only a few diodes to as many as several million diodes and other elements in a single package, and are usually designed to perform complex tasks. Surge almost exclusively distributes discrete, low power semiconductor components rather than integrated circuits.

The product line of discrete components we sell includes:

Rectifiers- Low power semiconductor rectifiers are devices that convert alternating current, or AC power, into one directional current, or DC power, by permitting current to flow in one direction only. They tend to be found in most electrical apparatuses, especially those drawing power from an AC wall outlet. All products are available in traditional leaded as well as surface mount (chip) packages. Surge's rectifier suppliers all have the aforementioned certifications, giving us an opportunity to market the products that we sell to the automotive industry.

Transistors- These products send a signal to the circuit for transmission of waves. They are commonly used in applications involving the processing or amplification of electric current and electric signals, including data, television, sound and power. All products are available in traditional leaded as well as surface mount (chip) packages. Surge sells many types of ISO 9002 transistors, including power transistors, designed for large currents to safely dissipate large amounts of power.

Diodes- Diodes are two-lead or surface mount components that allow electric current to flow in only one direction. They are used in a variety of electronic applications, including signal processing and direction of current. All products are available in traditional leaded as well as surface mount (chip) packages. Diodes sold include:

Circuit Protection Devices- Our circuit protection devices include transient voltage suppressors and metal oxide varistors, which protect circuits against switching, lightning surges and other uncontrolled power surges and/or interruptions in circuits. Transient voltage suppressors, which offer a higher level of protection for the circuit, are required in telecommunication products and are typically higher priced products than the metal oxide varistors, which are more economically priced and are used in consumer products. All products are available in traditional leaded as well as surface mount (chip) packages.

Audible Components- These include audible transducers, Piezo buzzers, speakers, and microphones, which produce an audible sound for, and are used in back-up power supplies for computers, alarms, appliances, smoke detectors, automobiles, telephones and other products which produce sounds. Challenge has initiated marketing relationships with certain Asian manufacturers of audible components to sell these products worldwide. All products are available in traditional leaded as well as surface mount (chip) packages.

New Products- We periodically introduce new products, which are intended to complement our existing product lines. These products are ones that are commonly used in the same circuit designs as other of the products that we sell and will further provide a one- stop-shop for the customer. Some of these products are common items used in all applications and others are niche items with a focus towards a particular application. These new products include

fuses, printed circuit boards and switches. All products are available in traditional leaded as well as surface mount (chip) versions.

Inventory

In order to adequately service our customers' needs, we believe that it is necessary to maintain large inventories, which makes us more susceptible to price and technology changes. At any given time, we attempt to maintain a one-to-two month inventory on certain products in high demand for customers and at least one month for other products. Our inventory currently contains more than 100 million component units consisting of more than 3,000 different part numbers. The products that we sell range in sales price from less than one cent for a commercial diode to more than \$2.00 for high power capacitors and semiconductors. As of November 30, 2018, we maintained inventory valued at \$3,389,065.

Because of the experience of our management, including Ira Levy and Steven Lubman, we believe that we know the best prices to buy the products we sell and as a result we generally waive rights to manufacturers' inventory protection agreements (including price protection and inventory return rights), and thereby bear the risk of increases in the prices charged by our manufacturers and decreases in the prices of products held in our inventory or covered by purchase commitments. If prices of components, which we hold in inventory decline, or if new technology is developed that displaces products that we sell, our business could be materially adversely affected. The Company has experienced very little impact from customer design changes and slowdown but this can potentially increase due to economic conditions and customer-specific business conditions. If our customers experience these changes, our business could be adversely affected.

Product Availability

Surge and Challenge obtain substantially all of their products from manufacturers in Asia. However, in Fiscal 2018 and Fiscal 2017, Challenge purchased approximately 94% and 95%, respectively, of its products overseas as a result of Challenge's introduction of new product lines. Of the total goods purchased by Surge and Challenge in Fiscal 2018, those foreign manufactured products were supplied from manufacturers in Taiwan (49%), Hong Kong (18%), elsewhere in Asia (30%) and overseas outside of Asia (less than 1%). The Company purchases its products from approximately sixteen different manufacturers.

Most of the facilities that manufacture products for Surge have obtained International Quality Standard ISO 9002 and other certifications. We typically purchase the products that we sell in United States currency in order to minimize the risk of currency fluctuations. In most cases, Surge utilizes two or more alternative sources of supply for each of its products with one primary and one complementary supplier for each product. Surge's relationships with many of its suppliers date back to the commencement of our import operations in 1983. We have established payment terms with our manufacturers of between 30 and 60 day open account terms.

We only have one agreement with a supplier, Lelon Electronics, which is terminable by either party upon six months' notice to the other party. We have an agreement to act as the sales agent in North America for one of our manufacturers, Lelon Electronics. While we believe that we have established close working relationships with our principal manufacturers, our success depends, in large part, on maintaining these relationships and developing new supplier relationships for our existing and future product lines. Because of the lack of long-term contracts, we may not be able to maintain these relationships.

For Fiscal 2018 and Fiscal 2017, one of Surge's vendors, Lelon Electronics, accounted for approximately 46% and 49% of Surge's consolidated purchases. The loss of or a significant disruption in the relationship with Lelon Electronics, which is our major supplier, could have a material adverse effect on our business and results of operations until a suitable replacement could be obtained.

The Company has a written agreement with Lelon Electronics regarding the supply of inventory for the Company's customers. The Company purchases products under both the Company's name and Lelon's brand name for the Company's inventory in order to supply the Company's customers. For the majority of purchases from Lelon Electronics, the Company takes title to the products, houses them in the Company's warehouse and sells directly to the Company's customers. There is no right of return on the products purchased from Lelon and the Company accepts all credit risk with regards to sales of these products.

The components business has, from time to time, experienced periods of shortages in product supply, usually as the result of demand exceeding available supply. When these shortages occur, suppliers tend to either increase prices and or reduce the number of units sold to given customers. Should there be shortages in the future, such shortages may benefit our business if we get preferential supply from our manufacturers. It could also have an adverse effect upon our business, in the case that our manufacturers don't have enough capacity to provide enough components. Conversely, due to poor market demand, there could be an excess of components in the market, causing stronger competition and an erosion of prices. While our manufacturing partners are experiencing extended delivery times we believe that these delivery times are less than the delivery times experienced by its competitors. This has caused a slower ramp up in new business because of the longer lead time necessary to get products to customers. We expect this trend to continue at least through mid-2019.

Marketing and Sales

Surge's sales efforts are directed towards Original Equipment Manufacturer (OEM) customers in numerous industries where the products that we sell have wide application. Surge currently employs twelve sales and marketing personnel, not including two of its executive officers, who are responsible for certain key customer relationships.

We use independent sales representatives or organizations, which often specialize in specific products and areas and have specific knowledge of and contacts in particular markets. We currently have representation agreements with approximately 30 sales representative organizations. Sales representative organizations, which are generally paid a 5% commission on net sales, are generally responsible in their respective geographic markets for identifying customers and soliciting customer orders. Pursuant to arrangements with our independent sales representatives, they are permitted to represent other electronics manufacturers, but are generally prohibited from carrying a line of products competitive with the products that we sell. These arrangements can be terminated on written notice by either party or if breached by either party. These organizations normally employ between one and twelve sales representatives. The individual sales representatives employed by the sales organizations generally possess an expertise which enhances the scope of our marketing and sales efforts. This permits us to avoid the significant costs associated with creating a direct marketing network. We have had relationships with certain sales organizations since 1988 and continue to engage new sales organizations as needed. We believe that additional sales organizations and representatives are available to us, if required.

We have initiated a formal national distribution program to attract more distributors to promote the products that we sell. We expect this market segment to contribute significantly to our sales growth over time.

Many customers require their suppliers to have a local presence and Surge's network of independent sales representatives are responsive to these needs. Surge formed a Hong Kong corporation, Surge Components, Limited and hired a regional sales manager to service the Hong Kong/Greater China region customers.

Other marketing efforts include generation and distribution of catalogs and brochures of the products we sell and attendance at trade shows. We have produced an exhibit for display at electronics trade shows throughout the year. The products that we sell have been exhibited at the electronic distribution show in Las Vegas, and we intend to continue our commitment and focus on the distribution segment of the industry by our visibility at the Electronic Distributor Trade Show. In addition, we have updated our website to make it more informative and user friendly. Our search engines have been improved so that customers can find us more easily and we have developed a new portal system to help with lead management and disbursement.

Customers

The products that we sell are sold to distributors and OEMs in such diverse industries as the automotive, computer, communications, cellular telephones, consumer electronics, garage door openers, security equipment, audio equipment, telecomm products, computer related products, power supply products, utility meters and household appliances industries. We request our distributors to provide point of sales reporting, which enables us to gain knowledge of the breakdown of industries into which the products that we sell are sold. One of our customers, , accounted for 13% of net sales for Fiscal 2018, and one of our customers accounted for 12% of net sales for Fiscal 2017. Our discrete components are often sold to the same clients as our capacitors. These OEM customers typically accept samples for evaluation and, if approved, we work towards procuring the next orders for these items.

Typically, we do not maintain contracts with our customers and generally sell products pursuant to customer purchase orders. Although our customer base has increased, the loss of our largest customers as well as, to a lesser extent, the loss of any other material customer, could have a materially adverse effect on our operations during the short-term until we are able to generate replacement business, although we may not be able to obtain such replacement business. Because of our contracts and good working relationships with our distributors, we offer the OEMs, when purchasing through distributors, extended payment terms, just-in- time deliveries and one-stop shopping for many types of electronic products.

Settlement Agreement

On December 22, 2016, the Company entered into a settlement agreement (the “Settlement Agreement”) with Michael D. Tofias and Bradley P. Rexroad (collectively, the “Stockholders”). The Settlement Agreement generally provided that:

the Board and the Stockholders will identify a mutually acceptable independent director to join the Board as a Class C director by February 28, 2017 and the Board will include that new director among its director nominees for the 2017 annual meeting;

the Company will take all steps to (i) change its state of incorporation from the State of Nevada to the State of Delaware and (ii) declassify the Board on a rolling basis by June 30, 2017, and the Company will convene a special meeting of stockholders of the Company for the purpose of approving such actions, at which meeting the Stockholders and the Insiders will vote all of their shares of common stock of the Company in favor of such actions, and

the Company will commence an issuer tender offer to all of its stockholders to repurchase at least 5.0 million shares of its common stock at a price of \$1.43 per share (the “Tender Offer”), which the Company completed in March 2017 whereby it purchased for cash 5,000,000 shares of its common stock, at a price of \$1.43 per share, or \$7,150,000.

the Stockholders will tender all of the shares of common stock of the Company that they hold beneficially or of record in the Tender Offer, subject to limited exceptions; and

the Company's officers and directors will not participate in the Tender Offer and will not transfer or sell any of their shares until six months after the Tender Offer is completed.

Pursuant to the Settlement Agreement, the Company also agreed to reimburse the expenses of the Stockholders associated with their investment in the Company, including their proxy solicitation and litigation costs, in an amount not to exceed \$300,000.

On April 6, 2017, the Board of Directors elected Peter Levy as a Class C Director. He is an independent director.

On October 4, 2018, the Company held its annual meeting of shareholders, at which shareholders approved (i) the change in the Company's state of incorporation from Nevada to Delaware and (ii) the declassification of the Company's board of directors on a rolling basis. No shareholders exercised their dissenters' rights in connection with the reincorporation proposal. The Company was reincorporated in Delaware on February 5, 2019.

Competition

We conduct business in the highly competitive electronic components industry. We expect this industry to remain competitive. We face intense competition in both our selling efforts and purchasing efforts from the many companies that manufacture or distribute electronic components. Our principal competitors in the sale of capacitors include Nichicon, Panasonic, Illinois Capacitor, NIC, AVX, Murata, Epcos, United Chemicon, Rubycon, Vishay and Kemet. Our principal competitors in the sale of discrete components include Vishay, General Semiconductor Division, General Instrument Corp., OnSemi, Inc., Microsemi Corp., Diodes, Inc. and Littlefuse, and Copper Bussman Division. Our principal competition in the audible business include AVX, Murata, Panasonic, Projects Unlimited, International Components Corp. and Star Micronics. Many of these companies are well established with substantial expertise, and have much greater assets and greater financial, marketing, personnel, and other resources than we do. Many larger competing suppliers also carry product lines which we do not carry. Generally, large semiconductor manufacturers and distributors do not focus their direct selling efforts on small to medium sized OEMs and distributors, which constitute many of our customers. As our customers become larger, and as the market becomes more competitive, our competitors may find it beneficial to focus direct selling efforts on those customers, which could result in our facing increased competition, the loss of customers or pressure on our profit margins. We are finding increased competition from manufacturers located in Asia due to the increased globalization nature of the business. There can be no assurance that we will be able to continue to compete effectively with existing or potential competitors. Other factors that will affect our success in these markets include our continued ability to attract additional experienced marketing, sales and management talent, and our ability to expand our support, training and field service capabilities.

Additionally, since the tsunami and earthquake in Japan in 2012, our competitors have established manufacturing facilities in China enabling them to be more competitive by lowering their labor rates and manufacturing costs. Also, as the world continues to become global and customers have easier access to suppliers in Asia, our business could be adversely affected since foreign suppliers are traveling to the United States and interacting with customers more often, where previously they communicated via long-distance. Also, the internet enables customers to meet and interact with suppliers through Google and other search engines which customers had not previously done.

Customer Service

We have customer service employees whose time is dedicated largely to responding to customer inquiries such as price quote requests, delivery status of new or existing purchase orders, changes of existing order dates, quantities, dates, etc. We intend to increase our customer service capabilities, as necessary.

Foreign Trade Regulation

Most products sold by Surge are manufactured in Asia, including such countries as Taiwan, South Korea, Hong Kong, India, Japan and China. The purchase of goods manufactured in foreign countries is subject to a number of risks, including economic disruptions, transportation delays and interruptions, foreign exchange rate fluctuations, impositions of tariffs and import and export controls, and changes in governmental policies, any of which could have a material adverse effect on our business and results of operations. Potential concerns may include drastic devaluation of currencies, loss of supplies and increased competition within the region.

From time to time, protectionist pressures have influenced United States trade policy concerning the imposition of significant duties or other trade restrictions upon foreign products. We cannot predict whether additional United States customs quotas, duties, taxes or other charges or restrictions will be imposed upon the importation of foreign components in the future or what effect such actions could have on our business, financial condition or results of operations.

Our ability to remain competitive with respect to the pricing of imported components could be adversely affected by increases in tariffs or duties, changes in trade treaties, strikes in air or sea transportation, and possible future United States legislation with respect to pricing and import quotas on products from foreign countries. Our ability to remain competitive could also be affected by other governmental actions related to, among other things, anti-dumping legislation and international currency fluctuations. While we do not believe that any of these factors adversely impact our business at the present time, there can be no assurance that these factors will not materially adversely affect us in the future. Since July 2018, when tariffs started to impact some of the Company's sales, the Company has been able to pass on the tariffs to its U.S. and Canadian customers. We have also changed our shipping terms with our Mexico customers to Free Carrier, which means we deliver the goods to the customers' Hong Kong freight forwarder, who then becomes responsible for the transportation and tariff costs. Any significant disruption in the delivery of merchandise from our suppliers, substantially all of whom are foreign, could have a materially adverse impact on our business and results of operations.

Government Regulation

Various laws and regulations relating to safe working conditions, including the Occupational Safety and Health Act, are applicable to our company. We believe we are in substantial compliance with all material federal, state and local laws and regulations regarding safe working conditions. We believe that the cost of compliance with such governmental regulations is not material.

We are subject to the United States Foreign Corrupt Practices Act, which generally prohibits United States companies from engaging in bribery or other prohibited payments to foreign officials for the purpose of obtaining or retaining business. Foreign companies, including some that may compete with us, are not subject to these prohibitions. If our employees or other agents are found to have engaged in such practices, we could suffer severe penalties and other consequences that may have a material adverse effect on our business, financial condition and results of operations. To the Company's knowledge, none of our employees or other agents have engaged in such practices.

The Company has been impacted by the tariffs in effect or being considered by the United States to impose on Chinese goods being imported into the United States, which includes the Company's products. The imposition of such tariffs will likely cause our costs, as well as the prices we charge customers, to increase.

Environmental and Regulatory Compliance

We are subject to various environmental laws and regulations relating to the protection of the environment, including those governing the handling and management of certain chemicals used in electronic components.

We do not believe that compliance with these laws and regulations will have a material adverse effect on our capital expenditures, earnings, or competitive position.

Patents, Trademarks and Proprietary Information

In September 2018, we filed a U.S. patent application with the United States Patent and Trademark Office for an improved pinpoint alarm designed to improve an individual's ability to determine the location of an alarm versus standard single, multi-frequency, or broadband alarms. The improved alarm can be used in a wide variety of applications, including reversing vehicles, medical emergency notification, and hardware devices that use Bluetooth or other wireless communications protocols in combination with mobile software applications to locate lost items, including phones, wallets, and keys. To the best of our knowledge, the manufacturers of the products that we sell do not have patents, trademarks or copyrights registered in the United States Patent and Trademark Office or in any state. We rely on the know-how, experience and capabilities of our management personnel. Although we believe that the products do not and will not infringe patents or trademarks, or violate proprietary rights of others, it is possible that infringement of existing or future patents, trademarks or proprietary rights of others may occur. In the event that the products that we sell infringe proprietary rights of others, these products may have to be modified or redesigned by the manufacturer of these products. However, there can be no assurance that any infringing products will be able to be modified or redesigned in a way that does not infringe on the proprietary rights of others, which could have a material adverse effect upon our operations. In addition, there can be no assurance that we will have the financial or other resources necessary to enforce or defend a patent infringement or proprietary rights violation action. Moreover, if the products we sell infringe patents, trademarks or proprietary rights of others, we could, under certain circumstances, become liable for damages, which also could have a material adverse effect on our business.

Backlog

As of November 30, 2018, our backlog was approximately \$11,294,000, as compared with \$8,189,000 at November 30, 2017. Substantially all backlog is expected to be shipped by us within 180 days of year end. Year to year comparisons of backlog are not necessarily indicative of future operating results.

Employees

As of November 30, 2018, Surge and Challenge employed 36 persons, two of whom are employed in executive capacities, twelve are engaged in sales, three in engineering, two in purchasing, five in administrative capacities, six in customer service, two in accounting and four in warehousing. None of our employees is covered by a collective bargaining agreement, and we consider our relationship with our employees to be good.

Item 1A. Risk Factors

An investment in our common stock involves a high degree of risk. An investor should carefully consider the risks described below as well as other information contained in this annual report on Form 10-K. If any of the following risks actually occur, our business, financial condition or results of operations could be materially adversely affected, the value of our common stock could decline, and an investor may lose all or part of his or her investment.

Risks Related to our Business

We have an agreement with only one of our suppliers and we depend on a limited number of suppliers

We have an agreement with only one of our suppliers (Lelon Electronics), which agreement is terminable by either party upon notice to the other party. Lelon Electronics accounted for approximately 46% and 49% of the Company's consolidated purchases in the years ending November 30, 2018 and November 30, 2017. We also act as the exclusive sales agent in North America for Lelon Electronics. While we believe that we have established close working relationships with our principal suppliers, our success depends, in large part, on maintaining these relationships and developing new supplier relationships for our existing and future product lines. There is no assurance that we will be able to maintain these relationships. While we believe that there are alternative semiconductor and capacitor suppliers whose replacement products may be acceptable to our customers, the loss of, or a significant disruption in the relationship with, one or more of our major suppliers would likely have a material adverse effect on our business and results of operations.

We need to maintain large inventories in order to succeed and as a result, price fluctuations could harm us.

In order to adequately service our customers, we believe that it is necessary to maintain a large inventory of products. Accordingly, we attempt to maintain a one-to-two month inventory of those products which we supply to our customers. As a result of our strategic inventory purchasing policies, under which we order products to obtain preferential pricing, we generally waive the right to manufacturers' inventory protection agreements (including price protection and inventory return rights). As a result, we bear the risk of increases in the prices charged by our manufacturers to the Company and decreases in the prices we are able to charge our customers. If prices of components which we hold in inventory decline or if new technology is developed that displaces products which we sell, our business could be materially adversely affected. Typically the Company has experienced very little impact from customer design changes and slowdown but this can potentially increase due to economic conditions and specific customers business conditions. If our customers experience these changes, our business could be adversely affected.

Our operations would be adversely affected if we lose certain of our customers.

For Fiscal 2018, approximately 11% and 13% of our net sales were derived from sales to two customers. Although our customer base has increased, the loss of our largest customers as well as, to a lesser extent, the loss of any other material customer, would be expected to have a materially adverse effect on our operations until we are able to generate replacement business, although we may not be able to obtain such replacement business.

We may not be able to compete against large competitors who have better resources.

We face intense competition, in both our selling efforts and purchasing efforts, from the many companies that manufacture or distribute electronic components and semiconductors. Our principal competitors in the sale of capacitors include Nichicon, Panasonic, Illinois Capacitor, NIC, AVX, Murata, Epcos, United Chemicon, Rubycon, Vishay and Kemet, General Semiconductor Division, General Instrument Corp., OnSemi, Inc., Microsemi Corp., Diodes, Inc. and Littelfuse, and Copper Bussman Division. Many of these companies are well established with substantial expertise, and have much greater assets and greater financial, marketing, personnel, and other resources than we do. Many larger competing suppliers also carry product lines which we do not carry. Generally, large semiconductor manufacturers and distributors do not focus their direct selling efforts on small to medium sized OEMs and distributors, which constitute most of our customers. As our customers become larger, however, our competitors may find it beneficial to focus direct selling efforts on those customers, which could result in our facing increased competition, the loss of customers or pressure on our profit margins. There can be no assurance that we will be able to continue to compete effectively with existing or potential competitors. The Company periodically introduces new products including most recently, switches.

System failure or cybersecurity breaches of our network security could subject us to increased operating costs, as well as litigation and other potential losses.

The computer systems and network infrastructure that we use could be vulnerable to unforeseen hardware and cybersecurity issues, including “hacking” and “identity theft.” Our operations are dependent upon our ability to protect our computer equipment against damage from fire, power loss, telecommunications failure or a similar catastrophic event. Any damage or failure that causes an interruption in our operations could have an adverse effect on our financial condition and results of operations. In addition, our operations are dependent upon our ability to protect our computer systems and network infrastructure against damage from physical break-ins, cybersecurity breaches and other disruptive problems caused by the Internet or other users. Such computer break-ins and other disruptions would jeopardize the security of information stored in and transmitted through our computer systems and network infrastructure, which may result in significant liability to us and damage our reputation.

Despite efforts to ensure the integrity of our systems, we will not be able to anticipate all security breaches of these types, nor will we be able to implement guaranteed preventive measures against such security breaches. Persistent attackers may succeed in penetrating defenses given enough resources, time and motive. The techniques used by cyber criminals change frequently, may not be recognized until launched and can originate from a wide variety of sources, including outside groups such as external service providers, organized crime affiliates, terrorist organizations or hostile foreign governments.

A successful attack to our system security could cause us serious negative consequences, including significant disruption of operations, misappropriation of confidential information, or damage to our computers or systems or those of our customers. A successful security breach could result in violations of applicable privacy and other laws, financial loss to us or to our customers, loss of confidences in our security measures, significant litigation exposure, and harm to our reputation, all of which could have a material adverse effect on our business and results of operations.

Our business will be adversely affected if there is a shortage of components.

The components business has, from time to time, experienced periods of extreme shortages in product supply, generally as the result of demand exceeding available supply. When these shortages occur, suppliers tend to either increase prices or reduce the number of units sold to customers. We believe that because of our large inventory and our relationships with our manufacturers, we have not been adversely affected by shortages in certain discrete semiconductor components. However, future shortages may have an adverse effect upon our business especially if we were to reduce inventory to cut costs and reduce risks of obsolescence.

Our success depends on key personnel whose continued service is not guaranteed.

Our continued success and our ability to manage anticipated future growth depend, in large part, upon the efforts of key personnel, particularly Ira Levy and Steven Lubman, our chief executive officer and vice president, respectively, who have extensive industry knowledge and relationships and exercise substantial influence over our operations. The loss of services of one or both of these individuals, or our inability to attract and retain highly qualified personnel, could adversely affect our business, and weaken our relationships with suppliers, business partners, and industry personnel, which could adversely affect our financial condition, results of operations, cash flow and trading price of our common stock.

Our business is subject to risks from trade regulation and foreign economic conditions.

Approximately 97% of the total goods which we purchased in Fiscal 2018 were manufactured in foreign countries, with the majority purchased from Taiwan (49%), Hong Kong (18%), elsewhere in Asia (30%) and outside of Asia (less than 1%). These purchases subject us to a number of risks, including economic disruptions, transportation delays and interruptions, foreign exchange rate fluctuations, imposition of tariffs and import and export controls and changes in governmental policies, any of which could have a materially adverse effect on our business and results of operations. Potential concerns may include drastic devaluation of currencies, loss of supplies and increased competition within the region.

The ability to remain competitive with respect to the pricing of imported components could be adversely affected by increases in tariffs or duties, changes in trade treaties, strikes in air or sea transportation, and possible future United States legislation with respect to pricing and import quotas on products from foreign countries. For example, it is possible that political or economic developments in China, or with respect to the United States' relationship with China, could have an adverse effect on our business. Our ability to remain competitive could also be affected by other governmental actions related to, among other things, anti-dumping legislation and international currency fluctuations. While we do not believe that any of these factors have adversely impacted our business in the past, there can be no assurance that these factors will not materially adversely affect us in the future. Because the China internal consumption market is depressed, this will increase competition, as there is now a smaller market potential target. Therefore, we believe certain of our competitors will reduce their pricing to capture more market share.

Electronics industry cyclicalities may adversely affect our operations.

The electronics industry has been affected historically by general economic downturns, which have had an adverse economic effect upon manufacturers and end-users of capacitors and semiconductors. In addition, the life-cycle of existing electronic products and the timing of new product developments and introductions can affect demand for semiconductor components. Any downturns in the electronics distribution industry could adversely affect our business and results of operations.

Our products are not protected by patents, trademarks and proprietary information.

We have no patents, trademarks or copyrights registered in the United States Patent and Trademark Office or in any state. In September 2018, we filed a U.S. patent application for an improved pinpoint alarm designed to improve an individual's ability to determine the location of an alarm versus standard single, multi-frequency, or broadband alarms. The improved alarm can be used in a wide variety of applications, including reversing vehicles, medical emergency notification, and hardware devices that use Bluetooth or other wireless communications protocols in combination with mobile software applications to locate lost items, including phones, wallets, and keys. We rely on the know-how, experience and capabilities of our management personnel. Therefore, without trademark and copyright protection, we have no protection from other parties attempting to offer similar services. Although we believe that the products that we sell do not and will not infringe patents or trademarks, or violate proprietary rights of others, it is possible that infringement of existing or future patents, trademarks or proprietary rights of others may occur. In the event that the products that we sell infringe proprietary rights of others, the manufacturers of the products that we sell may be required to modify the design of the products that we sell, change the name of these products and/or obtain a license. There can be no assurance that the manufacturers will be able to modify or redesign the products in a way that does not infringe on the proprietary rights of others. Our failure to do any of the foregoing could have a material adverse effect upon our operations. In addition, there can be no assurance that we will have the financial or other resources necessary to enforce or defend a patent infringement or proprietary rights violation action. Moreover, if the products that we sell infringe patents, trademarks or proprietary rights of others, we could, under certain circumstances, become liable for damages, which also could have a material adverse effect on our business.

Failure to comply with the United States Foreign Corrupt Practices Act could subject us to penalties and other adverse consequences.

We are subject to the United States Foreign Corrupt Practices Act, which generally prohibits United States companies from engaging in bribery or other prohibited payments to foreign officials for the purpose of obtaining or retaining business. Foreign companies, including some that may compete with us, are not subject to these prohibitions. To our knowledge, none of our employees or other agents have engaged in such practices. However, if our employees or other agents are found to have engaged in such practices, we could suffer severe penalties and other consequences that may have a material adverse effect on our business, financial condition and results of operations.

Risks Related to our Common Stock

Our common stock is quoted on the OTC Pink Market, which may limit the liquidity and price of our common stock more than if our common stock were listed on the Nasdaq Stock Market or another national exchange.

Our securities are currently quoted on the OTC Pink Market, an inter-dealer electronic quotation and trading system for equity securities. Quotation of our securities on the OTC Pink Market may limit the liquidity and price of our securities more than if our securities were listed on The Nasdaq Stock Market or another national exchange. Some investors may perceive our securities to be less attractive because they are traded in the over-the-counter market. In addition, as an OTC quoted company, we do not attract the extensive analyst coverage that accompanies companies listed on national exchanges. Further, institutional and other investors may have investment guidelines that restrict or prohibit investing in securities traded on the OTC Pink Market. These factors may have an adverse impact on the trading and price of our common stock.

The market price of our common stock may fluctuate significantly in response to the following factors, most of which are beyond our control:

variations in our quarterly operating results;

changes in general economic conditions;

changes in market valuations of similar companies;

announcements by us or our competitors of significant new contracts, acquisitions, strategic partnerships or joint ventures, or capital commitments;

loss of a major supplier or customer; and
the addition or loss of key managerial and collaborative personnel.

Any such fluctuations may adversely affect the market price of our common stock, regardless of our actual operating performance. As a result, stockholders may be unable to sell their shares, or may be forced to sell them at a loss.

The application of the “penny stock” rules could adversely affect the market price of our common stock and increase an investor’s transaction costs to sell those shares.

Rule 3a51-1 of the Exchange Act defines “penny stock,” in part, as any equity security that has a market price of less than \$5.00 per share or an exercise price of less than \$5.00 per share, subject to certain exceptions. For any transaction involving a penny stock, unless exempt, Rule 15c-9 of the Exchange Act requires that a broker or dealer:

approve a person’s account for transactions in penny stocks; and
receive from the investor a written agreement to the transaction, setting forth the identity and quantity of the penny stock to be purchased.

In order to approve a person’s account for transactions in penny stocks, the broker or dealer must:

obtain financial information and investment experience and objectives of the person; and
make a reasonable determination that the transactions in penny stocks are suitable for that person and the person has sufficient knowledge and experience in financial matters to be capable of evaluating the risks of transactions in penny stocks.

The broker or dealer must also deliver, prior to any transaction in a penny stock, a disclosure schedule prescribed by the SEC relating to the penny stock market, which:

sets forth the basis on which the broker or dealer made the suitability determination; and

that the broker or dealer received a signed, written agreement from the investor prior to the transaction.

Generally, brokers may be less willing to execute transactions in securities subject to the “penny stock” rules. This may make it more difficult for investors to dispose of our common stock and cause a decline in the market value of our stock.

The market price for our common stock is particularly volatile given our status as a relatively unknown company with a small and thinly traded public float which could lead to wide fluctuations in our share price. Investors may be unable to sell their common stock at or above your purchase price, which may result in substantial losses to investors.

The market for our common stock is characterized by significant price volatility when compared to seasoned issuers, and we expect that our share price will continue to be more volatile than a seasoned issuer for the indefinite future. The volatility in our share price is attributable to a number of factors. First, as noted above, our common stock is sporadically and thinly traded. As a consequence of this lack of liquidity, the trading of relatively small quantities of shares by our shareholders may disproportionately influence the price of those shares in either direction. The price for our shares could, for example, decline precipitously in the event that a large number of our shares of common stock are sold on the market without commensurate demand, as compared to a seasoned issuer which could better absorb those sales without adverse impact on its share price. Secondly, investors may consider us a speculative or risky investment due to the uncertainty of future market acceptance for our potential products. As a consequence of this enhanced risk, more risk-averse investors may, under the fear of losing all or most of their investment in the event of negative news or lack of progress, be more inclined to sell their shares on the market more quickly and at greater discounts than would be the case with the stock of a seasoned issuer. Many of these factors are beyond our control and may decrease the market price of our common stock, regardless of our operating performance. We cannot make any predictions or projections as to the prevailing market price for our common stock at any time, including whether our common stock will sustain its current market price, or the effect that the sale or the availability shares for sale at any time will have on the prevailing market price.

Anti-takeover provisions in our organizational documents and the shareholder rights plan that we have adopted may discourage or prevent a change of control, even if an acquisition would be beneficial to our stockholders, which could affect our stock price adversely and prevent attempts by our stockholders to replace or remove our current management.

Our certificate of incorporation and bylaws currently contain provisions that could delay or prevent a change of control of our company or changes in our Board of Directors that our stockholders might consider favorable. Some of these provisions:

authorize the issuance of preferred stock which can be created and issued by the Board of Directors without prior stockholder approval, with rights senior to those of our common stock;

provide for a classified Board of Directors, with each director serving a staggered three-year term;

prohibit our stockholders from calling special stockholder meetings or taking action by written consent; and

require advance written notice of stockholder proposals and director nominations.

We have also adopted a shareholder rights plan that could make it more difficult for a third party to acquire, or could discourage a third party from acquiring, us or a large block of our common stock. A third party that acquires 5% or more of our common stock could suffer substantial dilution of its ownership interest under the terms of the shareholder rights plan through the issuance of our shares to all stockholders other than the acquiring person. These and other provisions in our certificate of incorporation and bylaws could make it more difficult for stockholders or potential acquirers to obtain control of our Board of Directors or initiate actions that are opposed by our then-current Board of Directors, including a merger, tender offer, or proxy contest involving our company. Any delay or prevention of a change of control transaction or changes in our Board of Directors could cause the market price of our common stock to decline.

Item 1B. Unresolved Staff Comments

Not applicable.

Item 2. Properties.

Our executive offices and warehouse facilities are located at 95 Jefryn Boulevard, Deer Park, New York, 11729. We lease our facilities from Great American Realty of Jefryn Blvd., LLC (“Great American”), an entity that is 50% owned by Ira Levy, Surge’s president and Steven Lubman, Surge’s vice president. Our lease is through September 30, 2020 and our monthly rent for the year ended November 30, 2018 is \$15,211. Our monthly rent will increase over the 10 year term to \$15,516 in the final year. We occupy approximately 23,250 square feet of office space and warehouse space. The rental rate is typical for the type and location of Surge’s and Challenge’s facilities.

In June 2015, the Company renewed its lease to rent office space and a warehouse in Hong Kong for two years and is currently in negotiations to renew the lease. Annual minimum rental payments for this space are approximately \$58,500.

In January 2019, the Company entered into a lease to rent additional warehouse space in Hong Kong for two years. Annual minimum rental payments for this space are approximately \$36,840.

Item 3. Legal Proceedings.

None.

Item 4. Mine Safety Disclosures.

Not applicable.

PART II

Item 5. Market For Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Shares of our common stock are quoted on the OTC Pink Market maintained by OTC Markets Group under the symbol "SPRS". Trading in our common stock is limited. Quotations represent inter-dealer prices without retail mark-up, mark-down, or commission and may not necessarily represent actual transactions.

As of the date of the filing of this report, there are 5,262,128 shares of common stock issued and outstanding.

As of the date of the filing of this report, there are approximately 181 holders of record of our common stock.

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

None.

Equity Compensation Plan Information

The following table provides information as of November 30, 2018 with respect to the shares of common stock that may be issued under our existing equity compensation plans:

| Plan Category | Number of securities to be issued upon exercise of outstanding options, warrants | Weighted-average price of outstanding options, | Number of securities remaining available for future issuance under equity |
|---------------|--|--|---|
|---------------|--|--|---|

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| | and rights (a) | warrants and rights (b) | compensation plans (excluding securities reflected in column (a)) (c) |
|---|-------------------|----------------------------------|---|
| Equity compensation plan approved by security holders (1) | 175,000 | \$ 0.99 | 1,666,859 |
| Equity compensation plan not yet approved by security holders | - | - | - |
| Total | 175,000 | \$ 0.99 | 1,666,859 |

(1) Represents the Company's 2010 Incentive Stock Plan and the Company's 2015 Incentive Stock Plan.

Recent Sales of Unregistered Securities.

None.

Item 6. Selected Financial Data

We are a smaller reporting company and therefore, we are not required to provide information required by this Item of Form 10-K.

Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations

This report contains forward-looking statements. All statements other than statements of historical facts contained herein, including statements regarding our future results of operations and financial position, business strategy and plans and objectives of management for future operations, are forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements.

In some cases, forward-looking statements can be identified by terms such as “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “could,” “intends,” “target,” “projects,” “contemplates,” “believes,” “estimates,” “predicts,” “potential” or “contingent,” and negative of these terms or other similar words. These statements are only predictions. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our business, financial condition and results of operations. We discuss many of the risks in greater detail under the heading “Risk Factors.” Also, these forward-looking statements represent our estimates and assumptions only as of the date of the filing of this report. Except as required by law, we assume no obligation to update any forward-looking statements after the date of the filing of this report.

Overview

The Company operates with two sales groups, Surge Components (“Surge”) and Challenge Electronics (“Challenge”). Surge is a supplier of electronic products and components. These products include capacitors, which are electrical

energy storage devices, and discrete semiconductor components, such as rectifiers, transistors and diodes, which are single function low power semiconductor products that are packaged alone as compared to integrated circuits such as microprocessors. The products sold by Surge are typically utilized in the electronic circuitry of diverse products, including, but not limited to, automobiles, audio products, temperature control products, lighting products, energy related products, computer related products, various types of consumer products, garage door openers, household appliances, power supplies and security equipment. These products are sold to both original equipment manufacturers, commonly referred to as OEMs, who incorporate them into their products, and to distributors of the lines of products we sell, who resell these products within their customer base. These products are manufactured predominantly in Asia by approximately sixteen independent manufacturers. We act as the master distribution agent utilizing independent sales representative organizations in North America to sell and market the products for one such manufacturer pursuant to a written agreement. When we act as a sales agent, our supplier who sold the product to the customer that we introduced to our supplier pays us a commission. The amount of the commission is determined on a sale by sale basis depending on the profit margin of the product. Commission revenue totaled \$48,730 and \$244,631 for the fiscal year ended November 30, 2018 and November 30, 2017 respectively.

Challenge is engaged in the sale of electronic components. In 1999, Challenge began as a division to sell audible components. We have been able to increase the types of products that we sell because some of our suppliers introduced new products, and we also located other products from new suppliers. Our core products include buzzers, speakers, microphones, resonators, alarms, chimes, filters, and discriminators. We now also work with our suppliers to have our suppliers customize many of the products we sell for many customers through the customers' own designs and those that we work with our suppliers to have our suppliers redesign for them at our suppliers' factories. We have an engineer on our staff who works with our suppliers on such redesigns and assists with the introduction of new product lines. We are continually looking to expand the line of products that we sell. We sell these products through independent representatives that earn a commission on the products we sell. We are also working with local, regional, and national distributors to sell these products to local accounts in every state.

The Company has a Hong Kong office to effectively handle the transfer business from United States customers purchasing and manufacturing in Asia after designing the products in the United States. This office has strengthened the Company's global position, improving our capabilities and service to our customer base.

The electronic components industry continues to change, and at this time there is a shortage of certain electronic components in the markets that the Company serves, which may continue through the first half of 2019. The Company believes that this may be a potential opportunity for the Company to achieve business from new customers who are seeking alternative suppliers. Conversely, as our factory lead time has extended, we are now offering less benefits to customers as we had previously done.

The world of business is constantly changing because of "disruptors," which are significant changes in traditional business practices that did not previously exist. For example, customers are moving to centralized purchasing from regional purchasing and are stretching their payment terms. These changes also include customers moving their manufacturing operations from North America to Asia, and the trend of globalization. This trend makes business more complicated and costly for the Company. The Company must have a presence in Asia to service and further develop the business. For these reasons, we established Surge Ltd., our Asia subsidiary. Currency fluctuations also have an effect on doing business outside of North America. Customers have moved to reduce their supply chain, which could adversely affect the Company. In some market segments, demand for electronic components have decreased, and in other segments, the demand is still strong. Some technologies have become obsolete, while customers develop new products using different kinds of components. Management expects 2019 to be a year of change and challenge. These challenges could affect the Company in negative ways, possibly reducing sales and or profitability. In order for the Company to grow, we will depend on, among other things, the continued growth of the electronics and semiconductor industries, our ability to withstand intense price competition, our ability to obtain new customers, our ability to retain and attract sales and other key personnel in order to expand our marketing capabilities, our ability to secure adequate sources of products, which are in demand on commercially reasonable terms, our success in executing and managing growth, including monitoring an expanded level of operations and systems, controlling costs, the availability of adequate financing, and our ability to deal successfully, with new and future disruptors. Another aspect of the electronics industry that has caused disruption and stress is the extended lead time for products in certain categories. Because of this extended lead time, the time from approval to shipping to customers is longer, which may prevent us from increasing our business as quickly as we had done previously. The global economic slowdown, especially in China, is negatively impacting the growth of our customers and many of the manufacturing companies in China.

Critical Accounting Policies

Accounts Receivable

The allowance for doubtful accounts is based on the Company's assessment of the collectability of specific customer accounts and an assessment of international, political and economic risk as well as the aging of the accounts receivable. If there is a change in actual defaults from the Company's historical experience, the Company's estimates of recoverability of amounts due could be affected and the Company would adjust the allowance accordingly.

Revenue Recognition

Revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed and determinable, collectability is reasonably assured and title and risk of loss have been transferred to the customer. This occurs when product is shipped from the Company's warehouse. For direct shipments from our suppliers to our customer, revenue is recognized when product is shipped from the Company's supplier. The Company acts as a sales agent for certain customers buying direct from one of its suppliers. The Company reports these commissions as revenues in the period earned.

The Company performs ongoing credit evaluations of its customers and maintains reserves for potential credit losses.

Inventory Valuation

Inventories are recorded at the lower of cost or market. Write-downs of inventories to market value are based on stock rotation, historical sales requirements and obsolescence as well as in the changes in the backlog. Reserves required for obsolescence were not material in any of the periods in the financial statements presented. If market conditions are less favorable than those projected by management, additional write-downs of inventories could be required. For example, each additional 1% of obsolete inventory would reduce operating income by approximately \$36,000.

The Company does not have price protection agreements with any of its vendors and assumes the risk of changes in the prices of its products. The Company does not believe there to be a significant risk with regards to the lack of price protection agreements as many of its inventory items are purchased to fulfill purchase orders received.

Income Taxes

We have made a number of estimates and assumptions relating to the reporting of a deferred income tax asset to prepare our financial statements in accordance with generally accepted accounting principles. These estimates have a significant impact on our valuation allowance relating to deferred income taxes. Our estimates could materially impact the financial statements.

Results of Operations

Consolidated net sales for the fiscal year ended November 30, 2018 increased by \$2,596,753 or 8.7%, to \$32,372,030 as compared to net sales of \$29,775,277 for the fiscal year ended November 30, 2017. We attribute the increase to an increase in business with new customers as well as additional business with existing customers.

Our gross profit for the fiscal year ended November 30, 2018 increased by \$772,702 to \$8,283,198, or 10.3%, as compared to \$7,510,496 for the fiscal year ended November 30, 2017. Gross margin as a percentage of net sales increased to 25.6% for the fiscal year ended November 30, 2018 compared to 25.2% for the fiscal year ended November 30, 2017. The increase can be attributed to an increase in sales volume as well as certain products being sold at a higher profit margin. Profit margins in 2017 and 2018 have been impacted as a result of certain of our customers, who are some of the biggest buyers of components, demanding the lowest prices for our products. Our industry will continue to receive pressure from customers for price reductions. Some of them further demand periodic price reductions on a quarterly or semi-annual basis, as opposed to annual fixed pricing. We work with electronic manufacturing service subcontractor customers who manufacture products for other customers who do not have their own manufacturing operations. At times we are not able to recover these price reductions from our suppliers. The Company has agreements with these subcontractor customers to provide periodic cost reductions through rebates in the amount of 5%. These reductions only affect future shipments of our products, and do not affect existing orders. These reductions can have a negative impact on our profit margins since they reduce the amount of commissions we can earn. Even though this rebate can impact the Company's gross profit margin, these subcontractor customers represent very significant potential growth for the Company, because they can help the Company become an approved supplier at the customers they manufacture for, and they purchase our components for these customers. We believe it would be very difficult for the Company to achieve business at these customers without the help of these subcontractor customers. During Fiscal 2018, the Company was impacted by tariff costs on certain products imported from China, which went into effect as of July 6, 2018. The Company has been able to pass along a portion of these costs to its customers. The Company is also moving some customer deliveries directly to Hong Kong in order to mitigate some of these costs. In the first half of 2019, the Company expects the effects of the tariffs to be similar to 2018.

Selling and shipping expenses for the fiscal year ended November 30, 2018 was \$2,649,456, an increase of \$121,857, or 4.8%, as compared to \$2,527,599 for the fiscal year ended November 30, 2017. We attribute the increase to increases in selling expenses such as commission expenses, travel and entertainment expenses, and auto expenses, offset by a decrease in freight out and shipping expenses.

General and administrative expenses for the fiscal year ended November 30, 2018 was \$4,069,823, a decrease of \$544,979, or 11.8%, as compared to \$4,614,802 for the fiscal year ended November 30, 2017. The decrease is due primarily to a decrease in legal fees incurred by the Company during the proxy contest and related settlement with certain shareholders of the Company and the completed tender offer in Fiscal 2017. In Fiscal 2018, the Company incurred approximately \$28,000 relating to the proxy contest. In Fiscal 2017, the Company incurred approximately

\$37,000 of expenses during the proxy contest and related settlement with certain shareholders of the Company and approximately \$218,000 for the tender offer completed by the Company in March 2017 and other related expenses. In October 2018, the Company received reimbursement from its insurance carrier in the amount of \$603,362 for a portion of the costs the Company incurred in connection with the proxy contest and related settlement agreement. This amount is included in the Company's consolidated statements of operations as other income. Offsetting increases are due to the hiring of additional employees and increased costs for health insurance, computer and rent expenses as well as increases in general insurance expenses and directors fees, and partially offset by decreases in temporary help expenses, telephone expenses and consulting expenses as well as decreases in dues and utilities. Additionally, general and administrative expenses for the fiscal year ended November 30, 2018 reflect a \$243,000 decrease in legal fees previously incurred by the Company in connection with the proxy contest and the settlement agreement, which was originally recorded as legal fees during the years ended November 30, 2016 and 2017.

Depreciation expense for the fiscal year ended November 30, 2018 was \$48,972, an increase of \$16,858, or 52.5%, as compared to \$32,114 for the fiscal year ended November 30, 2017. The increase is due to the Company purchasing new equipment during the fiscal year ended November 30, 2018.

Other income for the fiscal year ended November 30, 2018 was \$603,367, an increase of \$600,260 compared to \$3,107 for the fiscal year ended November 30, 2017. We attribute the increase to insurance reimbursement of \$603,362 from the settlement and proxy contest, which amount was received in October 2018.

Interest expense for the fiscal year ended November 30, 2018 was \$15,728, a decrease of \$6,715, or 29.9% compared to \$22,443 for the fiscal year ended November 30, 2017. We attribute the decrease to the Company paying down the line of credit during the fiscal year ended November 30, 2018.

Tax expense for the fiscal year ended November 30, 2018 was \$140,992, an increase of \$181,813 as compared to a tax benefit of \$(40,821) for the fiscal year ended November 30, 2017. The changes result from our net income for such periods and management's revised estimate of future taxable income and the related impact on the reported deferred tax. The change in the valuation allowance is based on management estimates of future taxable income. The degree of variability inherent in the estimates of future taxable income is significant and subject to change in the near term. The Company reviews its estimates of future taxable income in each reporting period and adjustments to the valuation allowance are reflected in the current operations.

As a result of the foregoing, net income for the fiscal year ended November 30, 2018 was \$1,961,594, compared to a net income of \$357,466 for the fiscal year ended November 30, 2017.

Liquidity and Capital Resources

As of November 30, 2018 we had cash of \$1,761,863, and working capital of \$5,628,885. We believe that our working capital levels are adequate to meet our operating requirements during the next twelve months.

During the fiscal year ended November 30, 2018, we had net cash flow provided by operating activities of \$1,187,413, as compared to net cash flow provided by operating activities of \$665,920 for the fiscal year ended November 30, 2017. The increase in cash flow from operating activities resulted from an increase in net income, accounts receivable and prepaid expenses, as partially offset by an decrease in cash provided by accrued expenses and accounts payable.

We had net cash flow used in investing activities of \$(26,638) for the fiscal year ended November 30, 2018, as compared to net cash flow used in investing activities of \$(49,522) for the fiscal year ended November 30, 2017. We attribute the change to the Company purchasing less new equipment during the fiscal year ended November 30, 2018.

We had net cash flow used in financing activities of \$(485,911) during the fiscal year ended November 30, 2018 as compared to \$(6,650,000) used in financing activities for the fiscal year ended November 30, 2017. The repayments of \$500,000 of the line of credit reflect the change during the fiscal year ended November 30, 2018. During fiscal year ended November 30, 2017, the Company utilized \$7,150,000 to repurchase common stock in the tender offer as offset by \$500,000 in net borrowing from the line of credit.

As a result of the foregoing, the Company had a net increase in cash of \$674,864 for the fiscal year ended November 30, 2018, as compared to a net decrease in cash of \$6,033,602 for the fiscal year ended November 30, 2017.

In March 2017, the Company completed a tender offer whereby it purchased for cash 5,000,000 shares of its common stock, at a price of \$1.43 per share, or \$7,150,000. In February 2017, the Company obtained a line of credit of up to \$3.0 million for working capital. In March 2017, the Company borrowed \$1,000,000 under the line of credit for working capital purposes and to be repaid out of expected cash flows from operations. The Company subsequently repaid \$1,000,000 under the line of credit and as of November 30, 2018 the balance on the line of credit was \$0. As of November 30, 2018, the Company was in compliance with the covenant for the debt service coverage ratio for the line of credit.

The table below sets forth our contractual obligations, including long-term debt, operating leases and other long-term obligations, as of November 30, 2018:

| | Total | Payments due | | | |
|---------------------------|-----------|------------------|-------------------|-------------------|------------------------------|
| | | 0 – 12 Months | 13 – 36 Months | 37 – 60 Months | More than 60 Months |
| Contractual Obligations | | | | | |
| Capital Lease Obligations | \$32,536 | \$7,036 | \$16,197 | \$9,303 | \$ - |
| Operating leases | \$381,976 | 186,912 | 195,064 | - | - |
| Total obligations | \$414,512 | \$193,948 | \$211,261 | \$9,303 | \$- |

Inflation

In the past two fiscal years, inflation has not had a significant impact on our business. However, any significant increase in inflation and interest rates could have a significant effect on the economy in general and, thereby, could affect our future operating results.

Off Balance Sheet Arrangements

We do not have any off balance sheet arrangements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

We are a smaller reporting company and therefore, we are not required to provide information required by this Item of Form 10-K.

Item 8. Financial Statements and Supplementary Information

Our financial statements, together with the independent registered public accounting firm's report of Seligson & Giannattasio, LLP, begin on page F-1, immediately after the signature page.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

None.

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Item 9A. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures.

We maintain “disclosure controls and procedures,” as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the “Exchange Act”), that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Additionally, in designing disclosure controls and procedures, our management was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

As of November 30, 2018 we carried out an evaluation, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective.

Management’s Report of Internal Control over Financial Reporting.

We are responsible for establishing and maintaining adequate internal control over financial reporting in accordance with Exchange Act Rule 13a-15. With the participation of our Chief Executive Officer and Chief Financial Officer, our management conducted an evaluation of the effectiveness of our internal control over financial reporting as of November 30, 2018 based on the criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that our internal control over financial reporting was effective as of November 30, 2018. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected.

Changes in Internal Controls.

During the quarter ended November 30, 2018, there were no changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rule 13a-15 or Rule 15d-15 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information

None.

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PART III

Item 10. Directors, Executive Officers, and Corporate Governance.

Our board of directors is classified into three classes, with the term of office of one class expiring each year. The term of Class C directors expires at the Company's annual meeting of shareholders to be held in 2020, the term of Class A and Class B directors expires at the Company's next annual meeting of shareholders to be held in 2019, and, commencing at the next annual meeting of shareholders to be held in 2019, each director will be elected for a term of one year to end at the next annual meeting of shareholders.

Our executive officers and directors, and their ages, positions and offices with us are as follows:

| Name | Age | Position |
|---------------------------|-----|--|
| Ira Levy | 62 | Chief Executive Officer, Chief Financial Officer, President and Class A Director |
| Steven J. Lubman | 63 | Vice President, Secretary, Treasurer and Class A Director |
| Alan Plafker* (2)(3) | 60 | Class B Director |
| Martin Novick* (2)(3) | 82 | Class B Director |
| Lawrence Chariton* (2)(3) | 61 | Class C Director |
| Gary Jacobs* (1)(2)(3) | 61 | Class C Director |
| Peter Levy* (1)(2)(3) | 58 | Class C Director |

*Independent director

(1)Member of Compensation Committee.

(2)Member of Audit Committee

(3)Member of Nominating and Corporate Governance Committee

Class A Directors

Ira Levy has served as our President, Chief Executive Officer and director since our inception in November 1981, and as our Chief Financial Officer since March 2010. From 1976 to 1981, Mr. Levy was employed by Capar Components Corp., an importer and supplier of capacitor and resistor products. Mr. Levy has served on the board of trustees of the

Bellmore Jewish Center since 2002 and served as its president from 2006 to 2008. From 2000 to 2004, he served as a member of the board of trustees of METNY, the governing body of the Conservative movement of Judaism for New York, New Jersey, and Connecticut. Mr. Levy studied Business Management at Hofstra University. Mr. Levy's experience in, and knowledge of, the electronics components business led to the conclusion that he should serve on our board.

Steven J. Lubman has served as our Vice President, Secretary and a director since our inception in November 1981. In June 1988, Mr. Lubman founded Challenge Electronics, a division of the Company. From 1980 through 1981, he served as the sales manager for NIC Components Corp., a division of Nu Horizons Electronics Corp., a distributor of electronic components which was acquired by Arrow Electronics, Inc. (NYSE: ARW) in January 2011. From 1976 through 1980, Mr. Lubman served as both an inside and then outside salesperson for Capar Components Corp., a division of Diplomat Electronics Inc., a broad line distributor of electronic components including integrated circuits, diodes, transistors, and capacitor products. Mr. Lubman's more than 35 years of experience in, and knowledge of the electronics components business, led to the conclusion that he should serve on our board.

Class B Directors

Alan Plafker has served as a director since June 2001. Since November 2016, he has served as Vice President of Garber Atlas Fries & Associates, Inc., an insurance agency providing commercial and personal insurance coverage. From July 2000 to November 2016, Mr. Plafker served as President and Chief Executive Officer of Member Brokerage Service LLC, a credit union service organization owned by Melrose Credit Union, and also served as director of business services for the credit union. From January 1993 to July 2000, he served as a member of the credit union's board of directors and supervisory committee. Mr. Plafker has more than 35 years of executive and management experience in the insurance and credit union industries. He is a New York State licensed insurance agent and broker. Mr. Plafker has earned certification as a Certified Professional Insurance Agent from the AIMS Society and earned the CIC designation from the Society of Certified Insurance Counselors. He has also earned the CUBLP (Credit Union Business Lending Professional) designation from the CUNA Business Lending Certification Institute. In addition, he is a past President and currently serves on the Board of Directors of the Professional Insurance Agents Association of New York State, and currently serves as Treasurer and as a member of the Board of Directors for the New York Independent Livery Drivers Benefit Fund, a New York State benefit fund providing injury benefits for livery drivers, to comply with the Workers' Compensation Board regulations. Mr. Plafker received a Bachelor's degree in business administration from Adelphi University. Mr. Plafker's experience in the insurance industry and knowledge of financial matters led to the conclusion that he should serve on our board.

Martin Novick is a real estate investor and was appointed to the Board in September 2016. He served as a vice president of Audiovox Electronic Corp., an international distributor and value-added service provider in the accessory, mobile and consumer electronics industries, from 1969 to 2008. He previously served on the board of directors of Audiovox Electronic Corp., Nu Horizons Electronics Corp., a distributor of electronic components which was acquired by Arrow Electronics, Inc. (NYSE: ARW) in January 2011 and Arielle Electronics, a company that sold bluetooth and wireless products. Mr. Novick holds a Bachelor's Degree in Marketing from New York University. Mr. Novick's significant experience in the electronics industry and as a director of a public company led to the conclusion that he should serve on our board.

Class C Directors

Lawrence Chariton has served as a director since 2001. Since May 2008, he has served as a consultant to Great American Jewelry, a retail jewelry firm. He served for 32 years as Chief Operating Officer of Linda Shop Jewelry, a retail jewelry firm. Since February 2018, Mr. Chariton has served as a member of the Board of Trustees of the State University of Old Westbury in New York. Mr. Chariton previously served as a member of the Board of Directors of New Island Hospital in Bethpage New York and subsequently served as a member of the Board of Directors of St. Joseph's Hospital from February 2007 to December 2010. Mr. Chariton served on the Board of Directors of Jewish National Fund of Long Island. Mr. Chariton has a Bachelor's degree in Accounting from Hofstra University and is a graduate of the Gemological Institute of America in Diamond Grading and Color Essentials. Mr. Chariton's experience running a small business led to the conclusion that he should serve on our board.

Gary M. Jacobs has served as a director since July 2003. Since October 2014, Mr. Jacobs has served as President of Bar Bakers, LLC, a commercial food manufacturer of nutritional bars, cookies and other baked goods. From March 2011 to October 2014, he served as a consultant to several companies, providing advisory services in the areas of turn-around and financial and operational efficiencies. Mr. Jacobs served as the Chief Financial Officer of Chem Rx from June 2008 until March 2011. From May 2005 to June 2008, Mr. Jacobs was the Chief Financial Officer and Chief Operating Officer of Gold Force International, Ltd., a supplier of gold, silver and pearl jewelry to U.S. retail chains, and Karat Platinum LLC, a developer of an alternative to platinum. From July 2003 to April 2005, Mr. Jacobs served as President of The Innovative Companies, LLC, a supplier of natural stone. From October 2001 to February 2003, Mr. Jacobs served as Executive Vice President of Operations and Corporate Secretary of The Hain Celestial Group, Inc., a food and personal care products company. Mr. Jacobs also served as Executive Vice President of Finance, Chief Financial Officer and Treasurer of The Hain Celestial Group, Inc. from September 1998 to October 2001. Prior to that, Mr. Jacobs was the Chief Financial Officer of Graham Field Health Products, Inc., a manufacturing and distribution company. Mr. Jacobs served for 13 years as a member of the audit staff of Ernst & Young LLP, where he attained the position of senior manager. He is a certified public accountant and holds a Bachelor's of Business Administration in Accounting from Adelphi University. Mr. Jacobs's experience as a certified public accountant and as a chief financial officer led to the conclusion that he should serve on our board.

Peter A. Levy has been a director of the Company since April 2017. He is an equity shareholder at the law firm of Mandelbaum Salsburg, one of the region's oldest and most renowned law firms. He joined Mandelbaum as a member in September of 2015. In addition to practicing law for 15 years, Mr. Levy spent 12 years as a partner at a regional accounting firm, Sobel & Company, and has served as the chief operating officer of two different public companies, The Empire Sports & Entertainment and MYOS Corporation. As the president of MYOS Corporation, he successfully positioned the company on the NASDAQ stock exchange. Mr. Levy has significant experience in mergers and acquisitions, joint venture partnering, corporate governance, business processes, and strategic planning. Community service is an important aspect of Mr. Levy's life. For over 20 years he has been on the Board and also served as the Corporate Liaison to Easter Seals – Camp ASCCA, America's flagship camp for People with Disabilities, and he is the co-builder of the Roswal-Levy Tower, the world's largest wheelchair-accessible interactive climbing tower for the disabled. For over a decade, Mr. Levy has been on the Board of Hamp's Camp, a charity founded by former N.Y. Giants running back Rodney Hampton, which is dedicated to providing leadership tools to underprivileged children in

Atlanta, Newark, and Houston. Mr. Levy's financial experience led to the conclusion that he should serve on our board.

The Board has determined that each of Messrs. Chariton, Jacobs, Plafker, Novick and Peter Levy qualify as "independent" under the Nasdaq Stock Market Rules as well as Rule 10A-3 promulgated under the Exchange Act.

Board and Committee Meetings

During the fiscal year ended November 30, 2018, the Board held 4 meetings. Each of the directors attended at least 75% of the aggregate of (i) the total number of meetings of the Board (held during the period for which he served as a director), and (ii) the total number of meetings held by all committees of the Board on which he served (during the periods that he served on such committees). We have no written policy regarding director attendance at annual meetings of stockholders. Our last annual meeting of stockholders was held on October 4, 2018 and all of our directors attended such meeting.

Board Committees

The composition and responsibilities of each of the Audit Committee, the Compensation Committee and the Nominating and Corporate Governance Committee are described below. Members will serve on these committees until their resignation or until otherwise determined by the Board. Each committee operates under a charter that has been approved by the Board, and which is available on our website at <http://www.surgecomponents.com/relations.asp>.

Audit Committee

Our Audit Committee is comprised of Messrs. Chariton, Plafker, Novick, Jacobs and Peter Levy, each of whom is an independent director of the Board. Mr. Jacobs serves as chairman of the Audit Committee. Our Board has determined that Mr. Jacobs is an "audit committee financial expert" as defined in Item 407(d)(5)(ii) of Regulation S-K. The audit committee members are "independent" as that term is defined under the Nasdaq Stock Market Rules. During the fiscal year ended November 30, 2018, the Audit Committee held four meetings.

The Audit Committee is authorized to:

approve and retain the independent auditors to conduct the annual audit of our books and records;

review the proposed scope and results of the audit;

review and pre-approve the independent auditor's audit and non-audit services rendered;

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approve the audit fees to be paid;

review accounting and financial controls with the independent auditors and our financial and accounting staff;

review and approve transactions between us and our directors, officers and affiliates;

recognize and prevent prohibited non-audit services;

establish procedures for complaints received by us regarding accounting matters;

oversee internal audit functions; and

prepare the report of the Audit Committee that SEC rules require to be included in our annual meeting proxy statement.

Compensation Committee

Our Compensation Committee is comprised of Peter Levy and Gary Jacobs, each of whom is an independent director. Mr. Levy serves as chairman of the Compensation Committee. During the fiscal year ended November 30, 2018, the Compensation Committee held one meeting.

The Compensation Committee is authorized to:

review and recommend the compensation arrangements for management, including the compensation for our chief executive officer;

establish and review general compensation policies with the objective of attracting and retaining superior talent, rewarding individual performance and achieving our financial goals;

administer our stock incentive plans; and

prepare the report of the Compensation Committee that SEC rules require to be included in our annual meeting proxy statement.

Nominating and Corporate Governance Committee

Our Nominating and Corporate Governance Committee is comprised of Messrs. Chariton, Plafker Novick, Peter Levy and Jacobs, each of whom is an independent director. Mr. Jacobs serves as chairman of the Nominating and Corporate Governance Committee. The Nominating and Corporate Governance Committee held no meetings during the fiscal year ended November 30, 2018.

The Nominating and Corporate Governance Committee is authorized to:

identify and nominate members of the board of directors;

oversee the evaluation of the board of directors and management;

develop and recommend corporate governance guidelines to the board of directors;

evaluate the performance of the members of the board of directors; and

make recommendations to the board of directors as to the structure, composition and functioning of the board of directors and its committees.

Director Nominations

In evaluating and determining whether to nominate a candidate for a position on the Board, the Nominating and Corporate Governance Committee utilizes a variety of methods and considers criteria such as high professional ethics and values, experience on the policy-making level in business or experience relevant to our product candidates and a commitment to enhancing stockholder value. Candidates may be brought to the attention of the Nominating and Corporate Governance Committee by current Board members, stockholders, officers or other persons. The Nominating and Corporate Governance Committee will review all candidates in the same manner regardless of the source of the recommendation.

We have no formal policy regarding board diversity. Our Nominating and Corporate Governance Committee and Board may therefore consider a broad range of factors relating to the qualifications and background of nominees, which may include diversity, which is not only limited to race, gender or national origin. Our Nominating and Corporate Governance Committee's and Board's priority in selecting board members is identification of persons who will further the interests of our stockholders through his or her established record of professional accomplishment, the ability to contribute positively to the collaborative culture among board members and professional and personal experiences and expertise relevant to our growth strategy.

The Nominating and Corporate Governance Committee also considers stockholder recommendations for director nominees that are properly received in accordance with our Bylaws and applicable rules and regulations of the SEC. In order to validly nominate a candidate for election or reelection as a director, stockholders must give timely notice of such nomination in writing to our Corporate Secretary and include, as to each person whom the stockholder proposes to nominate, all information relating to such person that is required to be disclosed in solicitations of proxies for election of directors in an election contest, or is otherwise required, in each case pursuant to Regulation 14A under the Exchange Act, and the rules and regulations thereunder (including such person's written consent to being named in the proxy statement as a nominee and to serving as a director if elected). For more information on director candidate nominations by stockholders, see "Procedures for Nominating Directors".

Procedures for Nominating Directors

Effective February 5, 2019, the Company began to be governed by newly adopted bylaws (the "Bylaws"). The Bylaws provide, among other things, for advance notice of director nominations.

The exclusive means by which a stockholder may nominate a director is as follows: (i) in the case of the nomination of a director for election at an annual meeting, by delivery of a notice to the secretary of the Company not less than sixty days nor more than ninety days prior to the anniversary of the date on which the Corporation first mailed its proxy materials for the previous year's annual meeting of stockholders (or within a reasonable time before the date on which the Company mails its proxy materials for the current year if during the prior year the Company did not hold an annual meeting); or (ii) in the case of the nomination of a director for election at a special meeting, by delivery of a notice to the secretary not less than sixty days nor more than ninety days prior to such special meeting, in either case setting forth: (a) the name, age, business address and the primary legal residence address of each nominee proposed in such notice, (b) the principal occupation or employment of such nominee, (c) the number of shares of capital stock of the Company which are owned directly or indirectly of record and directly or indirectly beneficially owned by the nominee and each of its affiliates, (d) any material agreements, understandings or relationships, including financial transactions and compensation, between the nominating stockholder and the proposed nominees and (d) such other information concerning each such nominee as would be required, under the rules of the SEC, in a proxy statement soliciting proxies in a contested election of such nominees. Such notice shall include a signed consent of each such nominee to serve as a director of the Company, if elected. In addition, any stockholder nominee, to be validly nominated, is required to submit to the secretary the questionnaire required pursuant to the Bylaws. A stockholder intending to nominate one or more candidates for election as directors must comply with the advance notice bylaw provisions specifically applicable to the nomination of candidates for election as directors for such nomination to be properly brought before the meeting.

To be eligible to be a director nominee nominated by a stockholder or stockholders for election or reelection as a director of the Company, a nominee must deliver (in accordance with the time periods prescribed for delivery of notice under Section 2.6.2 of the Bylaws) to the secretary a written questionnaire (the "Questionnaire") with respect to the background, qualification and experience of such person and the background of any other person or entity on

whose behalf the nomination is being made and a written representation and agreement that such person: (a) will abide by the requirements of the Bylaws and the Company's certificate of incorporation as in effect at the time of their nomination and as validly amended, (b) is not and will not become a party to (1) any agreement, arrangement or understanding with, and has not given any commitment or assurance to, any person or entity as to how such person, if elected as a director of the Company, will act or vote on any issue or question (a "Voting Commitment") that has not been disclosed to the Company or (2) any Voting Commitment that could limit or interfere with such person's ability to comply, if elected as a director of the Company, with such person's fiduciary duties under applicable law, (c) is not and will not become a party to any agreement, arrangement or understanding with any person or entity other than the Company with respect to any direct or indirect compensation, reimbursement or indemnification in connection with service or action as a director that has not been disclosed therein, and (d) in such person's individual capacity and on behalf of any person or entity on whose behalf the nomination is being made, would be in compliance, if elected as a director of the Company, and will comply with all applicable publicly disclosed corporate governance, conflict of interest, confidentiality and stock ownership and trading policies and guidelines of the Company. If, prior to the meeting, there is a change or inaccuracy in any information set forth on the Questionnaire, then the director candidate must promptly notify the secretary by submitting in writing a revised Questionnaire. If a nominee fails to provide such Questionnaire, revised Questionnaire or representation and agreement in accordance with the above, the information may be deemed by the Board of Directors in its discretion not to have been provided in accordance with the Bylaws and such nominee may be disqualified as a director nominee by the Board of Directors in its discretion.

In addition to all other requirements set forth in the Bylaws, a nominating stockholder (including its affiliates) and each director nominee must also comply with all applicable requirements of state law and of the Exchange Act and the rules and regulations thereunder with respect to the matters set forth in the Bylaws.

Board Leadership Structure and Role in Risk Oversight

Although we have not adopted a formal policy on whether the Chairman and Chief Executive Officer positions should be separate or combined, we have traditionally determined that it is in our best interests and in the best interests of our stockholders to combine these roles. Mr. Levy has served as our Chairman since November 1981. Due to our small size, we believe it is currently most effective to have the Chairman and Chief Executive Officer positions combined.

Our board of directors is primarily responsible for overseeing our risk management processes. The Board receives and reviews periodic reports from management, auditors, legal counsel, and others, as considered appropriate regarding our assessment of risks. The Board focuses on the most significant risks facing us and our general risk management strategy, and also ensures that risks undertaken by management are consistent with the board's appetite for risk. While the Board oversees our risk management, management is responsible for day-to-day risk management processes. We believe this division of responsibilities is the most effective approach for addressing the risks facing us and that our board leadership structure supports this approach.

Code of Ethics

We have adopted a code of ethics that applies to our officers, directors and employees. A copy of the code of ethics is accessible on our website at <http://www.surgecomponents.com/relations.asp>. Additional copies of the code of ethics may be obtained without charge, from us by writing or calling: 95 East Jefryn Blvd., Deer Park, New York 11729, Attention: Corporate Secretary, Telephone: (631) 595-1818.

Stockholder Communications with the Board

Stockholders who wish to do so may communicate directly with the Board or specified individual directors by writing to:

Board of Directors (or name of individual director)

c/o Corporate Secretary

Surge Components, Inc.

95 East Jefryn Blvd.

Deer Park, New York 11729

The Board of Directors maintains a process for stockholders or other interested parties to communicate with the Board or any Board member. Stockholders or interested parties who desire to communicate with the Board should send any communication to the Company's Corporate Secretary, Surge Components, Inc., 95 East Jefryn Blvd., Deer Park, New York 11729. We will forward all communications from security holders and interested parties to the full Board, to non-management directors, to an individual director or to the chairperson of the Board committee that is most closely related to the subject matter of the communication, except for the following types of communications: (i) communications that advocate that we engage in illegal activity; (ii) communications that, under community standards, contain offensive or abusive content; (iii) communications that have no relevance to our business or operations; and (iv) mass mailings, solicitations and advertisements. The Corporate Secretary will determine when a communication is not to be forwarded. Our acceptance and forwarding of communications to directors does not imply that directors owe or assume any fiduciary duties to persons submitting the communications.

Additionally, the Audit Committee has established procedures for the receipt, retention and confidential treatment of complaints received by Surge regarding accounting, internal accounting controls or auditing matters, including procedures for confidential, anonymous submissions by employees with respect to such matters. Employees and stockholders may raise a question or concern to the Audit Committee regarding accounting, internal accounting controls or auditing matters by writing to:

Chairman, Audit Committee

c/o Corporate Secretary

Surge Components, Inc.

95 East Jefryn Blvd.

Deer Park, New York 11729

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934 requires that our officers and directors, and persons who own more than ten percent of a registered class of our equity securities, file reports of ownership and changes in ownership with the Securities and Exchange Commission. Officers, directors and persons owning more than ten percent of such securities are required by Commission regulation to file with the Commission and furnish the Company with copies of all reports required under Section 16(a) of the Exchange Act. To our knowledge, based solely upon our review of the copies of such reports furnished to us, during the fiscal year ended November 30, 2018, all Section 16(a) filing requirements applicable to our officers, directors and greater than 10% beneficial owners were complied with the exception of one late Form 4 for Mr. Plafker.

Item 11. Executive Compensation.**Summary Compensation Table**

The following table sets forth information regarding compensation paid to our executive officers for the years ended November 30, 2018 and November 30, 2017:

| Name and Position | Fiscal Year | Salary (\$) | Bonus (\$) | Stock Awards (\$) | Option Awards (\$) | All Other Compensation (\$)(1) | Total (\$) |
|------------------------------|-------------|----------------|---------------|-------------------------|--------------------------|--------------------------------------|---------------|
| Ira Levy | 2018 | 275,000 | 137,500 | - | - | 56,038 | 468,538 |
| President CEO and CFO | 2017 | 275,000 | 168,375 | - | - | 53,872 | 497,247 |
| Steven J. Lubman | 2018 | 225,000 | 100,000 | - | - | 47,143 | 372,143 |
| Vice President and Secretary | 2017 | 225,000 | 142,670 | - | - | 43,975 | 411,645 |

(1) Amounts in this column include payments for medical insurance, automobile allowance and life and personal insurance. With respect to Fiscal 2018, the amounts were comprised of the following items:

| | Medical Insurance | Automobile Allowances | Life and Personal Insurance |
|------------------|----------------------|--------------------------|-----------------------------------|
| Ira Levy | \$ 27,968 | \$ 19,832 | \$ 8,238 |
| Steven J. Lubman | \$ 27,968 | \$ 11,400 | \$ 7,775 |

2018 Base Salary and Bonus

In February 2016, the Company entered into revised employment agreements with two officers of the Company. Pursuant to these agreements, the base salary for one officer is \$275,000 and the base salary for the other officer is \$225,000. The agreements continue until terminated by either party.

The Company's compensation committee may award these officers with bonuses and will review the base salary amounts for each of the officers on an annual basis to determine if any changes to the base salary amounts need to be

made. Pursuant to the employment agreements, the officers are prohibited from engaging in activities which are competitive with those of the Company during their employment with the Company and for one year following termination. If the agreement is terminated other than for cause, the officer would be entitled to all base salary earned through the date of termination, accrued but unused vacation, all vested equity, and bonus amounts payable to the officer through the date of termination. The officers would also be entitled to receive an additional thirty-six months of annual compensation equal to the average of his base salary and bonus for the three calendar years prior to the date of termination, payable in accordance with the Company's regular payroll practice over a 52-week period.

The bonus granted to the named executive officers in 2018 was based on certain performance goals that were set prior to the year by the Compensation Committee and the executive, but ultimately the bonus is discretionary, as the Compensation Committee has the authority to make all final decisions regarding the amount and form of bonuses provided to the executive officers. For Mr. Levy, his target bonus amount is equal to fifty percent (50%) of his base salary, and Mr. Lubman's target is equal to forty-five percent (45%) of his base salary.

In 2018 the Compensation Committee used four performance markers to guide their decisions regarding bonus amounts. The performance guidelines that were applicable to Messrs. Levy and Lubman's bonuses for the 2018 year included individual performance goals, revenue growth, achieving the operating plan goals for specific divisions of the company, and achieving the operating plan for the company as a whole. Each performance guideline was generally intended to make up twenty-five percent of the potential bonus amount for each executive. Based upon the Company's and the executives' performance during the 2018 year, the Compensation Committee granted awards that were approximately one hundred percent (100%) of the executives' target award amount.

2018 Equity Compensation Awards

We have historically granted fully vested stock awards and stock option awards. The amount of awards granted in any given year is determined based on the performance of the company and the executive in the previous year. Performance is generally based upon the same performance guidelines that are used for the annual cash bonus award for that year. The Compensation Committee sets a target award amount based upon a percentage of the executive's base salary. At the end of the year, the Compensation Committee determines the cash amount that resulted from the previous year's performance, with any discretionary adjustments that the Compensation Committee deems to be appropriate, and converts that cash amount into a number of shares of stock awards or stock option awards, as applicable.

With respect to the 2018 year, no equity awards were granted by the Compensation Committee.

Employment Agreements

In February 2016, the Company entered into revised employment agreements (the "Levy Agreement" and the "Lubman Agreement", individually, and collectively, the "Employment Agreements") with Ira Levy and Steven Lubman, respectively, which provides the executives with a base salary of \$275,000 and \$225,000, respectively ("Base Salary"). The executives shall receive an annual bonus as shall be determined by the Board or the Compensation Committee, as applicable, in its sole discretion, based upon criteria to be established in its sole discretion. The executives shall also be entitled to receive additional cash, equity or other compensation or benefits in consideration for their services to the

Company, at such times and in such amounts as shall be determined in the sole discretion of the Board or the Compensation Committee. In addition, the executives shall be entitled to receive grants of stock options, stock and/or any other equity incentive awards available to senior executives, under the Company's equity incentive plans, at such times and in such amounts as shall be determined in the sole discretion of the Board or the Compensation Committee.

The Employment Agreements will remain in effect until terminated by either the Company or the executive. In the event an executive's employment is terminated by the Company for Cause (as defined in the Employment Agreements), or if an executive resigns other than for Good Reason (as defined in the Employment Agreements), he shall be entitled to receive (i) any earned but unpaid salary, all vested equity, and any earned but unpaid bonus awards through the date of termination, and (ii) reimbursement for any unreimbursed business expenses incurred by him in accordance with the Company's policy prior to the date of termination.

In the event an executive's employment is terminated by the Company other than for Cause or if an executive resigns for Good Reason, including a Change of Control (as defined in the Employment Agreements) that is accompanied by the executive's resignation within a twelve month period following that Change of Control, such executive shall be entitled to any earned but unpaid salary, all vested equity, and any earned but unpaid bonus awards through the date of termination. Such executive will also be paid an additional thirty-six months of annual compensation equal to the average of his base salary and bonus for the three calendar years prior to the date of termination, payable in accordance with the Company's regular payroll practice over a 52-week period. The Company shall also (i) accelerate the vesting on any of the executive's unvested stock options, restricted stock grants or other equity incentive awards; and (ii) reimburse the executive for any unreimbursed business expenses incurred by him in accordance with the Company's policy prior to the date of termination. In the event that the executive is terminated without Cause due to our inability to pay our debts when they generally become due, we will not be liable for the cash severance payments or the payment of annual bonuses due to the executive. The severance benefits potentially payable upon a termination other than for Cause or for Good Reason will be provided subject to the executive signing a general release of claims in our favor prior to payment.

In the event an executive's employment is terminated by the Company upon death or disability, the executive or his estate shall be entitled to receive his salary then in effect along with all other fringe benefits (including, without limitation, family medical benefits) for a period of one year following the date of such termination. In addition, the executive or his estate shall have the right to exercise any unexercised and vested options for a period of ninety days following the date of termination and to receive payment for any accrued but unpaid vacation time.

The Employment Agreements contain customary non-competition and non-solicitation provisions that extend to one year after the date of termination of the executives' employment with the Company. The executives also agreed to customary terms regarding confidentiality and ownership of product ideas.

Outstanding Equity Awards at November 30, 2018

| Name | Number of securities underlying options, Unexercisable (#) | Number of Securities Underlying Unexercised Options, Exercisable (#) | Option Exercise Price (\$) | Option Expiration Date |
|---------------|--|--|----------------------------|------------------------|
| Ira Levy | - | - | - | |
| Steven Lubman | - | - | - | |

Director Compensation for Year Ending November 30, 2018

The following table summarizes the compensation for our non-employee board of directors for the fiscal year ended November 30, 2018. All compensation paid to our employee directors is included under the summary compensation table above. With respect to the 2018 fiscal year, the director compensation program consisted of a monthly cash fee of \$2,500 per month, with the amount increased to \$3,500 per month for a non-employee director that serves as the chairman of more than two committees on the Board of Directors. The non-employee directors are also eligible to receive equity awards, although there is no annual target amount set for the non-employee directors.

| Name | Fees Earned or Paid in Cash (\$) | Option Awards (\$) ⁽¹⁾ | Total (\$) |
|-------------------|----------------------------------|-----------------------------------|------------|
| Alan Plafker | 30,000 | - | 30,000 |
| Martin Novick | 30,000 | - | 30,000 |
| Lawrence Chariton | 30,000 | - | 30,000 |
| Gary Jacobs | 42,000 | - | 42,000 |
| Peter Levy | 30,000 | - | 30,000 |

Amounts in this column reflect the grant date value of the option awards granted to each of the directors in accordance with Topic 718, disregarding any estimates of forfeitures. Further details of the methods and assumptions used for purposes of valuing these awards are included in Note H of the Notes to Consolidated Financial Statements in this Annual Report. As of November 30, 2018, Messrs. Plafker and Chariton each held 25,000 shares of unexercised but vested stock option awards, and Mr. Jacobs held 50,000 shares of unexercised but vested stock option awards.

Item 12. Security Ownership of Certain Beneficial Owners and Management.

Under Rule 13d-3, a beneficial owner of a security includes any person who, directly or indirectly, through any contract, arrangement, understanding, relationship, or otherwise has or shares: (i) voting power, which includes the power to vote, or to direct the voting of shares; and (ii) investment power, which includes the power to dispose or direct the disposition of shares. Certain shares may be deemed to be beneficially owned by more than one person (if, for example, persons share the power to vote or the power to dispose of the shares). In addition, shares are deemed to be beneficially owned by a person if the person has the right to acquire the shares (for example, upon exercise of an option) within 60 days of the date as of which the information is provided. In computing the percentage ownership of any person, the amount of shares outstanding is deemed to include the amount of shares beneficially owned by such person (and only such person) by reason of these acquisition rights.

The following table sets forth as of February 22, 2019, information regarding the beneficial ownership of our common stock by: (i) each person known by the Company to be the beneficial owner of than five percent of the outstanding shares of common stock, (ii) each of our directors and officers and (iii) all officers and directors, as a group:

| Name and address of Beneficial Owner ⁽¹⁾ | Amount and Nature of Common Stock Beneficially Owned | Percentage of Common Stock Beneficially Owned ⁽²⁾ | |
|---|--|--|---|
| Ira Levy | 1,170,299 | 22.2 | % |
| Steven J. Lubman | 970,108 | 18.4 | % |
| Lawrence Chariton | 157,573 (3) | 3.00 | % |
| Alan Plafker | 33,197 (3) | - | |
| Martin Novick | - | - | |
| Gary Jacobs | 112,000 (4) | 2.11 | % |
| Peter Levy | - | - | |
| All directors and executive officers as a group (7 persons) | 2,443,177 | 45.6 | % |

*Less than 1%

- (1) Except as otherwise indicated, the address of each beneficial owner is c/o Surge Components, Inc., 95 East Jefryn Boulevard, Deer Park, NY 11729.
- (2) Applicable percentage ownership is based on 5,262,128 shares of common stock outstanding as of February 26, 2019.
- (3) Includes 25,000 shares issuable upon exercise of options with an exercise price of \$0.87, which are exercisable within 60 days.
- (4) Includes 50,000 shares issuable upon exercise of options with an exercise price of \$0.87, which are exercisable within 60 days.

Item 13. Certain Relationships And Related Transactions, and Director Independence.

Certain Relationships and Related Transactions

Surge and Challenge each lease their current executive offices from Great American Realty of Jefryn Blvd., LLC, an entity owned 50% by Ira Levy, our Chief Executive Officer, and President and Steven Lubman, our Vice President, Secretary and Treasurer. Our lease is through September 2020 and our annual rent payments were approximately \$260,241 and \$256,721 for Fiscal 2018 and Fiscal 2017, respectively.

Item 14. Principal Accounting Fees And Services

Fees Billed by Our Independent Registered Public Accounting Firm During Fiscal 2017 and 2018

The following table sets forth the aggregate fees billed to us for the fiscal years ended November 30, 2017 and 2018 by Seligson & Giannattasio, LLP:

| | 2017 | 2018 |
|---------------------------|------------|------------|
| Audit Fees ⁽¹⁾ | \$ 151,000 | \$ 172,500 |
| Tax Fees ⁽²⁾ | \$ 12,000 | \$ 12,000 |

Audit Fees represent the aggregate fees for professional services for the audit of our annual financial statements (1) and review of financial statements included in our quarterly reports on Form 10-Q or services that are normally provided in connection with statutory and regulatory filings or engagements for those fiscal years.

(2) Tax fees represent the aggregate fees billed for tax compliance, tax advice, and tax planning.

Audit Committee Pre-Approval Policies and Procedures

Pursuant to its charter, the Audit Committee is responsible for the pre-approval of all audit and permissible non-audit services provided by our principal independent accountants on a case-by-case basis. Our Audit Committee has established a policy regarding approval of all audit and permissible non-audit services provided by our principal

independent accountants. Our Audit Committee pre-approves these services by category and service. Our Audit Committee has preapproved all of the services provided by our principal independent accountants in the fiscal year ending November 30, 2018.

PART IV

Item 15. Exhibits and Financial Statement Schedules.

The following documents are filed as a part of this report or incorporated herein by reference:

1. Our Consolidated Financial Statements commencing on page F-1 of this Annual Report.
2. Exhibits:

The following documents are included as exhibits to this Annual Report:

| Exhibit Number | Description |
|----------------|---|
| 3.1 | <u>Certificate of Incorporation of Surge Components, Inc. (filed as exhibit 3.3 to Form 8-K filed on February 11, 2019 and incorporated herein by reference)</u> |
| 3.2 | <u>Bylaws of Surge Components, Inc. (filed as exhibit 3.4 to Form 8-K filed on February 11, 2019 and incorporated herein by reference)</u> |
| 4.1 | <u>Rights Agreement dated as of October 7, 2016 between Surge Components, Inc., as the Company, and Continental Stock Transfer & Trust Company, as Rights Agent (filed as exhibit to Form 8-K filed on October 7, 2016 and incorporated herein by reference).</u> |
| 10.1 | <u>Lease between Surge Components and Great American Realty of 95 Jefryn Blvd., LLC (filed as exhibit to Amendment No. 1 to Form 10 filed on August 20, 2010 and incorporated herein by reference)</u> |
| 10.2 | <u>Lease between Challenge Electronics and Great American Realty of 95 Jefryn Blvd., LLC (filed as exhibit to Amendment No. 1 to Form 10 filed on August 20, 2010 and incorporated herein by reference)</u> |
| 10.3 | <u>Employment Agreement between Surge Components, Inc. and Ira Levy (filed as exhibit to Form 8-K filed on February 24, 2016 and incorporated herein by reference)</u> |
| 10.4 | <u>Employment Agreement between Surge Components Inc. and Steven Lubman (filed as exhibit to Form 8-K filed on February 24, 2016 and incorporated herein by reference)</u> |

- 10.5 Declaration of Trust (filed as exhibit to Amendment No. 1 to Form 10 filed on August 20, 2010 and incorporated herein by reference)
- 10.6 2010 Incentive Stock Plan (filed as exhibit to Amendment No. 2 to Form 10 filed on November 4, 2010 and incorporated herein by reference)
- 10.7 2015 Incentive Stock Plan (filed as exhibit to Form 10-K filed on February 26, 2016 and incorporated herein by reference)
- 10.8 Lease Agreement, dated October 1, 2010, between Great American Realty of Jefryn Boulevard, LLC and Surge Components, Inc. (filed as exhibit to Amendment No. 2 to Form 10 filed on November 4, 2010 and incorporated herein by reference)
- 10.9 Lease Agreement, dated October 1, 2010, between Great American Realty of Jefryn Boulevard, LLC and Challenge Electronics, Inc. (filed as exhibit to Amendment No. 2 to Form 10 filed on November 4, 2010 and incorporated herein by reference)
- 10.10 Agreement, dated March 18, 1999 between Surge Components, Inc. and Future Electronics Incorporated (filed as exhibit to Amendment No. 3 to Form 10 filed on January 11, 2011 and incorporated herein by reference)
- 10.11 Addendum A, dated March 18, 1999, between Surge Components, Inc. and Future Electronics (filed as exhibit to Amendment No. 3 to Form 10 filed on January 11, 2011 and incorporated herein by reference)
- 10.12 Agreement, dated October 21, 2009, between Challenge Electronics, Inc. and Cam RPC Electronics (filed as exhibit to Amendment No. 3 to Form 10 filed on January 11, 2011 and incorporated herein by reference)

| Exhibit Number | Description |
|----------------|---|
| 10.13 | <u>Agreement, dated October 21, 2009, between Challenge Electronics, Inc. and Nu-Way Electronics (filed as exhibit to Amendment No. 3 to Form 10 filed on January 11, 2011 and incorporated herein by reference)</u> |
| 10.14 | <u>Agreement, dated October 19, 2009 between Challenge Electronics, Inc. and Aesco Electronics (filed as exhibit to Amendment No. 3 to Form 10 filed on January 11, 2011 and incorporated herein by reference)</u> |
| 10.15 | <u>Agreement, dated May 5, 2009, between Challenge Electronics, Inc. and TLC Electronics, Inc. (filed as exhibit to Amendment No. 3 to Form 10 filed on January 11, 2011 and incorporated herein by reference)</u> |
| 10.16 | <u>Distributor Agreement, dated August 14, 2012, between Surge Components, Inc. and TTI, Inc. (filed as exhibit to Form 10-K filed on February 28, 2013 and incorporated herein by reference)</u> |
| 10.17 | <u>Sole Agent Agreement, dated January 1, 2007, between Surge Components, Inc. and Lelon Electronics (filed as exhibit to Form 10-K filed on February 28, 2012 and incorporated herein by reference)</u> |
| 10.18 | <u>Master Distributor Agreement, dated February 7, 2011, between Surge Components, Inc. and Avnet, Inc. (filed as exhibit to Form 10-K filed on February 28, 2012 and incorporated herein by reference)</u> |
| 10.19 | <u>First Amendment to Master Distributor Agreement, dated February 17, 2011, between Surge Components, Inc. and Avnet, Inc. (filed as exhibit to Form 10-K filed on February 28, 2012 and incorporated herein by reference)</u> |
| 10.20 | <u>Rental Agreement with Adcock Investment Company Limited dated May 5, 2013 (filed as exhibit to Form 10-Q filed on July 15, 2013 and incorporated herein by reference)</u> |
| 10.21 | <u>Settlement Agreement, dated as of December 22, 2016, by and among Surge Components, Inc., Ira Levy, Steven J. Lubman, Alan Plafker, Lawrence Chariton, Gary Jacobs and Martin Novick, and Messrs. Michael D. Tofias and Bradley P. Rexroad (filed as exhibit to Form 8-K filed on December 23, 2016 and incorporated herein by reference).</u> |
| 10.22 | <u>Amendment to Settlement Agreement, dated as of August 16, 2018, by and among Surge Components, Inc., Ira Levy, Steven J. Lubman, Alan Plafker, Lawrence Chariton, Gary Jacobs and Martin Novick, and Messrs. Michael D. Tofias and Bradley P. Rexroad (filed as exhibit 10.1 to Form 8-K filed on August 22, 2018 and incorporated herein by reference).</u> |
| 21.1 | <u>Subsidiaries (filed as exhibit to Amendment No. 1 to Form 10 filed on August 20, 2010 and incorporated herein by reference)</u> |
| 23.1 | <u>Consent of Seligson & Giannattasio, Independent Registered Public Accounting Firm</u> |
| 31 | <u>Certification of principal executive officer and principal financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u> |

32 Certification of principal executive officer and principal financial officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101.INS XBRL Instance Document

101.SCH XBRL Taxonomy Extension Schema Document

101.CAL XBRL Taxonomy Extension Calculation Linkbase Document

101.DEF XBRL Taxonomy Extension Definition Linkbase Document

101.LAB XBRL Taxonomy Extension Label Linkbase Document

101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

Item 16. Form 10-K Summary.

None.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SURGE COMPONENTS, INC.

Date: February 28, 2019 By: /s/ Ira Levy
Ira Levy
Chief Executive Officer and Chief Financial Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

/s/ Ira Levy
Ira Levy
Chief Executive Officer, Chief Financial Officer and
Chairman of the Board (Principal Executive Officer,
Principal Financial Officer and Principal Accounting Officer) February 28, 2019

/s/ Steven J. Lubman
Steven J. Lubman
Vice President, Secretary, Treasurer and Director February 28, 2019

/s/ Alan Plafker
Alan Plafker
Director February 28, 2019

/s/ Martin Novick
Martin Novick
Director February 28, 2019

/s/ Lawrence Chariton
Lawrence Chariton
Director February 28, 2019

/s/ Peter A. Levy
Peter A. Levy
Director February 28, 2019

/s/ Gary M. Jacobs
Gary M. Jacobs
Director

February 28, 2019

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and
Stockholders of Surge Components, Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Surge Components, Inc. and subsidiaries (the “Company”) as of November 30, 2018 and 2017, and the related consolidated statements of operations, shareholders’ equity, and cash flows for each of the years in the two-year period ended November 30, 2018, and the related notes (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of November 30, 2018 and 2017, and the results of its operations and its cash flows for each of the years in the two-year period ended November 30, 2018, in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits, we are required to obtain an understanding of internal control over financial reporting, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also

included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Seligson & Giannattasio, LLP

We have served as the Company's auditor since 2002.

White Plains, New York

February 28, 2019

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SURGE COMPONENTS, INC. AND SUBSIDIARIES

Consolidated Balance Sheets

| | November 30, 2018 | November 30, 2017 |
|--|----------------------|----------------------|
| ASSETS | | |
| Current assets: | | |
| Cash | \$ 1,761,863 | \$ 1,086,999 |
| Accounts receivable - net of allowance for doubtful accounts of \$161,560 | 5,997,493 | 5,933,268 |
| Inventory, net | 3,389,065 | 3,161,587 |
| Prepaid expenses and income taxes | 19,589 | 158,869 |
| Deferred income taxes | - | 327,627 |
| Total current assets | 11,168,010 | 10,668,350 |
| Fixed assets – net of accumulated depreciation and amortization of \$2,266,627 and \$2,217,654 | 115,995 | 138,329 |
| Deferred income taxes | 982,624 | 655,253 |
| Other assets | 13,384 | 13,384 |
| Total assets | \$ 12,280,013 | \$ 11,475,316 |

See notes to consolidated financial statements

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Consolidated Balance Sheets

(Continued)

| | November 30, 2018 | November 30, 2017 |
|---|----------------------|----------------------|
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 4,420,013 | \$ 4,629,932 |
| Loan payable | - | 500,000 |
| Capital lease payable, current maturities | 7,036 | 6,411 |
| Accrued expenses and taxes | 603,203 | 937,249 |
| Accrued salaries | 508,873 | 621,930 |
| Total current liabilities | 5,539,125 | 6,695,522 |
| Capital lease payable, net of current maturities | 25,500 | 32,536 |
| Deferred rent | 25,554 | 34,518 |
| Total liabilities | 5,590,179 | 6,762,576 |
| Commitments and contingencies | | |
| Shareholders' equity: | | |
| Preferred stock - \$.001 par value, 5,000,000 shares authorized: | | |
| Series C—100,000 shares authorized, 10,000 and 10,000 shares issued and outstanding, redeemable, convertible, and a liquidation preference of \$5 per share | 10 | 10 |
| Series D – 75,000 shares authorized, none issued or outstanding, voting, convertible, redeemable. | | |
| Common stock - \$.001 par value, 50,000,000 shares authorized, 5,262,128 and 5,224,431 shares issued and outstanding | 5,262 | 5,224 |
| Additional paid-in capital | 16,577,772 | 16,557,310 |
| Accumulated deficit | (9,893,210) | (11,849,804) |
| Total shareholders' equity | 6,689,834 | 4,712,740 |
| Total liabilities and shareholders' equity | \$ 12,280,013 | \$ 11,475,316 |

See notes to consolidated financial statements.

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SURGE COMPONENTS, INC. AND SUBSIDIARIES

Consolidated Statements of Operations

| | Year Ended November 30, | |
|--|----------------------------|--------------|
| | 2018 | 2017 |
| Net sales | \$32,372,030 | \$29,775,277 |
| Cost of goods sold | 24,088,832 | 22,264,781 |
| Gross profit | 8,283,198 | 7,510,496 |
| Operating expenses: | | |
| Selling and shipping expenses | 2,649,456 | 2,527,599 |
| General and administrative expenses | 4,069,823 | 4,614,802 |
| Depreciation and amortization | 48,972 | 32,114 |
| Total operating expenses | 6,768,251 | 7,174,515 |
| Income before other income and income taxes | 1,514,947 | 335,981 |
| Other (expense) income : | | |
| Interest expense | (15,728) | (22,443) |
| Other income including insurance recovery | 603,367 | 3,107 |
| Other income (expense) : | 587,639 | (19,336) |
| Income before income taxes | 2,102,586 | 316,645 |
| Income (benefit) taxes | 140,992 | (40,821) |
| Net income | \$1,961,594 | \$357,466 |
| Dividends on preferred stock | 5,000 | 5,000 |
| Net income available to common shareholders | \$1,956,594 | \$352,466 |
| Net income per share available to common shareholders: | | |
| Basic | \$.37 | \$.05 |
| Diluted | \$.37 | \$.05 |

Weighted Shares Outstanding:

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| | | |
|---------|-----------|-----------|
| Basic | 5,226,604 | 6,498,404 |
| Diluted | 5,345,061 | 6,610,492 |

See notes to consolidated financial statements.

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SURGE COMPONENTS, INC. AND SUBSIDIARIES

Consolidated Statements of Changes in Shareholders' Equity

Years ended November 30, 2018 and 2017

| | Series C Preferred | | Common | | Additional Paid-In Capital | Accumulated Deficit | Total |
|-----------------------------|--------------------|--------|--------------|----------|----------------------------|---------------------|--------------|
| | Shares | Amount | Shares | Amount | | | |
| Balance – November 30, 2016 | 10,000 | \$ 10 | 10,224,431 | \$10,224 | \$23,702,310 | \$(12,202,270) | \$11,510,274 |
| Preferred stock dividends | - | - | - | - | - | (5,000) | (5,000) |
| Repurchase of common shares | - | - | (5,000,000) | (5,000) | (7,145,000) | - | (7,150,000) |
| Net Income | - | - | - | - | - | 357,466 | 357,466 |
| Balance – November 30, 2017 | 10,000 | 10 | 5,224,431 | 5,224 | 16,557,310 | (11,849,804) | 4,712,740 |
| Preferred stock dividends | - | - | - | - | - | (5,000) | (5,000) |
| Stock option exercise | - | - | 37,697 | 38 | 20,462 | - | 20,500 |
| Net Income | - | - | - | - | - | 1,961,594 | 1,961,594 |
| Balance – November 30, 2018 | 10,000 | \$ 10 | 5,262,128 | \$5,262 | \$16,577,772 | \$(9,893,210) | \$6,689,834 |

See notes to consolidated financial statements.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

| | Year Ended November 30, 2018 | 2017 |
|--|------------------------------------|----------------|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net Income | \$ 1,961,594 | \$ 357,466 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 48,972 | 32,114 |
| Stock compensation expense | - | - |
| Deferred income taxes | 256 | (68,220) |
| Allowance for doubtful accounts | - | (1,584) |
| CHANGES IN OPERATING ASSETS AND LIABILITIES: | | |
| Accounts receivable | (64,225) | (372,876) |
| Inventory | (227,478) | (232,017) |
| Prepaid expenses and income taxes | 139,280 | (14,045) |
| Other assets | - | - |
| Accounts payable | (209,919) | 1,392,340 |
| Deferred rent | (8,964) | (5,444) |
| Accrued expenses | (452,103) | (421,814) |
| NET CASH FLOWS PROVIDED BY) OPERATING ACTIVITIES | 1,187,413 | 665,920 |
| CASH FLOWS FROM INVESTING | | |

ACTIVITIES:

| | | | | |
|-----------------------------|---------|---|---------|---|
| Acquisition of fixed assets | (26,638 |) | (49,522 |) |
|-----------------------------|---------|---|---------|---|

NET CASH FLOWS

| | | | | | | |
|------------------------------|----|---------|---|----|---------|---|
| USED IN INVESTING ACTIVITIES | \$ | (26,638 |) | \$ | (49,522 |) |
|------------------------------|----|---------|---|----|---------|---|

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

(Continued)

| | Year Ended November 30, | |
|--|----------------------------|--------------------|
| | 2018 | 2017 |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Repurchase of common stock | \$- | \$- |
| Proceeds from exercise of stock options | 20,500 | - |
| Repurchase of common stock in tender offer | - | (7,150,000) |
| Net Borrowings on loans payable | (506,411) | 500,000 |
| NET CASH FLOWS (USED IN) FINANCING ACTIVITIES | (485,911) | (6,650,000) |
| NET CHANGE IN CASH | 674,864 | (6,033,602) |
| CASH AT BEGINNING OF PERIOD | 1,086,999 | 7,120,601 |
| CASH AT END OF PERIOD | \$1,761,863 | \$1,086,999 |
| SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION: | | |
| Income taxes paid | \$21,611 | \$27,399 |
| Interest paid | \$15,728 | \$22,443 |
| NONCASH INVESTING AND FINANCING ACTIVITIES: | | |
| Accrued dividends on preferred stock | \$5,000 | \$5,000 |
| Acquisition of fixed assets by capital lease | \$- | \$38,947 |

See notes to consolidated financial statements.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE A – ORGANIZATION, DESCRIPTION OF COMPANY’S BUSINESS AND BASIS OF PRESENTATION

Surge Components, Inc. (“Surge”) was incorporated in the State of New York and commenced operations on November 24, 1981 as an importer of electronic products, primarily capacitors and discrete semi-conductors selling to customers located principally throughout North America. On June 24, 1988, Surge formed Challenge/Surge Inc. (“Challenge”), a wholly-owned subsidiary to engage in the sale of electronic component products and sounding devices from established brand manufacturers to customers located principally throughout North America.

In May 2002, Surge and an officer of Surge founded and became sole owners of Surge Components, Limited (“Surge Limited”), a Hong Kong corporation. Under current Hong Kong law, Surge Limited is required to have at least two shareholders. Surge owns 999 shares of the outstanding common stock and the officer of Surge owns 1 share of the outstanding common stock. The officer of Surge has assigned his rights regarding his 1 share to Surge. Surge Limited started doing business in July 2002. Surge Limited operations have been consolidated with the Company. Surge Limited is responsible for the sale of Surge’s products to customers located in Asia.

On August 31, 2010, the Company changed its corporate domicile by merging into a newly-formed corporation, Surge Components, Inc. (Nevada), which was formed in the State of Nevada for that purpose. Surge Components Inc. is the surviving entity.

In February 2019, the Company converted into a Delaware corporation. The number of authorized shares of common stock was decreased to 50,000,000 shares.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(1) Principles of Consolidation:

The consolidated financial statements include the accounts of Surge, Challenge, and Surge Limited (collectively the “Company”). All material intercompany balances and transactions have been eliminated in consolidation.

(2) Accounts Receivable:

Trade accounts receivable are recorded at the net invoice value and are not interest bearing. The Company considers receivables past due based on the payment terms. The Company reviews its exposure to amounts receivable and reserves specific amounts if collectability is no longer reasonably assured. The Company also reserves a percentage of its trade receivable balance based on collection history and current economic trends that might impact the level of future credit losses. The Company re-evaluates such reserves on a regular basis and adjusts its reserves as needed. Based on the Company’s operating history and customer base, bad debts to date have not been material.

(3) Revenue Recognition:

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standard Update (“ASU”) No. 2014-09, “Revenue from Contracts with Customers: Topic 606.” This ASU replaces nearly all existing U.S. generally accepted accounting principles guidance on revenue recognition. The standard prescribes a five-step model for recognizing revenue, the application of which will require significant judgment by the Company. The Company adopted the standard using the modified retrospective approach in its fiscal year beginning December 1, 2017. The preponderance of the Company’s contracts with customers are standard ship and bill arrangements where revenue is recognized at the time of shipment. Adoption of this ASU did not have a significant impact on the Company’s consolidated financial position, results of operations or cash flows.

Revenue is recognized for products sold by the Company when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed and determinable, collectability is reasonably assured and title and risk of loss have been transferred to the customer. This occurs when product is shipped from the Company’s warehouse.

For direct shipments, revenue is recognized when product is shipped from the Company’s supplier. The Company has a long term supply agreement with one of our suppliers. The Company purchases the merchandise from the supplier and has the supplier directly ship to the customer through a freight forwarder. Title passes to customer upon the merchandise being received by a freight forwarder. Direct shipments were approximately \$4,277,000 and \$3,221,000 for the years ended November 30, 2018 and November 30, 2017 respectively.

The Company also acts as a sales agent to certain customers in North America for one of its suppliers. The Company reports these commissions as revenues in the period earned. Commission revenue totaled \$48,730 and \$244,631 for the years ended November 30, 2018 and November 30, 2017 respectively.

The Company performs ongoing credit evaluations of its customers and maintains reserves for potential credit losses.

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SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(3) Revenue Recognition (continued):

The Company and its subsidiaries currently have agreements with several distributors. There are no provisions for the granting of price concessions in any of the agreements. Revenues under these distribution agreements were approximately \$6,101,000 and \$5,067,000 for the years ended November 30, 2018 and November 30, 2017 respectively.

(4) Inventories:

Inventories, which consist solely of products held for resale, are stated at the lower of cost (first-in, first-out method) or market. Products are included in inventory when the Company obtains title and risk of loss on the products, primarily when shipped from the supplier. Inventory in transit principally from foreign suppliers at November 30, 2018 was \$1,617,382. The Company, at November 30, 2018, has a reserve against slow moving and obsolete inventory of \$233,565. From time to time the Company's products are subject to legislation from various authorities on environmental matters.

(5) Depreciation and Amortization:

Fixed assets are recorded at cost. Depreciation is generally calculated on a straight line method and amortization of leasehold improvements is provided for on the straight-line method over the estimated useful lives of the various assets as follows:

Furniture, fixtures and equipment 5 - 7 years

| | |
|------------------------|---|
| Computer equipment | 5 years |
| Leasehold Improvements | Estimated useful life or lease term, whichever is shorter |

Maintenance and repairs are expensed as incurred while renewals and betterments are capitalized.

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SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(6) Concentration of Credit Risk:

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of accounts receivable. The Company maintains substantially all of its cash balances in a limited number of financial institutions. At November 30, 2018 and November 30, 2017, the Company's uninsured cash balances totaled \$1,197,367 and \$522,504, respectively.

(7) Income Taxes:

The Company's deferred income taxes arise primarily from the differences in the recording of net operating losses, allowances for bad debts, inventory reserves and depreciation expense for financial reporting and income tax purposes. A valuation allowance is provided when it has been determined to be more likely than not that the likelihood of the realization of deferred tax assets will not be realized. See Note J.

The Company follows the provisions of the Accounting Standards Codification topic, ASC 740, "Income Taxes" (ASC 740). There have been no unrecognized tax benefits and, accordingly, there has been no effect on the Company's financial condition or results of operations as a result of ASC 740.

The Company files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. The Company is no longer subject to U.S. federal tax examinations for years before fiscal years ending November 30, 2014, and state tax examinations for years before fiscal years ending November 30, 2013. Management does not believe there will be any material changes in our unrecognized tax positions over the next twelve months.

The Company's policy is to recognize interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense. As of the date of adoption of ASC 740, there was no accrued interest or penalties associated with any unrecognized benefits, nor was any interest expense recognized during the years ended November 30, 2018 and November 30, 2017.

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SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(8) Cash Equivalents:

The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

(9) Use of Estimates:

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

(10) Marketing and promotional costs:

Marketing and promotional costs are expensed as incurred and have not been material to date. The Company has contractual arrangements with several of its distributors which provide for cooperative advertising rights to the distributor as a percentage of sales. Cooperative advertising is reflected as a reduction in revenues and has not been material to date.

(11) Fair Value of Financial Instruments:

The carrying amount of cash balances, accounts receivable, accounts payable and accrued expenses approximate their fair value based on the nature of those items. Estimated fair values of financial instruments are determined using available market information and appropriate valuation methodologies. Considerable judgment is required to interpret the market data used to develop the estimates of fair value, and accordingly, the estimates are not necessarily indicative of the amounts that could be realized in a current market exchange.

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SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(12) Shipping Costs

The Company classifies shipping costs as a component of selling expenses. Shipping costs totaled \$7,240 and \$8,970 for the years ended November 30, 2018 and November 30, 2017 respectively.

(13) Earnings Per Share

Basic earnings per share includes no dilution and is computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding for the period. The difference between reported basic and diluted weighted-average common shares results from the assumption that all dilutive stock options and convertible preferred stock exercised into common stock. Total potentially dilutive shares excluded from diluted weighted shares outstanding at November 30, 2018 and November 30, 2017 totaled 156,543 and 237,911, respectively.

(14) Stock Based Compensation

Stock Based Compensation to Employees

The Company accounts for its stock-based compensation for employees in accordance with Accounting Standards Codification (“ASC”) 718. The Company recognizes in the statement of operations the grant-date fair value of stock options and other equity-based compensation issued to employees and non-employees over the related vesting period.

Stock Based Compensation to Other than Employees

The Company accounts for equity instruments issued in exchange for the receipt of goods or services from other than employees in accordance with ASC 718. Costs are measured at the estimated fair market value of the consideration received or the estimated fair value of the equity instruments issued, whichever is more reliably determinable. The value of equity instruments issued for consideration other than employee services is determined on the earlier of a performance commitment or completion of performance by the provider of goods or services. 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.

(15) Recently Issued Standards

In February 2016, the FASB issued ASU No. 2016-02, "Leases." This ASU requires all lessees to be recognized on the balance sheet as right to use assets and lease liabilities for the rights and obligations created by lease arrangements with terms greater than 12 months. The amendments in this ASU are effective for fiscal years beginning after December 15, 2018 and for interim periods therein. The Company is in the process of assessing the impact the adoption this ASU will have on its consolidated financial position, results of operations and cash flows. At a minimum, total assets and total liabilities will increase in the period the ASU is adopted. Early adoption of this ASU is permitted. At November 30, 2018, the Company's undiscounted future minimum payments outstanding for lease obligations (including those currently included as capital lease obligations) were approximately \$421,092

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE C - FIXED ASSETS

Fixed assets consist of the following:

| | November 30, 2018 | November 30, 2017 |
|-------------------------------|----------------------|----------------------|
| Furniture and Fixtures | \$ 327,971 | \$ 327,971 |
| Leasehold Improvements | 991,646 | 987,137 |
| Computer Equipment | 1,063,005 | 1,040,875 |
| Less-Accumulated Depreciation | (2,266,627) | (2,217,654) |
| Net Fixed Assets | \$ 115,995 | \$ 138,329 |

Depreciation and amortization expense for the years ended November 30, 2018 and November 30, 2017 was \$48,972 and \$32,114, respectively.

NOTE D – CAPITALIZED LEASE OBLIGATIONS

The Company is obligated under capitalized leases for telephone equipment. The Company leases equipment under two capital lease arrangements with NEC Financial Services. Pursuant to the leases, the lessor retains actual title to the leased property until the termination of the lease, at which time the equipment can be purchased for one dollar for each lease. The terms of the leases are 60 months with a combined monthly payment of \$815, respectively. The assumed interest rates on the leases are 9.342%. The leases terminate in 2022.

Future minimum lease payments under these capitalized lease obligations as of November 30, 2018 are as follows:

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| | |
|---|----------|
| 2019 | \$9,779 |
| 2020 | \$9,779 |
| 2021 | \$9,779 |
| 2022 | \$9,779 |
| Total | \$39,116 |
| Less: interest portion | 6,580 |
| Present value of net minimum lease payments | \$32,536 |
| Less: current portion | 7,036 |
| Non-current portion | \$25,500 |

Capital lease obligations mature as follows:

Fiscal year ending December 31:

| | |
|------------------------------|----------|
| 2019 | \$7,036 |
| 2020 | \$7,722 |
| 2021 | \$8,475 |
| 2022 | \$9,303 |
| Principal payments remaining | \$32,536 |

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SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE E – LINE OF CREDIT

In February 2017, the Company obtained a line of credit with a bank for up to \$3,000,000 (the “Credit Line”). Borrowings under the Credit Line are due upon demand and accrue interest at the greater of the prime rate or the LIBOR rate plus two percent (and may be increased by three percent in the event the Company fails to (i) repay all amounts due on the Credit Line upon demand or (ii) comply with any terms or conditions relating to the Credit Line). As of November 30, 2018, the balance on the Credit Line was \$0. As of November 30, 2018, the Company was in compliance with the covenant for the debt service coverage ratio for the Credit Line.

NOTE F – ACCRUED EXPENSES

Accrued expenses consist of the following:

| | November 30, 2018 | November 30, 2017 |
|---------------------------|----------------------|----------------------|
| Commissions | \$ 228,199 | \$ 186,282 |
| Preferred stock dividends | 141,569 | 136,569 |
| Other accrued expenses | 233,435 | 158,928 |
| Accrued professional fees | - | 455,470 |
| | \$ 603,203 | \$ 937,249 |

NOTE G – RETIREMENT PLAN

In June 1997, the Company adopted a qualified 401(k) retirement plan for all full-time employees who are twenty-one years of age and have completed twelve months of service. The plan allows total employee contributions of up to fifteen percent (15%) of the eligible employee’s salary through salary reduction. The Company makes a matching contribution of twenty percent (20%) of each employee’s contribution for each dollar of employee deferral up to five

percent (5%) of the employee's salary. Net assets for the plan, as estimated by Union Central, Inc., which maintains the plan's records, were approximately \$1,201,000 at November 30, 2018. Pension expense for the years ended November 30, 2018 and November 30, 2017 was \$1,908 and \$1,626, respectively.

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SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE H – SHAREHOLDERS’ EQUITY

[1] Preferred Stock:

In February 1996, the Company amended its Certificate of Incorporation to authorize the issuance of 1,000,000 shares of preferred stock in one or more series. In August 2010, the number of preferred shares authorized for issuance was increased to 5,000,000 shares.

In November 2000, the Company authorized 100,000 shares of preferred stock as Non-Voting Redeemable Convertible Series C Preferred Stock (“Series C Preferred”). Each share of Series C Preferred is automatically convertible into 10 shares of our common stock upon shareholder approval. If the Series C Preferred were converted into common stock on or before April 15, 2001, these shares were entitled to cumulative dividends at the rate of \$.50 per share per annum commencing April 15, 2001 payable on June 30 and December 31 of each year. In November 2000, 70,000 shares of the Series C Preferred were issued in payment of financial consulting services to its investment banker and a shareholder of the Company. In April 2001, 8,000 shares of the Series C Preferred were repurchased and cancelled.

In April 2002, in connection with a Mutual Release, Settlement, Standstill and Non-Disparagement Agreement among other provisions, certain investors transferred back to the Company 252,000 shares of common stock, 19,300 shares of Series C preferred stock, and certain warrants, in exchange for \$225,000. These repurchased shares were cancelled.

In February 2006, the Company settled with a shareholder to repurchase 10,000 shares of Series C Preferred plus accrued dividends for \$50,000.

Pursuant to exchange agreements dated as of March 14, 2011, 9,000 shares of Series C Preferred were returned to the Company for cancellation in exchange for 112,500 shares of common stock.

In October 2014, 2,000 shares of Series C Preferred were converted into 20,000 shares of common stock.

In April 2015, the Company entered into a settlement agreement with a shareholder pursuant to which 7,500 shares of Series C Preferred were returned to the Company for cancellation in exchange for 110,000 shares of common stock plus \$65,000 for accrued dividends and legal fees and expenses.

In July 2015, 4,200 shares of Series C Preferred were exchanged for 42,000 shares of common stock and \$29,838 in accrued dividends.

Dividends aggregating \$141,569 have not been paid for the semi-annual periods ended December 31, 2001 through the semi-annual payment due June 30, 2018. The Company has accrued these dividends. At November 30, 2018, there are 10,000 shares of Series C Preferred issued and outstanding.

In October 2016, the Company authorized 75,000 shares of preferred stock as Voting Non-Redeemable Convertible Series D Preferred Stock ("Series D Preferred"). None of the Series D Preferred Stock is outstanding as of November 30, 2018.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE H – SHAREHOLDERS’ EQUITY (Continued)[2] 2010 Incentive Stock Plan

In March 2010, the Company adopted, and in April 2010 the shareholders ratified, the 2010 Incentive Stock Plan (“2010 Stock Plan”). The 2010 Stock Plan provides for the grant of options to officers, employees, directors or consultants to the Company to purchase an aggregate of 1,500,000 common shares.

Activity in the 2010 Stock Plan for the year ended November 30, 2018 is summarized as follows:

| | Shares | Weighted Average Exercise Price |
|---|-----------|--|
| Options outstanding December 1, 2017 | 250,000 | \$ 0.94 |
| Options issued in the year ended November 30, 2018 | - | \$ - |
| Options exercised in the year ended November 30, 2018 | (75,000) | \$ 0.82 |
| Options cancelled in the year ended November 30, 2018 | - | \$ - |
| Options outstanding at November 30, 2018 | 175,000 | \$ 0.99 |
| Options exercisable at November 30, 2018 | 175,000 | \$ 0.99 |

[3] 2015 Incentive Stock Plan

In November 2015, the Company adopted and the shareholders ratified, the 2015 Incentive Stock Plan (“2015 Stock Plan”). The 2015 Stock Plan provides for the grant of options to officers, employees, directors or consultants to the Company to purchase an aggregate of 1,500,000 common shares.

In May 2016 a total of 99,151 shares were issued to the Company's officers as part of their 2015 bonus compensation under the 2015 Stock Plan.

In April 2016, the Company awarded one employee director 67,901 shares of its common stock and another employee director 31,250 shares of its common stock under the 2015 Stock Plan as part of their 2015 bonus. The Company recorded a cost of \$74,363 relating to the issuance of these shares.

In October 2016, one employee director exercised options to acquire 50,000 shares of common stock at \$0.82 per share and 62,500 shares of common stock at \$0.80 per share. In October 2016, one employee director exercised options to acquire 25,000 shares of common stock at \$0.82 per share and 45,938 shares of common stock at \$0.80 per share.

The intrinsic value of the exercisable options at November 30, 2018 totaled \$6,000. At November 30, 2018 the weighted average remaining life of the stock options is 1.88 years. At November 30, 2018, there was no unrecognized compensation cost related to the stock options granted under the plan.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE H – SHAREHOLDERS’ EQUITY (Continued)

[4] Authorized Repurchase of Shares:

In November 2015, the Board of Directors authorized the Company to purchase up to \$500,000 of common stock in the open market or in privately negotiated transactions. Pursuant to such authority and pursuant to Rule 10b-18 under the Securities Exchange Act of 1934, as amended (“Exchange Act”), a total of 57,283 shares were repurchased by the Company for approximately \$48,300. In January 2017, the Company terminated its repurchase program.

In March 2017, the Company completed a tender offer whereby it purchased for cash 5,000,000 shares of its common stock, at a price of \$1.43 per share, or \$7,150,000.

[5] Compensation of Directors

Compensation for each non-employee director is \$2,500 per month (and \$3,500 per month for a non-employee director that serves as the chairman of more than two committees of the Board of Directors).

NOTE I – SETTLEMENT AGREEMENT

On December 22, 2016, the Company entered into a settlement agreement (the “Settlement Agreement”) with Michael D. Tofias and Bradley P. Rexroad (collectively, the “Stockholders”). The Settlement Agreement generally provided that:

the Board and the Stockholders will identify a mutually acceptable independent director to join the Board as a Class C director by February 28, 2017 and the Board will include that new director among its director nominees for the 2017 annual meeting;

the Company will take all steps to (i) change its state of incorporation from the State of Nevada to the State of Delaware and (ii) declassify the Board on a rolling basis by June 30, 2017, and the Company will convene a special meeting of stockholders of the Company for the purpose of approving such actions, at which meeting the Stockholders and the Insiders will vote all of their shares of common stock of the Company in favor of such actions, and

the Company will commence an issuer tender offer to all of its stockholders to repurchase at least 5.0 million shares of its common stock at a price of \$1.43 per share (the "Tender Offer"), which the Company completed in March 2017 whereby it purchased for cash 5,000,000 shares of its common stock, at a price of \$1.43 per share, or \$7,150,000.

the Stockholders will tender all of the shares of common stock of the Company that they hold beneficially or of record in the Tender Offer, subject to limited exceptions; and

the Company's officers and directors will not participate in the Tender Offer and will not transfer or sell any of their shares until six months after the Tender Offer is completed.

Pursuant to the Settlement Agreement, the Company also agreed to reimburse the expenses of the Stockholders associated with their investment in the Company, including their proxy solicitation and litigation costs, in an amount not to exceed \$300,000.

On April 6, 2017, the Board of Directors elected Peter Levy as a Class C Director. He is an independent director.

On October 4, 2018, the Company held its annual meeting of shareholders, at which shareholders approved (i) the change in the Company's state of incorporation from Nevada to Delaware and (ii) the declassification of the Company's board of directors on a rolling basis. No shareholders exercised their dissenters' rights in connection with the reincorporation proposal. The Company was reincorporated in Delaware on February 5, 2019.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE I – SETTLEMENT AGREEMENT (Continued)

until the day after the announcement of the completion of the Tender Offer, the Board will be composed of no more than seven individuals;

the Stockholders will tender all of the shares of common stock of the Company that they hold beneficially or of record in the Tender Offer, subject to limited exceptions;

the Company's officers and directors will not participate in the Tender Offer and will not transfer or sell any of their shares until six months after the Tender Offer is completed;

subject to certain conditions, if the Tender Offer is not completed by March 15, 2017, the Company will (i) appoint the Stockholders to the Board as Class A directors with terms expiring at the Company's annual meeting of stockholders for fiscal year 2018 (the "2019 Meeting") and (ii) reduce the size of the Board to six directors, including the Stockholders;

the Stockholders will withdraw with prejudice their lawsuit against the Company and the Insiders pending in the State of Nevada; and

the Stockholders will be subject to customary standstill provisions until the termination of the Settlement Agreement.

Pursuant to the Settlement Agreement, the Company also agreed to reimburse the expenses of the Stockholders associated with their investment in the Company, including their proxy solicitation and litigation costs, in an amount not to exceed \$300,000.

The Settlement Agreement terminates on the date that is 15 business days prior to the deadline for the submission of director nomination and stockholder proposals for the 2019 Meeting.

In August 2018, several provisions of the Settlement Agreement were amended (the “Amendment”). Pursuant to the Amendment, the Company agreed to take all steps necessary to change its state of incorporation from the state of Nevada to the state of Delaware. During Fiscal 2018, the Company must submit to its shareholders a proposal to approve the reincorporation. If a specified number of shares seek to exercise their dissenters’ rights, the Board may withdraw the reincorporation proposal. If withdrawn, the Company must resubmit the proposal to approve the reincorporation during a meeting held in Fiscal 2019. If holders of a specified number of shares seek to exercise their dissenters’ rights, the Company’s board of directors may withdraw the reincorporation proposal. If withdrawn, the Company must resubmit the proposal to approve the reincorporation during a meeting held in Fiscal 2020. The Amendment extended the period for prohibition of any equity grants until the completion of reincorporation into Delaware. The Settlement Agreement terminates at the latter of the date that is 15 business days prior to the deadline for the submission of director nomination and stockholder proposals for the 2019 Meeting or the date that the Company completes the reincorporation into Delaware.

On October 4, 2018, the Company held its annual meeting of shareholders, at which shareholders approved (i) the change in the Company’s state of incorporation from Nevada to Delaware and (ii) the declassification of the Company’s board of directors on a rolling basis. No shareholders exercised their dissenters’ rights in connection with the annual meeting and the Company expects to file the requisite documentation with the states of Nevada and Delaware to effectuate the reincorporation in the near future.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE J – INCOME TAXES

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes using the enacted tax rates in effect in the years in which the differences are expected to reverse.

The Company's deferred income taxes are comprised of the following:

| | November 30, 2018 | November 30, 2017 |
|---------------------------|----------------------|----------------------|
| Deferred Tax Assets | | |
| Net operating loss | \$ 2,008,906 | \$ 3,786,406 |
| Allowance for bad debts | 32,658 | 49,909 |
| Inventory | 69,757 | 92,225 |
| Deferred rent | 6,679 | 13,786 |
| Other | 62,071 | - |
| Depreciation | 73,140 | 115,752 |
| Total deferred tax assets | 2,253,211 | 4,058,078 |
| Valuation allowance | (1,270,587) | (3,075,198) |
| Deferred Tax Assets | \$ 982,624 | \$ 982,880 |

The valuation allowance for the deferred tax assets relates principally to the uncertainty of the utilization of deferred tax assets and was calculated in accordance with the provisions of ASC 740, which requires that a valuation allowance be established or maintained when it is "more likely than not" that all or a portion of deferred tax assets will not be realized. The valuation allowance decreased by approximately \$1,804,000 during the year ended November 30, 2018. This valuation is based on management estimates of future taxable income. Although the degree of variability inherent in the estimates of future taxable income is significant and subject to change in the near term, management believes, that the estimate is adequate. The estimated valuation allowance is continually reviewed and as adjustments to the allowance become necessary, such adjustments are reflected in the current operations.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE J – INCOME TAXES (Continued)

The Company's income tax expense consists of the following:

| | Years Ended | |
|----------------------------|----------------------|----------------------|
| | November 30, 2018 | November 30, 2017 |
| Current: | | |
| Federal | \$41,094 | \$ - |
| States | 99,642 | 27,399 |
| | 140,736 | 27,399 |
| Deferred: | | |
| Federal | 184 | (55,940) |
| States | 72 | (12,280) |
| | 256 | (68,220) |
| Provision for income taxes | \$ 140,992 | \$ (40,821) |

The Company files a consolidated income tax return with its wholly-owned subsidiaries and has net operating loss carryforwards of approximately \$7,687,000 for federal and state purposes, which expire through 2020. A reconciliation of the difference between the expected income tax rate using the statutory federal tax rate and the Company's effective rate is as follows:

| | Years ended | | | |
|---------------------------------------|----------------------|-----|----------------------|--|
| | November 30, 2018 | | November 30, 2017 | |
| U.S Federal Income tax statutory rate | 21 % | 34 | % | |
| Valuation allowance | (21)% | (56 |)% | |
| State income taxes | 7 % | 9 | % | |

| | | |
|--------------------|-----|--------|
| Other | - | - |
| Effective tax rate | 7 % | (13)% |

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SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE K – RENTAL COMMITMENTS

The Company leases its office and warehouse space through 2020 from a corporation that is controlled by officers/shareholders of the Company (“Related Company”). Annual minimum rental payments to the Related Company approximated \$180,000 for the year ended November 30, 2018, and increase at the rate of three per cent per annum throughout the lease term.

Pursuant to the lease, rent expense charged to operations differs from rent paid because of scheduled rent increases. Accordingly, the Company has recorded deferred rent. Rent expense is calculated by allocating to rental payments, including those attributable to scheduled rent increases, on a straight line basis, over the lease term.

In June 2015, the Company renewed its lease to rent office space and a warehouse in Hong Kong for two years and is currently in negotiations to renew the lease. Annual minimum rental payments for this space are approximately \$58,500.

In January 2019, the Company entered into a lease to rent warehouse space in Hong Kong for two years. Annual minimum rental payments for this space are approximately \$36,840.

The Company’s future minimum rental commitments at November 30, 2018 are as follows:

Twelve Months Ended November 30,

| | |
|------|------------|
| 2019 | \$ 186,912 |
| 2020 | \$ 191,994 |
| 2021 | \$ 3,070 |

\$381,976

Net rental expense for the years ended November 30, 2018 and November 30, 2017 were \$317,210 and \$314,746 respectively, of which \$260,241 and \$256,721 respectively, was paid to the Related Company.

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SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE L – EMPLOYMENT AND OTHER AGREEMENTS

In February 2016, the Company entered into revised employment agreements with two officers of the Company. Pursuant to these agreements, the base salary for one officer is \$275,000 and the base salary for the other officer is \$225,000. The agreements continue until terminated by either party.

The Company's compensation committee may award these officers with bonuses and will review the base salary amounts for each of the officers on an annual basis to determine if any changes to the base salary amounts need to be made and may also award these officers with annual bonuses. Pursuant to the employment agreements, the officers are prohibited from engaging in activities which are competitive with those of the Company during their employment with the Company and for one year following termination. If the agreement is terminated other than for cause, the officer would be entitled to all base salary earned through the date of termination, accrued but unused vacation, all vested equity, and bonus amounts payable to the officer through the date of termination. The officers would also be entitled to receive an additional thirty-six months of annual compensation equal to the average of his base salary and bonus for the three calendar years prior to the date of termination, payable in accordance with the Company's regular payroll practice over a 52-week period.

NOTE M – MAJOR CUSTOMERS

The Company had two customers who each accounted for 11% and 13% of net sales for year ended November 30, 2018 and one customer who accounted for 12% of net sales for the year ended November 30, 2017. The Company had two customers who each accounted for 11% and 14% of accounts receivable at November 30, 2018 and one customer who accounted for 11% of accounts receivable at November 30, 2017.

NOTE N – MAJOR SUPPLIERS

During the years ended November 30, 2018 and November 30, 2017 there was one foreign supplier accounting for 46% and 49% of total inventory purchased.

The Company purchases substantially all of its products overseas. For the year ended November 30, 2018, the Company purchased 49% of its products from Taiwan, 18% from Hong Kong, 30% from elsewhere in Asia and less than 1% overseas outside of Asia. The Company purchases the balance of its products in the United States.

NOTE O – EXPORT SALES

The Company's export sales were as follows:

| | Year Ended | |
|-----------------------|--------------|--------------|
| | November 30, | November 30, |
| | 2018 | 2017 |
| Canada | 4,250,717 | 3,748,226 |
| China | 4,838,884 | 4,688,335 |
| Other Asian Countries | 1,690,734 | 2,160,762 |
| South America | 407,894 | 411,376 |
| Europe | 1,012,220 | 1,185,304 |

Revenues are attributed to countries based on location of customer.