Knowles Corp
Form 10-K
March 28, 2014
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2013
or

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

For the transition period from to

Commission File Number: 001-36102
Knowles Corporation
(Exact Name of Registrant as Specified in Its Charter)

| | |
|---|---|
| Delaware | 90-1002689 |
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification No.) |
| 1151 Maplewood Drive, Itasca, IL 60143 | 60143 |
| (Address of Principal Executive Offices) | (Zip Code) |

Registrant's telephone number, including area code: (630) 250-5100

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

| Title of each class | Name of each exchange on which registered |
|---|---|
| Common Stock, par value $0.01 per share | New York Stock Exchange |

Securities registered pursuant to Section 12(g) of the Act: None

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or Section 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 o No þ

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

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 registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. þ

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

Large accelerated filer o Accelerated filer o Non-accelerated filer þ Smaller reporting company o
(Do not check if a smaller reporting company)

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

As of June 30, 2013, the registrant's common stock was not publicly-traded. The number of outstanding shares of the registrant's common stock as of March 21, 2014 was 85,027,624.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information contained in the registrant's Proxy Statement for its 2014 Annual Meeting of Shareholders (to be filed not later than 120 days after the end of registrant's fiscal year) (the "2014 Proxy Statement") is incorporated by reference into Part III hereof.

Cautionary Statement Concerning Forward-Looking Statements

This Annual Report on Form 10-K contains certain statements regarding business strategies, market potential, future financial performance, future action, results and other matters which are “forward-looking” statements within the meaning of the Securities Act of 1933, as amended, the Securities Exchange Act of 1934, as amended, and the Private Securities Litigation Reform Act of 1995. The words “believe,” “expect,” “anticipate,” “project,” “estimate,” “budget,” “contin “could,” “intend,” “may,” “plan,” “potential,” “predict,” “seek,” “should,” “will,” “would,” “expect,” “objective,” “forecast,” “ “outlook,” “effort,” “target” and similar expressions, among others, generally identify forward-looking statements, which speak only as of the date the statements were made. Additionally, forward-looking statements include, but are not limited to:

- expectations as to future sales of products;
- ability to protect intellectual property in the United States and abroad;
- estimates regarding capital requirements and needs for additional financing;
- estimates of expenses, future revenues and profitability;
- estimates of the size of the markets for products and services;
- expectations related to the rate and degree of market acceptance of products; and
- estimates of the success of other competing technologies that may become available.

In particular, information included under the sections entitled “Business,” “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” contain forward-looking statements.

The matters discussed in these forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results to differ materially from those projected, anticipated or implied in the forward-looking statements. Where, in any forward-looking statement, an expectation or belief as to future results or events is expressed, such expectation or belief is based on the current plans and expectations of management and expressed in good faith and believed to have a reasonable basis, but there can be no assurance that the expectation or belief will be achieved or accomplished. Factors that could cause actual results or events to differ materially from those anticipated include the matters described under the sections entitled “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” Knowles does not undertake any obligation to update any forward-looking statement, except as required by applicable law.

TABLE OF CONTENTS

Table of Contents

# PART I

## ITEM 1. BUSINESS

### Separation from Dover Corporation

On February 28, 2014, Knowles Corporation ("Knowles") became an independent, publicly-traded company as a result of the distribution by Dover Corporation ("Dover") of 100% of the outstanding common stock of Knowles to Dover’s shareholders. Dover’s Board of Directors approved the distribution of its shares of Knowles on February 6, 2014. Knowles’ Registration Statement on Form 10 was declared effective by the U.S. Securities and Exchange Commission on February 10, 2014. On February 28, 2014, Dover's shareholders of record as of the close of business on February 19, 2014 received one share of Knowles common stock for every two shares of Dover common stock held as of the record date. Knowles common stock began trading “regular-way” under the ticker symbol “KN” on the New York Stock Exchange on March 3, 2014.

Unless the context otherwise requires, references in this Annual Report on Form 10-K to (i) “Knowles,” the “Company,” “we,” “our” or “us” refer to Knowles Corporation and its combined subsidiaries, after giving effect to the spin-off of Knowles from Dover Corporation, (ii) “Former Parent” refer to Dover Corporation and (iii) the “Separation” or the “Distribution” refer to our spin-off from our Former Parent. Knowles was incorporated in Delaware on June 12, 2013 for the purpose of holding certain of Former Parent’s communication technologies businesses in connection with the Separation. The address of our principal executive offices is 1151 Maplewood Drive, Itasca, Illinois 60143. Our telephone number is 630-250-5100.

### Overview

Knowles engages in the design and manufacture of innovative products and components which serve the mobile consumer electronics, medical technology, telecommunications infrastructure, military/space and other industrial end markets. We were built by our Former Parent through a series of acquisitions (including Knowles Electronics, Vectron International, Novacap, Syfer, Dielectric, Voltronics and Sound Solutions) and internal growth initiatives spanning the last 20 years. We have a leading position in MicroElectroMechanical Systems (“MEMs”) microphones, speakers and receivers which are used in mobile handsets, smartphones and tablets within the consumer electronics market. We are also a leading manufacturer of transducers used in the hearing health segment of the medical technology market and have a strong position in oscillators (timing devices) and capacitors which serve the telecommunication infrastructure, military/space and other industrial markets.

### Management Philosophy

Our leadership guides the continued progress of our research and development, the expansion of our technology platforms, and the efficacy of our businesses. This guidance is achieved through an understanding of end-user needs and by anticipating the opportunities we can bring to our product design and manufacturing. We are an application-based technology company, and our businesses are committed to operational excellence and to being market leaders as measured by market share, customer service, innovation, profitability and return on invested capital. In addition, we are committed to creating value for our customers, employees and shareholders through sustainable business practices that protect the environment, and developing products that help our customers meet their sustainability goals.

### Our Strengths

We believe that the following competitive strengths will enable us to continue to expand on our industry-leading position serving the communication technologies industry:

Leader in the communication technologies industry

We have built an industry-leading enterprise in terms of brand recognition, technology and market presence in communication technologies. Based on market share, we are a leading supplier of acoustic components to all major handset original equipment manufacturers ("OEMs") and hearing aid OEMs. We also have a strong position in supplying oscillators and capacitors to customers in the telecommunications infrastructure, military/space and other industrial markets. Dynamic research and fast product development cycles, and high-volume, scalable manufacturing capabilities are characteristics that we have developed and intend to continue to build upon.

Table of Contents

Market leading product innovation

We invest significant resources in research and development and bring significant application expertise with capabilities to quickly and effectively design, develop and manufacture new products to meet our customers' needs. We maintain design centers in multiple locations in North America, Europe and Asia, which enables us to attract the best talent in every region of the world. We have increased our spending by over 50% to support our research and development functions over the last three years and spend approximately 7% of revenue on an annual basis on projects intended to preserve and extend our technological advantage.

Operational excellence

We have a proven track record of executing operational improvements, through cost reductions, increased yields and improving capacity utilization. Our diversified operations include high-volume scalable production capabilities, fully automated production lines and labor-intensive assembly processes. We maintain major manufacturing facilities in three countries which are integrated through a centralized operating system and supply chain.

Well-established, collaborative relationships with leading customers

Our close relationship with our customers enables us to develop critical expertise regarding our customers' requirements and needs. We use that expertise and application knowledge, coupled with our research and development, to design differentiated products that are used to enhance the end users' acoustic interface with their mobile devices or ensure performance in mission critical applications. Our products have been designed into multiple generations of our customers' products.

Executive management team with proven history of success

Our President and Chief Executive Officer and the majority of his direct reports and the core operational team have worked together for a significant number of years. The executive management team has driven our strong history of profitability and cash flow generation, and demonstrated a proven ability to execute under multiple ownership structures, including private equity and as part of the segment company structure within our Former Parent. In addition to Jeffrey Niew, our President and Chief Executive Officer, our named executive officers include John Anderson, Michael Adell, Raymond Cabrera and David Wightman, who all held senior positions of responsibility at our Former Parent prior to the Separation. For more information regarding the named executive officers and other members of the management team of Knowles, see "Executive Officers of the Registrant."

Strong financial performance allows us to exceed customer demands

Our business model has evolved as our end markets have developed and grown over the years. Our strong history of profitability and cash flow generation, supported by a strong and flexible balance sheet, will enable us to continue to invest in new products and technology at a rapid pace in order to meet and exceed customer demands.

Business Segments

We are organized into two reportable segments based on how management analyzes performance, allocates capital and makes strategic and operational decisions. These segments were determined in accordance with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 280—Segment Reporting and are comprised of (i) Mobile Consumer Electronics ("MCE") and (ii) Specialty Components ("SC"). The segments are aligned around similar product applications serving our key end markets, to enhance focus on end market growth strategies.

- MCE designs and manufactures innovative acoustic products, including microphones, speakers and receivers, used in several applications that serve the handset, tablet and other consumer electronic markets. Locations include the corporate office in Itasca, Illinois; sales, support and engineering facilities in North America, Europe and Asia; and manufacturing facilities in Europe and Asia.

4

Table of Contents

- SC specializes in the design and manufacture of specialized electronic components used in medical and life science applications, as well as high-performance solutions and components used in communications infrastructure and a wide variety of other markets. SC's transducer products are used principally in hearing aid applications within the commercial audiology markets, while its oscillator products predominantly serve the telecom infrastructure market and its capacitor products are used in applications including radio, radar, satellite, power supplies, transceivers and medical implants serving the defense, aerospace, telecommunication and life sciences markets. Operating facilities and sales, support and engineering facilities are located in North America, Europe and Asia.

We sell our products directly to OEMs and to their contract manufacturers and suppliers, and to a lesser extent through distributors worldwide.

The following table shows the percentage of total revenue and segment earnings generated by each of our segments for the years ended December 31, 2013, 2012 and 2011:

| | Revenue Years Ended December 31, | | | Segment Earnings Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| | 2013 | 2012 | 2011 | 2013 | 2012 | 2011 |
| Mobile Consumer Electronics | 64 % | 60 % | 52 % | 70 % | 62 % | 54 % |
| Specialty Components | 36 % | 40 % | 48 % | 30 % | 38 % | 46 % |

The following table shows total assets by segment at December 31, 2013 and 2012:

| (in thousands) | December 31, 2013 | 2012 |
|---|---|---|
| Mobile Consumer Electronics | $1,638,241 | $1,561,398 |
| Specialty Components | 538,659 | 487,256 |
| Corporate / eliminations | (6,784) | 2,438 |
| Total | $2,170,116 | $2,051,092 |

Our Markets and Market Trends

Our products serve a variety of end markets, notably, consumer mobile devices, medical technology, aerospace and defense and telecom, and can generally be divided into two categories: Acoustic Components and Specialty Components, as described below.

- Acoustic Components. Includes analog and digital microphones, MEMs microphones, surface mounted device microphones, receivers, speakers, speaker modules, multi-functional devices, ultrasonic sensors and integrated audio sub-systems.
- Specialty Components. Includes transducers, oscillators, capacitors and filters.

The markets served by Acoustic Components continue to be driven by trends in smartphone and tablet innovation and demand. Today, mobile device OEMs are facing ever-rising challenges to differentiate their products in the global marketplace while managing growing cost pressures and time-to-market expectations. However, mobile consumers and mobile carriers alike are expecting better quality voice calls, audio and video conferencing, capturing and playback, media content consumption and gaming, as well as extended battery life. To enable smart mobile devices to handle ever more demanding audio use cases, OEMs are increasingly adopting more intelligent active audio components (audio chipset) and higher performance passive acoustic components. Trends impacting the smartphone market today include:

- Smartphone growth from feature phone substitution. The smartphones segment within the handset device market has exhibited consistently strong unit growth over the past five years (>40% unit volume compound annual growth rate). There continues to be a positive mix shift from the proliferation of lower-end smartphone devices and the further cannibalization of feature phones (i.e., non-smartphones). The average smartphone continues to drive higher audio content including more microphones and higher value speakers than its feature phone counterpart, compounding the growth of acoustic content as mobile phone sales rise.

Table of Contents

- Smartphone OEM market share shifts are likely to remain volatile for some time. Recently, Nokia and Blackberry have lost significant market share to other U.S. and Asian-based OEMs who have released smartphones that have been more readily accepted due to, among other factors, perceived feature sets and price points. We expect the OEM market to continue to be dynamic over time, characterized by rapid market share shifts driven by new product introductions, price points and feature sets.
- New OEM product line rollouts. Smartphones continue to shift to Long Term Evolution ("LTE"), a standard for 4G wireless technology, and the shift is expected to buoy unit growth in developed markets and drive the competitive landscape in high-end chipsets through 2014. Aggressive LTE deployments are expected in China, in addition to a build-out of deeper coverage profiles in the U.S., Japan, Korea and Northern Europe. This will likely drive an increase in LTE smartphone units over the next five years, which should help maintain some level of high-end smartphone volume growth despite high market penetration.
- Shortened smartphone upgrade plans at U.S. carriers. Several U.S. carriers have recently introduced new smartphone plans which offer consumers the option of paying for their phone in monthly installments with no upfront lump sum payment, and the ability to upgrade again in 12 months. Plans such as these could drive greater-than-expected unit growth (turnover) at the high end, as they are most likely to appeal to high-income consumers seeking to upgrade their phone more frequently.
- High-end consumer elasticity. Consumers are reluctant to downgrade from a high-end smartphone to a low-end smartphone in most circumstances. This is especially true as high-end smartphones will likely continue to offer significant performance advantages and new functionality compared to low-end smartphones.
- Proliferation of premium acoustics. Consumers are seeking improved acoustics solutions, regardless of the country they live in or the type of device they are using. As a result, acoustic dollar content is generally expanding per device for two primary reasons. First, many of the solutions we are introducing are higher performance and command higher value. Secondly, OEMs are increasing the number of acoustic components per device. Over the past several years, we have seen an increase in the number of microphones used in high end smartphones. The benefits to the user are substantial, including reduced background noise, improved voice recognition, better hands-free communication and enhanced audio recording and playback capabilities. OEMs and their customers recognize the importance of these features in their next-generation products. We believe an additional opportunity exists for these trends to proliferate to mid-range phones and tablets, as well as emerging wearable devices. Knowles can capitalize on these market demands by leveraging our acoustics expertise and proprietary process technologies to deliver solutions that improve the performance of our OEM customers' devices.

Specialty Components products are sold across diverse end markets, and relative to the Acoustic Components end markets, portions of this business face much greater exposure to capital investment cycles and government spending, both direct and indirect, as some of these end markets are largely dependent on project upgrades and expansion, and government contracts. These products can be divided into the following categories:

- Medical and life sciences products (i.e., transducers, hearing aids, capacitors). Product sales are largely driven by aging demographics, healthcare spending, the rise of a middle class in emerging markets and government subsidies.
- Aerospace and defense communications (i.e., capacitors, filters, oscillators). Aerospace and defense spending and automation (largest end market), telecom regional coverage and bandwidth expansion, and growing industrial power supply requirements are a few of the end market trends driving the product sales in this sector.
- Telecom infrastructure (i.e., capacitors, filters, oscillators). Sales are typically levered to the expansion of large telecom companies, looking to increase wireless signal in new or existing territories, although these products are also sold to aerospace and defense companies (i.e., airplane radio frequencies).

Geographic Trends

We strive to maintain our manufacturing facilities in close proximity to our direct customers. In the case of MCE, we operate four facilities in Asia to serve the contract manufacturers who build OEM equipment on behalf of our end-customers. These contract manufacturers are largely based in China, Taiwan and India. Although end-user demand for consumer electronics is global, and marketing activities occur globally, critical mass for manufacturing is located in Asia and, as a result, a large majority of MCE's manufacturing capacity is based in Asia, primarily China, Malaysia and the Philippines.

Table of Contents

In the case of SC, we operate three facilities in Asia to serve the manufacturing sites of both hearing aid OEMs and the contract manufacturers who build OEM headsets on behalf of earphone makers. These OEM manufacturing sites are largely based in China, Singapore, Indonesia and Vietnam. Although marketing activities and end-user demand for hearing aid and specialty consumer components is global, critical mass for manufacturing is located in Asia for the purposes of being close to the point of assembly. We also operate three facilities in the United States, one in Mexico, and three in Europe for the manufacturing of capacitors and oscillators that support our global telecom and military customers, as well as their suppliers and contract manufacturers.

While no significant statutory limitation exists, a repatriation of profits from foreign markets to the United States is inherently inefficient, as business expansion opportunities and capital expenditure requirements are expected to be consistent with the needs of our direct customer and manufacturing locations.

Competitive Landscape

Success in the electronic components industry is primarily driven by innovation and flexibility as customers compete to gain a share of the fast growing handset market. Capturing growth opportunities usually results from competition across both platform and component designs, which supports position, pricing and margins. Continuous research and development investment allows for the capture of all emerging new brands with early mover advantage. Flexibility in balancing full and semi-automation is a key to achieving a superior cost structure. Additionally, it is important for component vendors to have flexibility and quick time-to-market to meet clients' needs. Notably, according to industry estimates, the product cycle for handsets has shortened to eight months from two years. Key competitors include:

- MCE: AAC Technologies and Goertek
- SC: Sonion for hearing health and a highly fragmented set of competitors across capacitor and oscillator products for each end market

In the mobile consumer electronics segment, our investments in research and development enable us continually to introduce new products that are higher performance. Our customers are quickly adopting these higher value microphones, speakers and receivers in their new products as they improve the overall audio performance in the end application, which in turn improves the end user experience. With each successive generation, our new products generally have higher average selling prices than the products they are replacing. Once introduced, the pricing for these products follows a normal downward trend as typically seen in the consumer electronics market. To get additional performance gains, OEMs are moving to our even higher value integrated audio solutions with microphones and an antenna in a plastic module.

For products that were introduced more than 18 months ago, we have consistently offset projected price erosion through bill of material cost reductions, yield improvements, equipment efficiency and labor reductions.

In the specialty components segment, the end markets are more stable, and mix of products and customers are drivers of average selling prices and margin.

Customers, Sales and Distribution

We serve customers in the mobile consumer electronics, medical technology, defense/aerospace, telecommunication infrastructure and other industrial markets. Our customers include some of the largest operators in these markets. In addition, many of our OEM customers outsource their manufacturing to Electronic Manufacturing Services ("EMS") companies. Other customers include global cell phone and hearing aid manufacturers and many of the largest global EMS companies, particularly in China. For the year ended December 31, 2013, Apple, Inc. and Samsung Group accounted for approximately 25% and 15%, respectively, of our total revenue. For the years ended December 31, 2012 and 2011, Apple, Inc. accounted for approximately 18% and 12%, respectively, of our total revenue. No other customer accounted for more than 10% of total revenues during these periods.

Table of Contents

The following table details our sales by geographic location for the years ended December 31, 2013, 2012 and 2011. These results do not necessarily indicate the geographies where our products are deployed or where end-customer demand is originated.

| (in thousands) | Years Ended December 31, | | |
|---|---|---|---|
| | 2013 | 2012 | 2011 |
| Asia | $950,449 | $855,450 | $681,740 |
| Europe | 120,751 | 110,559 | 139,207 |
| Other Americas | 14,479 | 15,182 | 14,849 |
| Other | 6,063 | 6,901 | 9,404 |
| Subtotal non-U.S. | $1,091,742 | $988,092 | $845,200 |
| United States | 123,061 | 129,900 | 138,118 |
| Total | $1,214,803 | $1,117,992 | $983,318 |

We own and conduct manufacturing operations through a network of facilities throughout the world. We also maintain quality assurance, manufacturing technology, supply chain and distribution departments. Our global distribution center is located in Penang, Malaysia. For our long-lived assets by geographic region, see Note 15. Segment Information of the notes to the Combined Financial Statements under Item 8, "Financial Statements and Supplementary Data."

Raw Materials

We use a wide variety of raw materials, primarily metals and semi-processed or finished components, which are generally available from a number of sources. As a result, shortages or the loss of any single supplier have not had, and are not likely to have, a material impact on operating profits. While the required raw materials are generally available, commodity pricing for various precious metals, such as palladium, gold and silver and “rare earth” materials (dysprosium and neodymium), fluctuates. As a result, our operating results are exposed to such fluctuations. Although some cost increases may be recovered through increased prices to customers if commodity prices trend upward, we attempt to control such costs through fixed-price contracts with suppliers and various other programs.

We have established a Green Materials Policy. The products offered are in compliance with the European Union Restriction of Hazardous Substances ("EU RoHS") and Waste Electrical and Electronic Equipment ("WEEE") directives. This standard is based on the list of substances identified in the Joint Industry Guide-101 Standard which is endorsed by the Electronic Industry Association, the Joint Electronics Device Engineering Council and the Japan Green Procurement Survey Standardization Initiative associations as well as the Sony Standard-00259.

Research and Development

We conduct research worldwide to discover and develop new acoustic and related products around the world and refine our existing products. Our research is primarily conducted internally. We employ approximately 400 employees worldwide in research and development. Our research and development efforts continue to expand the technology platforms that support our customers’ product and business development. By applying interrelated technologies to the design processes, we strive to enhance and accelerate our customers’ initial concepts and design work, as well as provide for cost-effective component customization, manufacturing and subassembly. Research and development expenses are classified within selling and administrative expense. We spent $82.6 million, $77.3 million and $65.9 million on research and development, or 6.8%, 6.9% and 6.7% as a percentage of revenue, for the years ended December 31, 2013, 2012 and 2011, respectively.

Intellectual Property and Intangible Assets

We own many patents, trademarks, licenses and other forms of intellectual property, which have been acquired over a number of years and, to the extent relevant, expire at various times over a number of years. A large portion of our intellectual property consists of patents, unpatented technology and proprietary information constituting trade secrets that we seek to protect in various ways, including confidentiality agreements with employees and suppliers, where appropriate. In addition, a significant portion of our intangible assets relate to customer relationships. While our intellectual property and customer relationships are important to our success, the loss or expiration of any of these rights or relationships, or any group of related rights or relationships, is not likely to materially affect our results on a combined basis. We believe that our commitment to continuous engineering improvements, new product development and improved manufacturing techniques, as well as strong sales, marketing and service efforts, are significant to our general leadership positions in the niche markets that we serve.

Table of Contents

## Seasonality

In general, our businesses, while not having significant seasonality, tend to have stronger revenue in the third and fourth quarters of each calendar year. This is particularly true of those businesses that serve the consumer electronics market. Our businesses tend to have short product cycles due to the highly technical nature of the industries they serve which can result in new OEM product launches that can impact quarterly revenues, earnings and cash flow.

## Environmental Matters

Our operations are governed by a variety of international, national, state and local environmental laws. These regulations include limitations on discharge of pollutants to air, water, and soil; manufacturing chemical use and handling restrictions; and requirements with respect to treatment, transport, storage and disposal of solid and hazardous wastes. We are committed to continued compliance and believe our operations generally are in substantial compliance with these laws.

We are dedicated to the preservation and improvement of our global environment. To help achieve this, we have established a Green Materials Policy pursuant to which we have established a Green Materials Standard. The products we offer are in compliance with the EU RoHS/WEEE regulations. Additionally, our products have been assessed and meet industry, customer, and regulatory requirements.

## Employees

We currently employ more than 10,000 persons across our facilities in 14 countries. Approximately 79% of these employees are located in facilities across Asia. We maintain strong labor relations throughout all of our facilities.

## Regulation

It has been our long-standing policy to maintain the highest ethical standards in the conduct of our affairs and in our relationship with customers, suppliers, employees and the communities in which our operations are located. In accordance with the Electronics Industry Citizenship Coalition, the Electronic Industry Code of Conduct and applicable laws in each country where we operate, including the U.S. Foreign Corrupt Practices Act, the U.K. Bribery Act and other countries' anti-corruption laws, we strive to ensure that working conditions are safe, our employees are treated with respect and dignity, and business operations are environmentally responsible and comply with all applicable laws. In addition, we proactively educate our suppliers and carry out our commitment to seek out business partners who share our values and, in accordance with our Supplier Code of Conduct, specifically prohibit our suppliers from using forced, bonded, involuntary, prison, or indentured labor.

## Other Information

We will make available through the "Financial Information" link on the Investor Relations section of our Internet website, www.knowles.com, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to these reports. We will post each of these reports on the website as soon as reasonably practicable after the report is filed with the Securities and Exchange Commission. The information on our Internet website is not incorporated into this Form 10-K.

Table of Contents

## ITEM 1A. RISK FACTORS

Our business, financial condition, operating results, cash flows and stock price can be impacted by a number of factors which could cause our actual results to vary materially from recent results or from anticipated future results. In general, we are subject to the same general risks and uncertainties that impact many other companies such as general economic, industry and/or market conditions and growth rates; the impact of natural disasters and their effect on global markets; possible future terrorist threats and their effect on the worldwide economy; and changes in laws or accounting rules. The risk factors discussed in this section should be considered together with information included elsewhere in this Form 10-K and should not be considered the only risks to which we are exposed.

### Risks Related to Our Business

- Our results may be impacted by domestic and international economic, legal, currency, political and compliance conditions and uncertainties.

Worldwide economic and capital market conditions are beyond our control, are highly unpredictable, and can have an adverse effect on our revenue, earnings, cash flows and cost of capital. We have significant operations in Austria, China, Germany, Malaysia, the Philippines, the United Kingdom and the United States. Our businesses may be adversely affected by disruptions in the financial markets or declines in economic activity both domestically and internationally in the countries where we operate or from which we derive substantial revenues. These circumstances will also impact our suppliers and customers in various ways which could have an impact on our business operations, particularly if global credit markets are not operating efficiently and effectively to support industrial commerce.

Our domestic and international sales and operations are subject to risks associated with changes in local government laws (including environmental and import/export laws), regulations and policies. Failure to comply with any of these laws could result in civil and criminal, monetary and non-monetary penalties and damage to our reputation. In addition, we cannot provide assurance that our costs of complying with new and evolving regulatory reporting requirements and current or future laws, including environmental protection, employment and health and safety laws, will not exceed our estimates. In addition, we have invested in certain countries, including Malaysia, China, the Philippines and Ukraine, that carry high levels of currency, political, compliance and/or economic risk. While these risks or the impact of these risks are difficult to predict, any one or more of them could adversely affect our businesses and reputation.

- We are subject to risks relating to our existing international operations and to expanding our global business.

Many of our manufacturing operations and suppliers are located outside the United States, and we continue to focus on global markets as part of our growth strategy. Our international operations and global expansion strategy are subject to various risks, including:

- political, social and economic instability and disruptions;
- government embargoes or trade restrictions;
- the imposition of duties and tariffs and other trade barriers;
- import and export controls;
- transportation delays and interruptions;

- labor unrest and current and changing regulatory environments;
- increased compliance costs, including costs associated with disclosure requirements and related due diligence;
- the impact of loss of one or more of our manufacturing facilities;
- difficulties in staffing and managing multi-national operations;
- limitations on our ability to enforce legal rights and remedies and the costs of such enforcement; and
- environmental liabilities arising from our current, historical and future operations and manufacturing sites.

If we are unable to successfully manage the risks associated with expanding our global business or adequately manage operational risks of our existing international operations, the risks could have a material adverse effect on our growth strategy involving expansion into new geographical markets or our results of operations and financial position.

- We face risks arising from the restructuring of our operations globally.

We continuously evaluate our operations and cost structure relative to general economic conditions, market demands, tax rates, foreign currency fluctuations, cost competitiveness and our geographic footprint. As a result of this ongoing evaluation, we plan to reduce our 18 facilities worldwide to 11 by the end of 2016 and will engage in restructuring activities from time to time. The restructuring process includes moving production between facilities or to new facilities, closing facilities, reducing staff levels, realigning our business processes and reorganizing our management.

Restructurings present significant potential risks that could adversely affect our businesses, including delays in finalizing the scope of, and implementing, the restructurings (including extensive consultations concerning potential workforce reductions and obtaining agreements from our affected customers for the relocation of our facilities in certain instances), the failure to achieve targeted cost savings, impacts on product quality and delivery interruptions, the failure to meet operational targets and customer requirements, and the acceleration of obligations to fund pension liabilities. These risks are further complicated by our international footprint, which subject us to various legal and regulatory requirements that govern the extent and speed of our ability to restructure our operations.

- If we are not able to anticipate, adapt to and capitalize on technological developments, we may not be able to sustain or grow our current level of revenues, operating profits or cash flows.

We sell our products in electronic and technology-based industries that are highly competitive, dynamic and constantly experiencing change as new technologies are developed. It is characteristic of such industries that sales prices for products decline over time following their introduction to market due to technological obsolescence and the introduction of new technologies. Downward pressure on product prices typically causes downward pressure on component prices as well. Our ability to compete depends on our ability to innovate successfully.

Our competitors may produce products that are more advanced than the products we produce. If our businesses are unable to anticipate our competitors' development of new products and services, identify customer needs and preferences on a timely basis, or successfully introduce new products and services in response to such competitive factors, including new or enhanced products with higher margins to offset price declines, we may experience lower revenue, operating profits and cash flows. In addition, if we are unable to adapt to the rapid technological changes (which include hiring and retaining top engineering talent), or for those products which are subject to declining average selling prices, we are unable to increase our unit volumes, introduce new or enhanced products with higher margins and/or reduce manufacturing costs to offset price decreases in existing products, our products could become obsolete or commoditized, and business and operating results may be materially adversely affected.

- Our products must undergo lengthy and expensive qualification processes without any assurance of product sales. The costs associated with new product introductions and imbalances between customer demand and capacity could negatively impact our operating results and profits.

A significant portion of our revenue is derived from products that are required to go through extensive customer qualification processes before being selected by customers for inclusion in their products under development. We devote substantial resources, including design, engineering, sales, marketing and management efforts, to these qualification processes. Our products may not be designed into a customer's product despite our investment in the qualification process, which could adversely impact our operating results and profits.

Even if our products are designed into a customer's product, the customer's product may not be commercially successful, or the customer's commercial plans for the product could change, which could adversely impact our sales and operating results. Similarly, a modification to the product or manufacturing process, or the selection of a new supplier by us, may require new qualification processes, which may result in delays, cause us to forego sales for the remainder of the life of the customer’s product and/or hold excess or obsolete inventory.

In addition, when our customers introduce new products, the time required and costs incurred by us to ramp up production can be significant. Certain non-recurring costs and expenditures for tooling and other equipment may not be reusable in manufacturing products for other customers or different products for the same customer. Product ramp-ups typically involve greater volumes of scrap, higher costs due to inefficiencies and delays in production, all of which can adversely impact our operating results and profits.

Table of Contents

Our operating results and profits could be adversely affected if we are unable to balance customer demand for our products and capacity. If demand increases and we are unable to increase our production capacity to meet the demand, or if there are unforeseen costs associated with adjusting our capacity levels, we may not be able to achieve our financial targets. Conversely, if demand does not increase at the rate forecasted, we may not be able to adequately absorb manufacturing expenses or overhead costs which could negatively impact our product margins. Additionally, if product demand decreases or we fail to forecast demand accurately, we may be required to record impairments on our long-lived assets or record other charges.

Any of these developments could have a material adverse impact on our sales and operating results. In addition, to the extent a customer has a “dual source” strategy whereby customers may purchase products from more than one supplier, we may realize lower sales from our products that are designed into the customer’s products.

- We could lose customers or generate lower revenue, operating profits and cash flows if there are significant increases in the cost of raw materials or if we are unable to obtain raw materials.

We purchase raw materials, sub-assemblies and components for use in manufacturing operations, which exposes us to volatility in prices for certain commodities. Significant price increases for these commodities could adversely affect operating profits for certain of our businesses. While we generally attempt to mitigate the impact of increased raw material prices by hedging or passing along the increased costs to customers, there may be a time delay between the increased raw material prices and the ability to hedge the price increase or increase the prices of products, or we may be unable to increase the prices of products due to a competitor’s pricing pressure or other factors. In addition, the inability to obtain necessary raw materials could affect our ability to meet customer commitments and satisfy market demand for certain products. Consequently, a significant price increase in raw materials, including certain rare earth materials, or their unavailability, may result in a loss of customers and adversely impact revenue, operating profits and cash flows.

We and our suppliers rely upon certain rare earth materials that are necessary for the manufacturing of our products, and our business could be harmed if we or our suppliers experience shortages or delays of these rare earth materials. We and/or our suppliers acquire these materials from a number of countries, including China. More than 95% of the world’s current supply of rare earth materials comes from China, which has enacted a policy to reduce its exports because of its rising domestic demand and new environmental restrictions. We cannot predict whether the government of China or any other nation will impose further regulations, quotas or embargoes upon these materials that would restrict their worldwide supply or increase their cost. If China or any other major supplier were to further restrict the supply available or increase the cost of the materials used in our products, we could experience a shortage in supply and an increase in production costs, which would harm our operating results.

- We rely on sole source and limited source suppliers for certain supplies of critical raw materials and components.

Our operations depend on obtaining sufficient supplies of raw materials and components used in our manufacturing processes. In particular, certain of our businesses rely on wafer fabrication facilities or foundries which are limited source suppliers to provide silicon-based products that are critical components of our products and to provide such products in sufficient quantities to meet our production needs. Although we have long-term supply arrangements with these foundries, they may experience financial difficulties, be unable to deliver product to us in a timely manner, have insufficient capacity to meet our requirements, or suffer business disruption resulting from damage to or destruction of their facilities due to natural disasters, and we might not be able to secure an alternative source of supply in a timely manner. These events could have a material adverse impact on our results of operations.

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*Customer requirements and new regulations may increase our expenses and impact the availability of certain raw materials, which could adversely affect our revenue and operating profits.*

Our businesses use parts or materials that are impacted by the Dodd-Frank Wall Street Reform and Consumer Protection Act requirement for disclosure of the use of “conflict minerals” mined in the Democratic Republic of the Congo and adjoining countries. Some of our customers require “conflict free” metals in products purchased from us. We have been following a process to comply with both regulatory and customer requirements. However, the supply chain due diligence and verification of sources require substantial periods of time to complete based on the current availability of origin information and the number of vendors. We may not be able to complete the process in the time frame required because of the complexity of our supply chain. Other governmental social responsibility regulations also may impact our suppliers, manufacturing operations and operating profits.

Table of Contents

The need to find alternative sources for certain raw materials or products because of customer requirements and regulations may impact our ability to secure adequate supplies of raw materials or parts, lead to supply shortages, or adversely impact the prices at which our businesses can procure compliant goods.

- Our effective tax rate may fluctuate and it could be subject to additional tax liabilities, including in the event of repatriation of our overseas earnings to fund our liquidity needs.

Our effective tax rate may be adversely impacted by changes in the mix of our earnings among countries with differing statutory tax rates, changes in the valuation allowance of deferred tax assets and changes in tax laws. We cannot give any assurance as to what our effective tax rate will be in the future because of, among other things, uncertainty regarding the tax policies of the jurisdictions where we operate. Further, our tax returns are subject to periodic audits by domestic and international authorities. If these audits result in allocations of income or other tax assessments different from amounts estimated, then our financial results may be adversely affected by unfavorable tax adjustments.

Our effective tax rate is favorably impacted by a significant tax holiday granted to us by Malaysia. This tax holiday is subject to our satisfaction of certain conditions, including exceeding certain annual thresholds of operating expenses and gross sales. We expect to continue to satisfy all of the conditions to this tax holiday. If we fail to satisfy such conditions, our effective tax rate may be significantly adversely impacted. For additional detail, see Note 10. Income Taxes of the notes to our Combined Financial Statements under Item 8, "Financial Statements and Supplementary Data."

In addition, if we encounter a significant need for liquidity domestically or at a particular location that we cannot fulfill through borrowings, equity offerings or other internal or external sources, we may experience unfavorable tax and earnings consequences due to cash repatriations. These adverse consequences would occur, for example, if the transfer of cash into the United States is taxed and no foreign tax credit is available to offset the U.S. tax liability, resulting in lower earnings. Foreign exchange ceilings imposed by local governments and the sometimes lengthy approval processes that foreign governments require for international cash transfers may delay our internal cash transfers from time to time. These factors may cause us to have an overall tax rate higher than other companies or higher than our tax rates have been in the past.

- Our revenue, operating profits and cash flows could be adversely affected if our businesses are unable to protect or obtain patent and other intellectual property rights, or to do so at expected cost levels, or if intellectual property litigation is successful against us.

We own patents, trademarks, licenses and other forms of intellectual property related to our products. Our businesses employ various measures to maintain and protect our intellectual property, including enforcing our intellectual property rights through litigation. While we have been successful to date in maintaining and protecting our intellectual property, these measures may not prevent our intellectual property from being challenged, invalidated or circumvented and our businesses may not be successful in litigation or other actions to enforce our intellectual property rights, particularly in countries where intellectual property rights are not highly developed or protected. Unauthorized use of these intellectual property rights could adversely impact the competitive position of our businesses and have a negative impact on revenue, operating profits and cash flows. Regardless of the merits of any specific claim, the expense of protecting and enforcing our intellectual property, or defending claims that our products or technology infringe the intellectual rights of others, can vary significantly period to period and, in any given period, could be material and divert the attention of management and key technical personnel. Further, regardless of the merits of any specific claim, we may not prevail in litigation because of the complex technical issues and uncertainties inherent in intellectual property litigation. If any such litigation or claims were to result in an adverse ruling, we could be required to:

- pay substantial damages;
- cease the manufacture, import, use, sale or offer for sale of infringing products or processes;
- discontinue the use of infringing technology;
- expend significant resources to develop non-infringing technology; and
- enter into royalty or license agreements from the third party claiming infringement, which license may not be available on commercially reasonable terms.

Table of Contents

Our operating results or financial condition may be materially adversely affected if we, or one of our customers, were required to take any one or more of the foregoing actions. In addition, if one of our customers or another supplier to one of our customers were found to have infringed the intellectual property rights of a third party, the supplier or customer could be ordered to cease the manufacture, import, use, sale or offer for sale of its infringing product(s) or process(es), any of which could result, indirectly, in a decrease in demand for our products. If such a decrease in demand for our products were to occur, it could have an adverse impact on our operating results and financial condition.

- Our growth and results of operations may be adversely affected if we are unsuccessful in our capital allocation and acquisitions program.

We expect to pursue a strategy of acquiring value-creating add-on businesses that broaden our existing position and global reach as well as, in the right circumstances, strategically pursuing larger acquisitions that could have the potential to either complement our existing businesses or allow us to pursue a new growth opportunity. However, there can be no assurance that we will be able to find suitable businesses to purchase or that we will be able to acquire such businesses on acceptable terms. If we are unsuccessful in our acquisition efforts, then our ability to grow could be adversely affected. In addition, a completed acquisition may underperform relative to expectations, may be unable to achieve synergies originally anticipated, or may expose us to unexpected liabilities. Further, if we fail to allocate capital appropriately, in respect of either our acquisition program or organic growth in operations, we could be overexposed in certain markets and geographies.

Additionally, we may be required to record a significant charge to earnings if our goodwill, other intangible assets or long-lived assets become impaired. Goodwill and purchased intangible assets with indefinite lives are not amortized, but are reviewed for impairment annually and more frequently when events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. We assess the recoverability of the unamortized balance of our definite-lived intangible assets when indicators of potential impairment are present. Factors that may indicate that the carrying value of goodwill or other intangible assets may not be recoverable include a decline in stock price and market capitalization and slower growth rates in our industry. We may be required to record a significant charge to earnings in our financial statements during the period in which any impairment of our goodwill or other intangible assets is determined to exist.

These factors could potentially have an adverse impact on our operating profits and cash flows.

- Failure to attract, retain and develop personnel or to provide adequate succession plans for key management could have an adverse effect on our operating results.

Our growth, profitability and effectiveness in conducting our operations and executing our strategic plans depend in part on our ability to attract, retain and develop qualified personnel, align them with appropriate opportunities and maintain adequate succession plans for key management positions. If we are unsuccessful in these efforts, our operating results could be adversely affected.

- We may face wage inflation and increased competition for our employees in the countries where we operate, which could increase our employment costs and our attrition.

Wage costs in Asia and other regions in which we operate have historically been significantly lower than wage costs in developed countries. However, wage increases in these countries where we operate may increase our costs, reduce our profit margins and adversely affect our business and results of operations. We may not be able to pass these increased costs on to our customers by increasing the price we charge for our products. If this occurs, our profits may decline.

Competition in Asia and other regions in which we operate for skilled-labor has increased, and we expect this competition will continue to increase as additional companies enter the market and expand their operations. If the availability of skilled-labor decreases, it could affect the availability and the cost of employees and increase our attrition rate, all of which may have an adverse effect on our operating results.

Table of Contents

- Our business operations may be adversely affected by information systems interruptions or intrusion.

Our businesses rely on a number of information technologies to manage, store and support business activities. We have put in place a number of systems, processes and practices designed to protect against intentional or unintentional misappropriation or corruption of our systems and information, disruption of operations or corruption of the software that supports our products. Disruptions or cybersecurity attacks, such as unauthorized access, malicious software or other violations, may lead to exposure of proprietary or confidential information as well as potential data corruption. Any intrusion may cause operational stoppages, violations of applicable law, diminished competitive advantages or reputational damages, and increased operational costs due to remedial activities. The theft or unauthorized use or publication of our trade secrets and other confidential business information resulting from a breach of our information systems could adversely affect our competitive position and the value of our investment in research and development.

- Our reputation, ability to do business and results of operations may be impaired by improper conduct by any of our employees, agents or business partners.

While we strive to maintain high standards, we cannot provide assurance that our internal controls and compliance systems will always protect us from acts committed by employees, agents or business partners that would violate U.S. and/or non-U.S. laws or fail to protect our confidential information, including the laws governing payments to government officials, bribery, fraud, anti-kickback and false claims rules, competition, export and import compliance, money laundering and data privacy laws, as well as the improper use of proprietary information or social media. Any such violations of law or improper actions could subject us to civil or criminal investigations in the U.S. and in other jurisdictions, could lead to substantial civil or criminal, monetary and non-monetary penalties and related shareholder lawsuits and could damage our reputation.

- Our exposure to exchange rate fluctuations on cross-border transactions and the translation of local currency results into U.S. dollars could negatively impact our results of operations.

We conduct business through our subsidiaries in many different countries, and fluctuations in currency exchange rates could have a significant impact on the reported results of operations, which are presented in U.S. dollars. A significant and growing portion of our products are manufactured in lower-cost locations and sold in various countries. Cross-border transactions, both with external parties and intercompany relationships, result in increased exposure to changes in foreign exchange rates. Accordingly, significant changes in currency exchange rates, particularly the Malaysian ringgit, the euro, the Chinese renminbi (yuan) and the Philippine peso, could cause fluctuations in the reported results of our businesses' operations that could negatively affect our results of operations. A weakening of the U.S. dollar could adversely impact the cost of materials, products and services purchased outside the U.S. and therefore adversely affect our results of operations. In addition, sales and expenses of our non-U.S. businesses are translated into U.S. dollars for reporting purposes and therefore any weakening of the U.S. dollar could result in unfavorable translation effects.

- We depend on a limited number of customers for a substantial portion of our revenues, and the loss of, or a significant reduction in orders from, any key customer could significantly reduce our revenues and adversely impact our operating results.

We rely on several key customers. For 2013, our top ten customers accounted for approximately 65% of total revenue. For the year ended December 31, 2013, Apple, Inc. and Samsung Group accounted for approximately 25% and 15%, respectively, of our total revenue. For the years ended December 31, 2012 and 2011, Apple, Inc. accounted for approximately 18% and 12%, respectively, of our total revenue. We expect that a substantial portion of our revenue will continue to be attributable to several key customers. If these customers decide not to buy our products or to purchase lower volumes from us because their own products are not commercially successful or for other reasons, our revenues could substantially decline, which could have a material adverse effect on our results of operations.

The markets we serve are concentrated, with a limited number of companies active in these markets. A concentrated market and reliance on a small number of customers gives those customers substantial purchasing power and leverage in negotiating contracts with us. In addition, we do not have long-term agreements or purchase orders with any of our customers, our customers have irregular and unpredictable ordering patterns, and our customers may not have regular, predictable product introduction schedules. A decision by any of our major customers to decrease significantly the number of products purchased from us could substantially reduce sales and have a material adverse effect on our business, financial condition and results of operations.

• Some of our businesses are subject to the cycles inherent in the consumer electronics industry.

The consumer electronics industry is cyclical and characterized by continuous and rapid technological change, product obsolescence, price erosion, evolving standards, short product life cycles and significant fluctuations in product supply and demand. Markets or the markets for specific products incorporating our solutions may not continue to grow or may decline for a number of reasons outside of our control, including competition among companies and market saturation.

This industry experienced a significant downturn as part of the broader global recession in 2008 and 2009. Industry downturns have been characterized by diminished product demand, production overcapacity, high inventory levels and accelerated erosion of average selling prices. Future downturns could have a material adverse effect on our business and operating results.

• Costs related to product defects and errata may harm our results of operations and business.

Adverse consequences associated with unexpected product defects and errata (deviations from published specifications) due to, for example, unanticipated problems in our design and manufacturing processes, could include writing off or reserving the value of inventory of such products; disposing of products that cannot be fixed; recalling such products that have been shipped to customers; providing product replacements for, or modifications to, such products; and defending against litigation related to such products. The costs associated with these occurrences could be substantial and may temporarily increase our expenses and lower our margins and profitability. In addition, our reputation could be damaged as a result of such product defects and errata, and the demand for our products could be reduced.

Risks Related to Our Recent Separation

• We have limited history operating as an independent publicly-traded company, and our historical financial information is not necessarily representative of the results that we would have achieved as a separate, publicly-traded company and therefore may not be a reliable indicator of our future results.

We were spun-off from our Former Parent on February 28, 2014, and have limited operating history as an independent publicly-traded company. The historical information about us in this Form 10-K refers to Knowles' business as part of our Former Parent. Our historical financial information included in this Form 10-K is derived from the Combined Financial Statements and accounting records of our Former Parent. Accordingly, our historical financial information does not necessarily reflect the financial condition, results of operations or cash flows that we would have achieved as an independent publicly-traded company during the periods presented or those that we will achieve in the future primarily as a result of the factors described below:

- We have made, and will need to continue to make, significant investments to replicate or outsource certain systems, infrastructure and functional expertise as a result of the Separation. These initiatives to develop our independent ability to operate without access to our Former Parent's existing operational and administrative infrastructure will be costly to implement. We may not be able to operate our business at comparable costs, and our profitability may decline.

- Prior to the Separation, we relied upon our Former Parent for working capital requirements and other cash requirements, including in connection with our previous acquisitions. As a result of the Separation, our Former Parent ceased providing us with funds to finance our working capital or other cash requirements. After the Separation, our access to and cost of debt financing may be different from the historical access to and cost of debt financing from our Former Parent. Differences in access to and cost of debt financing may result in differences in the interest rate charged to us on financings, as well as the amounts of indebtedness, types of financing structures and debt markets that may be available to us, which could have an adverse effect on our business, financial condition and results of operations and cash flows.

For additional information about the past financial performance of our business and the basis of presentation of the historical Combined Financial Statements of our business, see the sections entitled “Selected Financial Data” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and the historical financial statements and accompanying notes under Item 8, “Financial Statements and Supplementary Data.”

Table of Contents

- Our Former Parent may fail to perform under various transaction agreements that were executed as part of the Separation or we may fail to have necessary systems and services in place when certain of the transaction agreements expire.

We and our Former Parent entered into certain agreements in connection with the Separation, such as a separation and distribution, tax matters and employee matters agreements providing for certain indemnification obligations and a transition services agreement providing for the performance of services by our Former Parent for the benefit of us for a period of time after the Separation. We will rely on our Former Parent to satisfy its performance and payment obligations under these agreements. If our Former Parent is unable to satisfy its obligations under these agreements, including its indemnification obligations, we could incur operational difficulties or losses.

If we do not have agreements with other providers of these services when the transitional or long-term agreements terminate, or if we do not implement new systems or replace our Former Parent's services successfully, we may not be able to operate our business effectively, which could disrupt our business and have a material adverse effect on our business, financial condition and results of operations. These systems and services may also be more expensive to install, implement and operate, or less efficient, than the systems and services our Former Parent is expected to provide during the transition period.

- Potential indemnification liabilities to our Former Parent pursuant to the separation and distribution agreement could materially and adversely affect our business, financial condition, results of operations and cash flows.

The separation and distribution agreement between us and our Former Parent, among other things, provides for indemnification obligations (for uncapped amounts) designed to make us financially responsible for substantially all liabilities that may exist relating to our business activities, whether incurred prior to or after the Separation. If we are required to indemnify our Former Parent under the circumstances set forth in the separation and distribution agreement, we may be subject to substantial liabilities.

- In connection with the Separation, our Former Parent has agreed to indemnify us for certain liabilities. However, there can be no assurance that the indemnity will be sufficient to insure us against the full amount of such liabilities, or that our Former Parent's ability to satisfy its indemnification obligation will not be impaired in the future.

Pursuant to the separation and distribution agreement and certain other agreements with our Former Parent, our Former Parent has agreed to indemnify us for certain liabilities. However, third parties could also seek to hold us responsible for any of the liabilities that our Former Parent has agreed to retain, and there can be no assurance that the indemnity from our Former Parent will be sufficient to protect us against the full amount of such liabilities, or that our Former Parent will be able to fully satisfy its indemnification obligations. In addition, our Former Parent's insurers may attempt to deny coverage to us for liabilities associated with certain occurrences of indemnified liabilities prior to the Separation. Moreover, even if we ultimately succeed in recovering from our Former Parent or such insurance providers any amounts for which we are held liable, we may be temporarily required to bear these losses. Each of these risks could negatively affect our business, financial position, results of operations and cash flows.

- We are subject to continuing contingent liabilities of our Former Parent following the Separation.

After the Separation, there are several significant areas where the liabilities of our Former Parent may become our obligations. For example, under the Internal Revenue Code of 1986, as amended (the "Code") and the related rules and regulations, each corporation that was a member of our Former Parent's U.S. consolidated group during a taxable period or portion of a taxable period ending on or before the effective time of the distribution is jointly and severally liable for the U.S. federal income tax liability of the entire U.S. consolidated group of our Former Parent for that taxable period. Consequently, if our Former Parent is unable to pay the consolidated U.S. federal income tax liability for a prior period, we could be required to pay the entire amount of such tax which could be substantial and in excess of the amount allocated to us under the tax matters agreement between us and our Former Parent. Other provisions of federal and state law establish similar liability for other matters, including laws governing tax-qualified pension plans as well as other contingent liabilities.

Table of Contents

- If the Distribution (as defined below), together with certain related transactions, does not qualify as a transaction that is generally tax-free for U.S. federal income tax purposes, we, our Former Parent and our shareholders could be subject to significant tax liability and, in certain circumstances, we could be required to indemnify our Former Parent for material taxes pursuant to indemnification obligations under the tax matters agreement.

Our Former Parent has received an opinion of Baker & McKenzie LLP, tax counsel to our Former Parent, substantially to the effect that, among other things, the distribution of all of the shares of our common stock owned by our Former Parent to shareholders of our Former Parent in connection with the Separation (the “Distribution”) will qualify as tax-free for U.S. federal income tax purposes under Sections 368(a)(1)(D) and 355 of the Code. The opinion of tax counsel relied on certain facts, assumptions, representations and undertakings from our Former Parent and us, including those regarding the past and future conduct of the companies’ respective businesses and other matters. If any of these facts, assumptions, representations or undertakings are incorrect or not satisfied, our Former Parent and its shareholders may not be able to rely on the opinion, and could be subject to significant tax liabilities. Notwithstanding the opinion of tax counsel, the IRS could determine on audit that the Distribution is taxable if it determines that any of these facts, assumptions, representations or undertakings are not correct or have been violated or if it disagrees with the conclusions in the opinion. In addition, we and our Former Parent intend for certain related transactions to qualify for tax-free treatment under federal, state and local tax law and/or foreign tax law.

If the Distribution is determined to be taxable for U.S. federal income tax purposes, our Former Parent and its shareholders that are subject to U.S. federal income tax could incur significant U.S. federal income tax liabilities. For example, if the Distribution fails to qualify for tax-free treatment, our Former Parent would for U.S. federal income tax purposes be treated as if it had sold the Knowles common stock in a taxable sale for its fair market value, and our Former Parent’s shareholders, who are subject to U.S. federal income tax, would be treated as receiving a taxable distribution in an amount equal to the fair market value of the Knowles common stock received in the Distribution. In addition, if certain related transactions fail to qualify for tax-free treatment under federal, state and local tax law and/or foreign tax law, our Former Parent (and, under the tax matters agreement described below, Knowles) could incur significant tax liabilities under U.S. federal, state, local and/or foreign tax law.

Under the tax matters agreement between our Former Parent and us, we would generally be required to indemnify our Former Parent against taxes incurred by our Former Parent that arise as a result of our taking or failing to take, as the case may be, certain actions that result in the Distribution failing to meet the requirements of a tax-free distribution under Section 355 of the Code or of such related transactions failing to qualify for tax-free treatment. Also, under the tax matters agreement, we would generally be required to indemnify our Former Parent for one-half of the taxes and other liabilities incurred by our Former Parent if the Distribution fails to meet the requirements of a tax-free distribution under Section 355 of the Code for reasons other than an act or failure to act on the part of us or our Former Parent, and therefore we might be required to indemnify our Former Parent for such taxes and liabilities due to circumstances and events not within our control. Under the tax matters agreement, we are also required to indemnify our Former Parent for one-half of certain taxes incurred as a result of the restructuring activities undertaken to effectuate the Distribution or as a result of the application of certain rules relating to consolidated federal income tax returns, whether payable upon filing tax returns related to the restructuring and Distribution or upon a subsequent audit of those returns. Our indemnification obligations to our Former Parent under the tax matters agreement are not limited by a maximum amount. If we are required to indemnify our Former Parent under the circumstances set forth in the tax matters agreement, we may be subject to substantial liabilities, which could materially adversely affect our financial position.

Table of Contents

• We may not be able to engage in certain corporate transactions as a result of the Separation.

To preserve the tax-free treatment to our Former Parent and its shareholders of Distribution and certain related transactions, under the tax matters agreement between us and our Former Parent, we are restricted from taking any action following the Distribution that prevents the Distribution and related transactions from being tax-free for U.S. federal income tax purposes. Under the tax matters agreement, for the two-year period following the Distribution, we will be prohibited, except in certain circumstances, from:

- entering into any transaction resulting in the acquisition of 40% or more of our stock or substantially all of our assets, whether by merger or otherwise;
- merging, consolidating or liquidating;
- issuing equity securities beyond certain thresholds;
- repurchasing our capital stock; and
- ceasing to actively conduct our business.

These restrictions may limit our ability to pursue certain strategic transactions or other transactions that we may believe to be in the best interests of our shareholders or that might increase the value of our business. In addition, under the tax matters agreement, we are required to indemnify our Former Parent against any such tax liabilities as a result of the acquisition of our stock or assets, even if we did not participate in or otherwise facilitate the acquisition.

• The Separation and related internal restructuring transactions may expose us to potential liabilities arising out of state and federal fraudulent conveyance laws and legal dividend requirements.

If our Former Parent files for bankruptcy or is otherwise determined or deemed to be insolvent under federal bankruptcy laws, a court could deem the Separation or certain internal restructuring transactions undertaken by our Former Parent in connection with the Separation to be a fraudulent conveyance or transfer. Fraudulent conveyances or transfers are defined to include transfers made or obligations incurred with the actual intent to hinder, delay or defraud current or future creditors or transfers made or obligations incurred for less than reasonably equivalent value when the debtor was insolvent, or that rendered the debtor insolvent, inadequately capitalized or unable to pay its debts as they become due. A court could void the transactions or impose substantial liabilities upon us, which could adversely affect our financial condition and our results of operations. Among other things, the court could require our shareholders to return to our Former Parent some or all of the shares of our common stock issued in the Separation, or require us to fund liabilities of other companies involved in the restructuring transactions for the benefit of creditors.

The distribution of Knowles' common stock is also subject to review under state corporate distribution statutes. Under the Delaware General Corporation Law ("DGCL"), a corporation may only pay dividends to its shareholders either (i) out of its surplus (net assets minus capital) or (ii) if there is no such surplus, out of its net profits for the fiscal year in which the dividend is declared and/or the preceding fiscal year. Although our Former Parent intended to make the distribution of Knowles' common stock entirely out of surplus, we cannot make any assurance that a court will not later determine that some or all of the distribution to the shareholders of our Former Parent was unlawful.

• Certain of our executive officers and directors may have actual or potential conflicts of interest because of their previous or continuing positions at our Former Parent.

Because of their former or continuing positions with our Former Parent, certain of our executive officers and directors own equity interests in our Former Parent. Even though our Board of Directors consists of a majority of directors who are independent, and our executive officers who were previously employees of our Former Parent ceased to be employees of our Former Parent upon the Separation and their equity awards from our Former Parent were converted to equity awards from our Company in connection with the Separation, some of our executive officers and directors continue to have a financial interest in shares of our Former Parent's common stock. In addition, certain of our directors continue to serve on the Board of Directors of our Former Parent. Continuing ownership of shares of our Former Parent's common stock, or service as a director at both companies could create, or appear to create, potential conflicts of interest if we and our Former Parent pursue the same corporate opportunities or face decisions that could have different implications for our Former Parent and us.

Table of Contents

- We may have received better terms from unaffiliated third parties than the terms we will receive in our agreements with our Former Parent.

The agreements we entered into with our Former Parent in connection with the Separation, including the separation and distribution agreement, transition services agreement, tax matters agreement and employee matters agreement, were prepared in the context of our separation from our Former Parent while we were still a wholly owned subsidiary of our Former Parent. Accordingly, during the period in which the terms of those agreements were prepared, we did not have an independent Board of Directors or a management team that was independent of our Former Parent. As a result, the terms of those agreements may not reflect terms that would have resulted from arm's-length negotiations between unaffiliated third parties. Arm's-length negotiations between our Former Parent and an unaffiliated third party in another form of transaction, such as a buyer in a sale of a business transaction, may have resulted in more favorable terms to the unaffiliated third party.

- We incurred new indebtedness in connection with the Separation, and the degree to which we are leveraged may have a material adverse effect on our business, financial condition or results of operations and cash flows.

We have historically relied upon our Former Parent for working capital requirements and other cash requirements, including in connection with our previous acquisitions. As a result of the Separation, we are no longer able to rely on the earnings, assets or cash flow of our Former Parent and our Former Parent will not provide funds to finance our working capital or other cash requirements. Accordingly, we are responsible for servicing our own debt, and obtaining and maintaining sufficient working capital and other funds to satisfy our cash requirements. On January 27, 2014, we entered into a $200 million five-year senior secured revolving credit facility, as well as a $300 million five-year senior secured term loan facility. In connection with the Separation, we incurred borrowings of $400 million under the facilities and distributed $400 million of the proceeds of such indebtedness to our Former Parent. After the Separation, our access to and cost of debt financing may be different from the historical access to and cost of debt financing under our Former Parent. Differences in access to and cost of debt financing may result in differences in the interest rate charged to us on financings, as well as the amounts of indebtedness, types of financing structures and debt markets that may be available to us.

Our ability to make payments on and to refinance our indebtedness, including the debt incurred in connection with the Separation, as well as any future debt that we may incur, will depend on our ability to generate cash in the future from operations, financings or asset sales and the tax consequences of our repatriation of overseas cash. Our ability to generate cash is subject to general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control. If we are not able to repay or refinance our debt as it becomes due, we may be forced to sell assets or take other disadvantageous actions, including (i) reducing financing in the future for working capital, capital expenditures and general corporate purposes or (ii) dedicating an unsustainable level of our cash flow from operations to the payment of principal and interest on our indebtedness. In addition, our ability to withstand competitive pressures and to react to changes in our industry could be impaired. The lenders who hold such debt could also potentially accelerate amounts due, which could potentially trigger a default or acceleration of any of our other debt.

In addition, we may increase our debt or raise additional capital, subject to restrictions in our debt agreements. If our cash flow from operations is less than we anticipate, or if our cash requirements are more than we expect, we may require more financing. However, debt or equity financing may not be available to us on terms acceptable to us, if at all. If we incur additional debt or raise equity through the issuance of preferred stock, the terms of the debt or preferred stock issued may give the holders rights, preferences and privileges senior to those of holders of Knowles' common stock, particularly in the event of liquidation. The terms of the debt may also impose additional and more stringent restrictions on our operations than it currently has. If we raise funds through the issuance of additional equity, your percentage ownership in Knowles would be diluted. If we are unable to raise additional capital when needed, it could affect our financial condition, which could negatively affect your investment in Knowles. Also, regardless of the terms of our debt or equity financing, the amount of our stock that we can issue may be limited because the issuance of our stock may cause the distribution to be a taxable event for our Former Parent under Section 355(e) of the Code, and under the tax matters agreement, we could be required to indemnify our Former Parent for the resulting tax. See the section entitled “Risk Factors—Risks Related to Our Recent Separation—We may not be able to engage in certain corporate transactions as a result of the Separation.”

Table of Contents

Risks Related to Knowles' Common Stock

• Our stock price may fluctuate significantly.

The market price of Knowles' common stock may fluctuate significantly due to a number of factors, some of which may be beyond our control, including:

- Our business profile and market capitalization may not fit the investment objectives of our Former Parent's shareholders, causing a shift in our investor base, and Knowles' common stock may not be included in some indices in which our Former Parent's common stock is included, causing certain holders to sell their shares;
- our quarterly or annual earnings, or those of other companies in our industry;
- the failure of securities analysts to cover Knowles' common stock;
- actual or anticipated fluctuations in our operating results;
- changes in earnings estimates by securities analysts or our ability to meet those estimates or our earnings guidance;
- the operating and stock price performance of other comparable companies;
- overall market fluctuations and domestic and worldwide economic conditions; and
- other factors described in these "Risk Factors" and elsewhere in this Form 10-K.

Stock markets in general have experienced volatility that has often been unrelated to the operating performance of a particular company. These broad market fluctuations may adversely affect the trading price of Knowles' common stock.

In addition, investors may have difficulty accurately valuing Knowles' common stock. Investors often value companies based on the stock prices and results of operations of other comparable companies. Currently, no public communication technologies company exists in the United States that is directly comparable to our size, scale and product offerings. As such, investors may find it difficult to accurately value Knowles' common stock, which may cause the trading price of Knowles' common stock to be below its true value.

• We cannot guarantee the timing, amount or payment of dividends on our common stock.

The timing, declaration, amount and payment of future dividends to our shareholders will fall within the discretion of our Board of Directors. The Board of Directors' decisions regarding the payment of dividends will depend on many factors, such as our financial condition, earnings, capital requirements, debt service obligations, industry practice, legal requirements, regulatory constraints, and other factors that the Board of Directors deems relevant. Our ability to pay dividends will depend on our ongoing ability to generate cash from operations and access to the capital markets. We cannot guarantee that we will pay a dividend in the future or continue to pay any dividend if we commence paying dividends.

Table of Contents

- Certain provisions in our amended and restated certificate of incorporation and amended and restated by-laws, and of Delaware law, may prevent or delay an acquisition of the Company, which could decrease the trading price of our common stock.

Our amended and restated certificate of incorporation and amended and restated by-laws contain, and Delaware law contains, provisions that are intended to deter coercive takeover practices and inadequate takeover bids by making such practices or bids unacceptably expensive to the bidder and to encourage prospective acquirers to negotiate with our Board of Directors rather than to attempt a hostile takeover. These provisions include, among others:

o the inability of our shareholders to call a special meeting or act by written consent;

o rules regarding how shareholders may present proposals or nominate directors for election at shareholder meetings;

o the right of our Board of Directors to issue preferred stock without shareholder approval;

o the division of our Board of Directors into three approximately equal classes of directors, with each class serving a staggered three-year term;

o a provision that shareholders may only remove directors for cause;

o the ability of our directors, without a shareholder vote, to fill vacancies on our Board of Directors (including those resulting from an enlargement of the Board of Directors); and

o the requirement that shareholders holding at least 80% of our voting stock are required to amend certain provisions in our amended and restated certificate of incorporation and our amended and restated by-laws.

In addition, we are subject to Section 203 of the DGCL. Section 203 provides that, subject to limited exceptions, persons that (without prior board approval) acquire, or are affiliated with a person that acquires, more than 15 percent of the outstanding voting stock of a Delaware corporation shall not engage in any business combination with that corporation, including by merger, consolidation or acquisitions of additional shares, for a three-year period following the date on which that person or its affiliate becomes the holder of more than 15 percent of the corporation’s outstanding voting stock.

We believe these provisions protect our shareholders from coercive or otherwise unfair takeover tactics by requiring potential acquirers to negotiate with our Board of Directors and by providing our Board of Directors with more time to assess any acquisition proposal. These provisions are not intended to make us immune from takeovers. However, these provisions will apply even if the offer may be considered beneficial by some shareholders and could delay or prevent an acquisition that our Board of Directors determines is not in the best interests of the Company and our shareholders. These provisions may also prevent or discourage attempts to remove and replace incumbent directors.

In addition, an acquisition or further issuance of our stock could trigger the application of Section 355(e) of the Code. Under the tax matters agreement, we would be required to indemnify our Former Parent for the tax imposed under Section 355(e) of the Code resulting from an acquisition or issuance of our stock, even if we did not participate in or otherwise facilitate the acquisition, and this indemnity obligation might discourage, delay or prevent a change of control that you may consider favorable.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

Table of Contents

## ITEM 2. PROPERTIES

Our corporate headquarters is located in Itasca, Illinois. We maintain technical customer support offices and operating facilities in North America, Europe and Asia.

The number, type, location and size of the properties used by our continuing operations as of December 31, 2013 are shown in the following charts:

| | |
|---|---|
| Number and nature of facilities: | |
| Manufacturing | 18 |
| Warehouse | 5 |
| Sales / Service | 13 |
| | |
| Square footage (in 000s): | |
| Owned | 817 |
| Leased [1] | 1,053 |
| | |
| Locations: | |
| Asia | 10 |
| North America | 8 |
| Europe | 7 |

[1] Expiration dates on leased facilities range from 1 to 15 years.

We believe that our owned and leased facilities are well-maintained and suitable for our operations.

## ITEM 3. LEGAL PROCEEDINGS

We are involved in various lawsuits, claims and investigations arising in the normal course of our business, including those related to intellectual property which may be owned by us or others. We own many patents which cover our products, technology and manufacturing processes. Some of these patents have been and, we expect, will continue to be challenged by others. In appropriate cases, we have taken and will take steps to protect and defend our patents and other intellectual property, including through the use of legal proceedings in various jurisdictions around the world. Such steps may result in retaliatory litigation, the costs of which may be material. Based on the strength of our intellectual property and our prior experience enforcing it, our current assessment is that the ultimate disposition of these matters is not expected to have a material adverse effect on our operating results or financial condition. We will periodically review the probable outcome of such proceedings, their impact on our operations, the associated costs and expenses incurred and reasonably expected to be incurred, and the amounts accrued.

In addition, we may, on a limited, customer specific basis, provide contractual indemnities for certain losses that arise out of claims that our products infringe the intellectual property of others. Historically, we have not made significant payments under such indemnity arrangements. At December 31, 2013, our legal reserves were not significant.

## ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

Table of Contents

EXECUTIVE OFFICERS OF THE REGISTRANT

The following table sets forth information regarding our executive officers, including their positions with the Company, and is followed by the biography of each such executive officer.

| Name | Age | Position |
|---|---|---|
| Jeffrey S. Niew | 47 | President & Chief Executive Officer |
| John S. Anderson | 51 | Senior Vice President & Chief Financial Officer |
| Michael A. Adell | 43 | Co-President, Mobile Consumer Electronics-Microphones |
| Christian U. Scherp | 48 | Co-President, Mobile Consumer Electronics-Speakers and Receivers |
| Gordon A. Walker | 38 | Co-President, Specialty Components-Acoustics & Hearing Health |
| David W. Wightman | 59 | Co-President, Specialty Components-Precision Devices |
| Raymond D. Cabrera | 47 | Senior Vice President, Human Resources & Chief Administrative Officer |
| Paul M. Dickinson | 43 | Senior Vice President, Corporate Development & Treasurer |
| Daniel J. Giesecke | 46 | Senior Vice President & Chief Operating Officer |
| Joseph W. Schmidt (1) | 67 | Senior Vice President, General Counsel |
| Thomas G. Jackson (1) | 48 | Senior Vice President, Corporate Secretary |
| James F. Wynn | 53 | Senior Vice President, Global Supply Chain |
| Bryan E. Mittelman | 43 | Vice President, Controller |

(1) As previously disclosed, Mr. Schmidt is expected to continue to serve as Senior Vice President and General Counsel until March 31, 2014. Effective April 1, 2014, Mr. Jackson will assume the title of Senior Vice President, General Counsel and Secretary.

Jeffrey S. Niew has served as President & Chief Executive Officer since September 2013 and as a member of our Board of Directors since February 2014. From November 2011 until the Separation in February 2014, Mr. Niew served as a Vice President of Dover Corporation and as President and Chief Executive Officer of Dover Communication Technologies. Mr. Niew joined Knowles Electronics LLC (“Knowles Electronics”) in May 2000, and became Chief Operating Officer in January 2007, President in January 2008 and President and Chief Executive Officer in February 2010. Prior to joining Knowles Electronics, Mr. Niew was employed by Littelfuse, Inc., from 1995 to 2000, where he held various positions in product management, sales and engineering in the Electronic Products group, and by Hewlett-Packard Company, from 1988 to 1994, where he served in various engineering and product management roles in the Optoelectronics Group in California.

John S. Anderson has served as Senior Vice President & Chief Financial Officer since December 2013. From January 2013 until the Separation in February 2014, Mr. Anderson served as Vice President and Chief Financial Officer of Dover Communication Technologies. Previously, Mr. Anderson served as Vice President and Chief Financial Officer of Dover Energy (from August 2010 to January 2013), and Vice President and Chief Financial Officer of Dover Fluid Management (from October 2009 to August 2010). Previous experience includes the roles of Corporate Controller and Director Financial Planning & Analysis for Sauer-Danfoss Inc. (from October 2004 to October 2009) and Director of Finance and Controller for Borg Warner Turbo Systems GmbH (from August 2002 to October 2004).

Michael A. Adell has served as Co-President, Mobile Consumer Electronics - Microphones since July 2011. Previously, Mr. Adell served as Vice President and General Manager in the Knowles Acoustics division of Knowles Electronics (“Knowles Acoustics”) (from January 2009 to July 2011), General Manager, Knowles Acoustics (from December 2006 to January 2009), Director, Product Management, Knowles Acoustics (from July 2004 to November 2006) and Product Manager for silicon microphone products, Knowles Acoustics (from November 2002 to July 2004).

Christian U. Scherp has served as Co-President, Mobile Consumer Electronics - Speakers and Receivers since September 2012. Prior to joining Knowles Electronics, Mr. Scherp served as the Global Head of Sales for the Consumer Devices business of TE Connectivity (from November 2011 to August 2012). Additional previous experience includes the following roles at Conexant Systems: Executive Vice President of Sales (from January 2011 to June 2011), Co-President, WW Sales, Marketing, Program Management (from July 2009 to December 2010) and President (from 2008 to 2009).

Gordon A. Walker has served as Co-President, Specialty Components - Acoustics & Hearing Health since July 2011. Previously, Mr. Walker served in the following roles in the Knowles Electronics division of Knowles Electronics: Vice President and General Manager (from December 2007 to July 2011), General Manager (from January 2006 to December 2007), and Director, Product Management (from September 2004 to December 2005). Prior to such positions, he held marketing, finance and operations roles after he joined Knowles Electronics in 1997.

David W. Wightman has served as Co-President, Specialty Components - Precision Devices since April 2013. Previously, Mr. Wightman held the position of President of Ceramic & Microwave Products (from August 2004 to April 2013) and President (from February 2000 to August 2004) of Dow-Key Microwave Corporation. Mr. Wightman’s experience also includes leadership roles at Danaher from February 1995 to February 2000.

Raymond D. Cabrera has served as Senior Vice President, Human Resources & Chief Administrative Officer since February 2014. From November 2011 until the Separation in February 2014, Mr. Cabrera served as Vice President, Human Resources of Dover Communication Technologies. Previously, Mr. Cabrera served as Vice President, Human Resources and Chief Administrative Officer (from January 2004 to November 2011), Vice President, Human Resources (from March 2000 to January 2004) and Director, Human Resources (from June 1997 to March 2000) of Knowles Electronics.

Paul M. Dickinson has served as Senior Vice President, Corporate Development & Treasurer since February 2014. Mr. Dickinson started his career with Knowles in October 2013. Previously, Mr. Dickinson was the Chief Financial Officer for EPAY Systems, Inc., from 2012 until moving to Knowles. Additional previous experience includes the following roles at Littelfuse, Inc.: Vice President and General Manager, Semiconductor Business (from 2008 to 2012), Vice President, Corporate Development & Treasurer (from 2005 to 2008), Treasurer (from 2003 to 2005), Director of Accounting and International Finance (from 2000 to 2003) and other finance leadership roles since he joined Littelfuse in 1993.

Daniel J. Giesecke has served as Senior Vice President & Chief Operating Officer since February 2014. From January 2012 until the Separation in February 2014, Mr. Giesecke served as Vice President, Global Operations of Dover Communication Technologies. Previously, Mr. Giesecke served as Vice President, Advanced Manufacturing Engineering, Knowles Electronics (from February 2009 to January 2012), Senior Director, Advanced Manufacturing Engineering, Knowles Electronics (from January 2008 to February 2009), Director of Engineering Operations, Knowles Electronics (from November 2003 to January 2008) and various operations, supply chain, and engineering positions since he joined Knowles Electronics in 1995.

Joseph W. Schmidt is our Senior Vice President, General Counsel. Mr. Schmidt became our Senior Vice President, General Counsel & Secretary on December 1, 2013 pursuant to a short-term independent contractor arrangement. Pursuant to the terms of this arrangement, Mr. Schmidt served in such capacity until February 28, 2014 and will continue as Senior Vice President, General Counsel until March 31, 2014. Knowles has extended the term of Mr. Schmidt's service as a consultant until May 31, 2014. Mr. Schmidt served as Dover’s Senior Vice President, General Counsel and Secretary from May 2011 until his retirement on December 31, 2012; prior thereto Mr. Schmidt served as Vice President, General Counsel and Secretary of Dover from January 2003 to May 2011. Mr. Schmidt has served as a valuable resource to Knowles in connection with the Separation given his 10 years of experience as General Counsel of Dover and his knowledge of Knowles' business and is helping the management team and the Board transition to a new General Counsel.

Thomas G. Jackson has served as Senior Vice President, Corporate Secretary since February 2014 and, effective April 1, 2014, Mr. Jackson will assume the title of Senior Vice President, General Counsel and Secretary. Prior to joining Knowles, Mr. Jackson served as Vice President and Assistant General Counsel at Jabil Circuit, Inc., a provider of electronic manufacturing services (from March 2012 to December 2013). In addition, he served as Vice President, General Counsel and Secretary at P.H. Glatfelter Company, a manufacturer of specialty papers and fiber-based engineered materials (from June 2008 to November 2011), and as its Assistant General Counsel, Assistant Secretary and Director of Compliance (from September 2006 to June 2008).

Table of Contents

James F. Wynn has served as Senior Vice President Global Supply Chain since February 2014. From January 2013 until the Separation in February 2014, Mr. Wynn served as Vice President, Global Supply Chain of Dover Communication Technologies. Previously, Mr. Wynn served as Vice President, Global Supply Chain (from February 2009 to January 2013), Senior Director, Global Supply Chain (from March 2004 to February 2009) and Director, Global Supply Chain (from March 2002 to March 2004) of Knowles Electronics.

Bryan E. Mittelman has served as Vice President, Controller since February 2014. Mr. Mittelman started his career at Knowles in September 2013. Previously, Mr. Mittelman served as the Controller for Morningstar, Inc. from December 2011 to September 2013. Additional prior experience includes operating his consulting business from June 2010 to December 2011 and the following roles at Siemens Healthcare Diagnostics and Dade Behring (which was acquired by Siemens in 2007): Vice President, Finance, North America (from January 2008 to May 2010), Vice President, Finance, Americas (from January 2007 to December 2007), Vice President, Corporate Audit and Advisory Services (from March 2006 to December 2006), Assistant Corporate Controller (from April 2005 to February 2006) and Director of Financial Reporting (from July 2002 to April 2005).

Table of Contents

PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

### Market Information

Our common stock is listed on the New York Stock Exchange (the “NYSE”) under the ticker symbol “KN.” A "when issued" trading market for our common stock began on the NYSE on February 14, 2014, and "regular way" trading of our common stock began on March 3, 2014. Prior to February 14, 2014, there was no public market for Knowles' common stock. The following table presents the high and low prices for common stock as reported on the NYSE since February 14, 2014.

| | 2014 Market Prices | |
|---|---|---|
| | High | Low |
| First Quarter (February 14, 2014 through March 21, 2014) | $33.66 | $27.58 |

### Dividends

Since the spin-off of Knowles Corporation from Dover Corporation, we have not paid cash dividends, and we do not anticipate paying a cash dividend on our common stock in the immediate future. Any determination to pay dividends in the future will be at the discretion of our Board of Directors and will depend on many factors, such as our financial condition, earnings, capital requirements, debt service obligations, industry practice, legal requirements, regulatory constraints, and other factors that the Board of Directors deems relevant. Our ability to pay dividends will depend on our ongoing ability to generate cash from operations and access to the capital markets.

### Holders

The number of holders of record of our common stock as of March 21, 2014 was approximately 1,587.

### Securities Authorized for Issuance Under Equity Compensation Plans

For information regarding securities authorized for issuance under our equity compensation plans, see Part III, Item 12 of this Form 10-K.

### Recent Sales of Unregistered Securities

On June 26, 2013, in connection with our formation, we issued 100 shares of common stock, par value $0.01 per share, to Dover Corporation for total consideration of $100 in cash. On February 28, 2014, we issued 85,019,059 shares of common stock, par value $0.01 per share, to Dover Corporation as a dividend to our sole shareholder. We did not register the issuance of these shares under the Securities Act of 1933, as amended (the “Securities Act”), because such issuance did not constitute a public offering and therefore was exempt from registration pursuant to Section 4(a)(2) of the Securities Act. All of these 85,019,159 shares were subsequently distributed on a pro rata basis to Dover’s shareholders in connection with the Separation.

### Issuer Purchases of Equity Securities

None.

Table of Contents

ITEM 6. SELECTED FINANCIAL DATA

The following table presents selected combined financial data. We derived the selected combined financial data as of December 31, 2013 and 2012 and for the years ended December 31, 2013, 2012 and 2011 from the audited Combined Financial Statements and accompanying notes that are under Item 8, "Financial Statements and Supplementary Data." We derived the selected combined financial data as of December 31, 2011 and for the year ended December 31, 2010 from our audited Combined Financial Statements and accompanying notes that are not included in this report. We derived the data as of December 31, 2010 and 2009 and for the year ended December 31, 2009 from our unaudited Combined Financial Statements that are not included in this report. In management's opinion, our unaudited Combined Financial Statements for these periods and as of these dates have been prepared on the same basis as our audited Combined Financial Statements and include all adjustments, consisting only of normal recurring adjustments and allocations, necessary for a fair statement of the information for the periods presented.

The selected financial data includes costs of Knowles' businesses, which include the allocation of certain corporate expenses from Dover. We believe that these allocations were made on a reasonable basis. The selected historical financial data may not be indicative of our future performance as an independent publicly-traded company. The selected financial data should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Combined Financial Statements and accompanying notes included under Item 8, "Financial Statements and Supplementary Data."

| | Years Ended December 31, | | | | |
|---|---|---|---|---|---|
| Statement of Earnings data (in thousands, except for share and per share amounts): | 2013 | 2012 | 2011 (1) | 2010 | 2009 (Unaudited) |
| Revenue | $1,214,803 | $1,117,992 | $983,318 | $730,444 | $ 587,006 |
| Operating earnings | 143,828 | 136,064 | 146,404 | 141,527 | 78,571 |
| Operating margin | 11.8 % | 12.2 % | 14.9 % | 19.4 % | 13.4 % |
| Net earnings | $105,814 | $79,097 | $98,457 | $109,272 | $ 37,295 |
| Adjusted for: | | | | | |
| Depreciation and amortization | $130,912 | $114,878 | $84,773 | $54,385 | $ 50,678 |
| Interest expense, net (2) | 42,024 | 56,470 | 39,892 | 20,253 | 21,154 |
| (Benefit from) provision for income taxes | (4,304 ) | (181 ) | 7,099 | 7,535 | 18,478 |
| EBITDA (3) | $274,446 | $250,264 | $230,221 | $191,445 | $ 127,605 |
| EBITDA margin (3) | 22.6 % | 22.4 % | 23.4 % | 26.2 % | 21.7 % |
| Basic and diluted earnings per share | $1.24 | $0.93 | $1.16 | $1.29 | $ 0.44 |
| Basic and diluted shares outstanding (4) | 85,019,159 | 85,019,159 | 85,019,159 | 85,019,159 | 85,019,159 |

| | As of December 31, | | | | |
|---|---|---|---|---|---|
| Balance Sheet Data (in thousands): | 2013 | 2012 | 2011 (1) | 2010 (Unaudited) | 2009 (Unaudited) |
| Total assets | $2,170,116 | $2,051,092 | $2,000,713 | $1,034,257 | $ 1,051,138 |
| Notes payable to Parent, net | — | 528,812 | 1,419,422 | 440,486 | 573,308 |
| Total Parent Company equity | 1,887,127 | 1,188,107 | 286,650 | 443,860 | 330,710 |

| | Years Ended December 31, | | | | |
|---|---|---|---|---|---|
| Other Data (in thousands): | 2013 | 2012 | 2011 (1) | 2010 | 2009(Unaudited) |
| Research and development | $82,568 | $77,321 | $65,895 | $49,286 | $ 45,014 |

| | | | | | |
|---|---|---|---|---|---|
| Capital expenditures | 91,267 | 145,647 | 96,314 | 32,920 | 19,323 |

Table of Contents

(1) On July 4, 2011, the Company completed the stock acquisition of the Sound Solutions business line from NXP Semiconductors N.V. ("NXP"). The combined statements of earnings and combined balance sheets include the results of operations, net assets acquired and depreciation and amortization expense related to Sound Solutions since the date of acquisition. See Note 3. Acquisition of Sound Solutions of the notes to the Combined Financial Statements for additional information related to this acquisition.

(2) The interest expense related to our net notes payable to our former parent that were settled in connection with the Separation is not necessarily representative of our post-Separation debt-related interest. See Revolving Credit Facility section of Liquidity and Capital Resources under "Management's Discussion and Analysis of Financial Condition and Results of Operations" for additional information related to our post-Separation debt.

(3) We use the term "EBITDA" throughout this Form 10-K, defined as net earnings plus (i) depreciation and amortization expense, (ii) interest expense and (iii) income taxes. EBITDA and EBITDA margin (defined as EBITDA as a percentage of revenue) are not presented in accordance with accounting principles generally accepted in the United States of America ("GAAP" or "U.S. GAAP") and may not be comparable to similarly titled measures used by other companies. We use EBITDA and EBITDA margin as supplements to our GAAP results of operations in evaluating certain aspects of our business, and our Board of Directors and executive management team focus on EBITDA and EBITDA margin as key measures of our performance for business planning purposes. These measures assist us in comparing its performance between various reporting periods on a consistent basis, as these measures remove from operating results the impact of items that, in our opinion, do not reflect our core operating performance. We believe that our presentation of EBITDA and EBITDA margin is useful because it provides investors and securities analysts with the same information that we use internally for purposes of assessing our core operating performance. For a reconciliation of EBITDA to net earnings, the most directly related GAAP measure, please see the table above.

(4) On February 28, 2014, the distribution date, Dover shareholders of record as of the close of business on February 19, 2014 received one share of Knowles common stock for every two shares of Dover's common stock held as of the record date. Basic and diluted earnings per common share and the average number of common shares outstanding were calculated using the number of Knowles common shares outstanding immediately following the distribution. See Note 16. Earnings per Share of the notes to the Combined Financial Statements for information regarding earnings per common share.

Table of Contents

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The discussion and analysis presented below refer to and should be read in conjunction with the audited Combined Financial Statements and related notes under Item 8, "Financial Statements and Supplementary Data." The following discussion contains forward-looking statements. The matters discussed in these forward-looking statements are subject to risks, uncertainties, and other factors that could cause actual results to differ materially from those made, projected or implied in the forward-looking statements. Factors that could cause or contribute to these differences include those discussed below and elsewhere in this Form 10-K, particularly in “Risk Factors” and “Cautionary Statement Concerning Forward-Looking Statements.” We believe the assumptions underlying the Combined Financial Statements are reasonable. However, the Combined Financial Statements included herein may not necessarily reflect our results of operations, financial position and cash flows in the future or what they would have been had we been an independent publicly-traded company during the periods presented.

Management’s discussion and analysis, which we refer to as “MD&A,” of our results of operations, financial condition and cash flows is provided as a supplement to the audited Combined Financial Statements and footnotes included under Item 8, "Financial Statements and Supplementary Data," to help provide an understanding of our financial condition, changes in financial condition and results of our operations.

Overview and Outlook

Background

On February 28, 2014, our former parent company, Dover Corporation, completed the spin-off of Knowles into an independent, publicly-traded company. We have a leading position in MicroElectroMechanical Systems (“MEMs”) microphones, speakers and receivers which are used in mobile handsets, smartphones and tablets within the consumer electronics market. We are also a leading manufacturer of transducers used in the hearing health segment of the medical technology market and have a strong position in oscillators (timing devices) and capacitors which serve the telecommunication infrastructure, military/space and other industrial markets.

Business Segments

We are organized into two reportable segments based on how management analyzes performance, allocates capital and makes strategic and operational decisions. These segments were determined in accordance with FASB ASC Topic 280-Segment Reporting and are comprised of (i) Mobile Consumer Electronics (“MCE”) and (ii) Specialty Components (“SC”). The segments are aligned around similar product applications serving our key end markets, to enhance focus on end market growth strategies.

- MCE designs and manufactures innovative acoustic products, including microphones, speakers and receivers, used in several applications that serve the handset, tablet and other consumer electronic markets. Locations include the corporate office in Itasca, Illinois; sales, support and engineering facilities in North America, Europe and Asia; and manufacturing facilities in Europe and Asia.
- SC specializes in the design and manufacture of specialized electronic components used in medical and life science applications, as well as high-performance solutions and components used in communications infrastructure and a wide variety of other markets. SC’s transducer products are used principally in hearing aid applications within the commercial audiology markets, while its oscillator products predominantly serve the telecom infrastructure market and its capacitor products are used in applications including radio, radar, satellite, power supplies, transceivers and medical implants serving the defense, aerospace, telecommunication and life sciences markets. Operating facilities

and sales, support and engineering facilities are located in North America, Europe and Asia.

We sell our products directly to original equipment manufacturers (“OEMs”) and to their contract manufacturers and suppliers, and to a lesser extent through distributors worldwide.

Table of Contents

Our Markets and Market Trends

Our products serve a variety of end markets, notably, consumer mobile devices, medical technology, aerospace and defense and telecom, and can generally be divided into two categories: Acoustic Components and Specialty Components, as described below.

- Acoustic Components. Includes analog and digital microphones, MEMs microphones, surface mounted device microphones, receivers, speakers, speaker modules, multi-functional devices, ultrasonic sensors and integrated audio sub-systems.
- Specialty Components. Includes transducers, oscillators, capacitors and filters.

The markets served by Acoustic Components continue to be driven by trends in smartphone and tablet innovation and demand. Today, mobile device OEMs are facing ever-rising challenges to differentiate their products in the global marketplace while managing growing cost pressures and time-to-market expectations. However, mobile consumers and mobile carriers alike are expecting better quality voice calls, audio and video conferencing, capturing and playback, media content consumption and gaming, as well as extended battery life. To enable smart mobile devices to handle ever more demanding audio use cases, OEMs are increasingly adopting more intelligent active audio components (audio chipset) and higher performance passive acoustic components. Trends impacting the smartphone market today include:

- Smartphone growth from feature phone substitution. The smartphones segment within the handset device market has exhibited consistently strong unit growth over the past five years (>40% unit volume compound annual growth rate). There continues to be a positive mix shift from the proliferation of lower-end smartphone devices and the further cannibalization of feature phones (i.e., non-smartphones). The average smartphone continues to drive higher audio content including more microphones and higher value speakers than its feature phone counterpart, compounding the growth of acoustic content as mobile phone sales rise.
- Smartphone OEM market share shifts are likely to remain volatile for some time. Recently, Nokia and Blackberry have lost significant market share to other U.S. and Asian-based OEMs who have released smartphones that have been more readily accepted due to, among other factors, perceived feature sets and price points. We expect the OEM market to continue to be dynamic over time, characterized by rapid market share shifts driven by new product introductions, price points and feature sets.
- New OEM product line rollouts. Smartphones continue to shift to Long Term Evolution (“LTE”), a standard for 4G wireless technology, and the shift is expected to buoy unit growth in developed markets and drive the competitive landscape in high-end chipsets through 2014. Aggressive LTE deployments are expected in China, in addition to a build-out of deeper coverage profiles in the U.S., Japan, Korea and Northern Europe. This will drive an increase in LTE smartphone units over the next five years, which should help maintain some level of high-end smartphone volume growth despite high market penetration.
- Shortened smartphone upgrade plans at U.S. carriers. Several U.S. carriers have recently introduced new smartphone plans which offer consumers the option of paying for their phone in monthly installments with no upfront lump sum payment, and the ability to upgrade again in 12 months. Plans such as these could drive greater-than-expected unit growth (turnover) at the high end, as they are most likely to appeal to high-income consumers seeking to upgrade their phone more frequently.
- High-end consumer elasticity. Consumers are reluctant to downgrade from a high-end smartphone to a low-end smartphone in most circumstances. This is especially true as high-end smartphones will likely continue to offer significant performance advantages and new functionality compared to low-end smartphones.
- Proliferation of premium acoustics. Consumers are seeking improved acoustics solutions, regardless of the country they live in or the type of device they are using. As a result, acoustic dollar content is generally expanding per device for two primary reasons. First, many of the solutions we are introducing are higher performance and command higher value. Secondly, OEMs are increasing the number of acoustic components per device. Over the past several years, we

have seen an increase in the number of microphones used in high end smartphones. The benefits to the user are substantial, including reduced background noise, improved voice recognition, better hands-free communication and enhanced audio recording and playback capabilities. OEMs and their customers recognize the importance of these features in their next-generation products. We believe an additional opportunity exists for these trends to proliferate to mid-range phones and tablets, as well as emerging wearable devices. Knowles can

Table of Contents

capitalize on these market demands by leveraging our acoustics expertise and proprietary process technologies to deliver solutions that improve the performance of our OEM customers' devices.

Specialty Components products are sold across diverse end markets, and relative to the Acoustic Components end markets, portions of this business face much greater exposure to capital investment cycles and government spending, both direct and indirect, as some of these end markets are largely dependent on project upgrades and expansion, and government contracts. These products can be divided into the following categories:

- Medical and life sciences products (i.e., transducers, hearing aids, capacitors). Product sales are largely driven by aging demographics, healthcare spending, the rise of a middle class in emerging markets and government subsidies.
- Aerospace and defense communications (i.e., capacitors, filters, oscillators). Aerospace and defense spending and automation (largest end market), telecom regional coverage and bandwidth expansion, and growing industrial power supply requirements are a few of the end-market trends driving the product sales in this sector.
- Telecom infrastructure (i.e., capacitors, filters, oscillators). Sales are typically levered to the expansion of large telecom companies, looking to increase wireless signal in new or existing territories, although these products are also sold to aerospace and defense companies (i.e., airplane radio frequencies).

Geographic Trends

We strive to maintain our manufacturing facilities in close proximity to our direct customers. In the case of MCE, we operate four facilities in Asia to serve the contract manufacturers who build OEM equipment on behalf of our end-customers. These contract manufacturers are largely based in China, Taiwan and India. Although end-user demand for consumer electronics is global, and marketing activities occur globally, critical mass for manufacturing is located in Asia, and as a result, a large majority of MCE's manufacturing capacity is based in Asia, primarily China, Malaysia and the Philippines.

In the case of SC, we operate three facilities in Asia to serve the manufacturing sites of both hearing aid OEMs and the contract manufacturers who build OEM headsets on behalf of earphone makers. These OEM manufacturing sites are largely based in China, Singapore, Indonesia and Vietnam. Although marketing activities and end-user demand for hearing aid and specialty consumer components is global, critical mass for manufacturing is located in Asia for the purposes of being close to the point of assembly. We also operate three facilities in the United States, one in Mexico and three in Europe for the manufacturing of capacitors and oscillators that support our global telecom and military customers, as well as their suppliers and contract manufacturers.

While no significant statutory limitation exists, a repatriation of profits from foreign markets to the United States is inherently inefficient, as business expansion opportunities and capital expenditure requirements are expected to be consistent with the needs of our direct customer and manufacturing locations.

Competitive Landscape

Success in the electronic components industry is primarily driven by innovation and flexibility as customers compete to gain a share of the fast growing handset market. Capturing growth opportunities usually results from competition across both platform and component designs, which supports position, pricing and margins.

Continuous research and development investment allows for the capture of all emerging new brands with early mover advantage. Flexibility in balancing full and semi-automation is a key to achieving a superior cost structure. Additionally, it is important for component vendors to have flexibility and quick time-to-market to meet clients' needs. Notably, according to industry estimates, the product cycle for handsets has shortened to eight months from two years.

Key competitors include:

- MCE: AAC Technologies and Goertek
- SC: Sonion for hearing health and a highly fragmented set of competitors across capacitor and oscillator products for each end market

32

In the mobile consumer electronics segment, our investments in research and development enable us continually to introduce new products that are higher performance. Our customers are quickly adopting these higher value microphones, speakers and receivers in their new products as they improve the overall audio performance in the end application, which in turn improves the end user experience. With each successive generation, our new products generally have higher average selling prices than the products they are replacing. Once introduced, the pricing for these products follows a normal downward trend as typically seen in the consumer electronics market. To get additional performance gains, OEMs are moving to our even higher value integrated audio solutions with microphones and an antenna in a plastic module.

For products that were introduced more than 18 months ago, we have consistently offset projected price erosion through bill of material cost reductions, yield improvements, equipment efficiency and labor reductions.

In the specialty components segment, the end markets are more stable, and mix of products and customers are drivers of average selling prices and margin.

Research and Development

We spend approximately 7% of revenue on an annual basis on projects intended to preserve and extend our technological advantage. Recent research and development investments have been focused on providing better sound quality and increased integration of our audio components. Research and development expenses are classified within selling and administrative expense. We spent $82.6 million, $77.3 million and $65.9 million on research and development, or 6.8%, 6.9% and 6.7% as a percentage of revenue, for the years ended December 31, 2013, 2012 and 2011, respectively.

Results of Operations

Our Combined Financial Statements are derived from Dover's consolidated financial statements and accounting records. The Combined Financial Statements represent our financial position, results of operations and cash flows as our business was operated as part of Dover prior to the distribution, in conformity with U.S. generally accepted accounting principles.

Table of Contents

Combined Results of Operations

| (in thousands, except per share amounts) | Years Ended December 31, 2013 | 2012 | 2011 [1] | % Change 2013 vs. 2012 | 2012 vs. 2011 |
|---|---|---|---|---|---|
| Revenue | $1,214,803 | $1,117,992 | $983,318 | 8.7 % | 13.7 % |
| Cost of goods and services | 786,862 | 711,000 | 605,298 | 10.7 % | 17.5 % |
| Gross profit | 427,941 | 406,992 | 378,020 | 5.1 % | 7.7 % |
| Gross profit margin | 35.2 % | 36.4 % | 38.4 % | (1.2 ) | (2.0 ) |
| Selling and administrative expenses | 284,113 | 270,928 | 231,616 | 4.9 % | 17.0 % |
| Selling and administrative expenses as a percent of revenue | 23.4 % | 24.2 % | 23.6 % | (0.8 ) | 0.6 |
| Operating earnings | 143,828 | 136,064 | 146,404 | 5.7 % | (7.1 )% |
| Operating margin | 11.8 % | 12.2 % | 14.9 % | (0.4 ) | (2.7 ) |
| Restructuring charges | 16,291 | 5,864 | 1,761 | 177.8 % | 233.0 % |
| Research and development | 82,568 | 77,321 | 65,895 | 6.8 % | 17.3 % |
| Provision for income taxes | (4,304 ) | (181 ) | 7,099 | 2,277.9 % | (102.5 )% |
| Effective tax rate | (4.2 )% | (0.2 )% | 6.7 % | (4.0 ) | (6.9 ) |
| Net earnings | 105,814 | 79,097 | 98,457 | 33.8 % | (19.7 )% |
| Earnings per common share - basic & diluted [2] | $1.24 | $0.93 | $1.16 | 33.3 % | (19.8 )% |

[1] On July 4, 2011, the Company completed the stock acquisition of the Sound Solutions business line from NXP Semiconductors N.V. (“NXP”). The combined statements of earnings and combined balance sheets include the results of operations, net assets acquired and depreciation and amortization expense related to Sound Solutions since the date of acquisition. See Note 3. Acquisition of Sound Solutions of the notes to the Combined Financial Statements for additional information related to this acquisition.

[2] On February 28, 2014, the distribution date, Dover shareholders of record as of the close of business on February 19, 2014 received one share of Knowles common stock for every two shares of Dover's common stock held as of the record date. Basic and diluted earnings per common share and the average number of common shares outstanding were calculated using the number of Knowles common shares outstanding immediately following the distribution. See Note 16. Earnings per Share of the notes to the Combined Financial Statements for information regarding earnings per common share.

Revenue

2013 Versus 2012

Our 2013 revenue increased $96.8 million, or 8.7%, to $1.2 billion from $1.1 billion in 2012. The overall increase in revenue was primarily due to an increase in volume of $143.1 million, partially offset by a decrease of $49.4 million related to pricing concessions. The increase in volume was driven by $40.2 million in higher demand for components serving primarily the smartphone market, including an increase in multiple microphone applications, and $157.3 million related to new smartphone models introduced by major OEM customers as well as one OEM customer gaining share in the smartphone market. Additionally, 2013 benefited from higher demand from telecom customers serving the anticipated build out of wireless infrastructure in China. The volume increase was partially offset by a $49.0 million impact of market share losses by two other key smartphone OEM customers and $6.2 million as a result of reduced demand for acoustic components used in specialty headset applications. Foreign currency translation positively impacted revenue by a negligible amount.

Table of Contents

2012 Versus 2011

Our 2012 revenue increased $134.7 million, or 13.7%, to $1.1 billion from $983.3 million in 2011. The overall increase in revenue resulted primarily from increased MEMs microphone volumes, due to new product introductions and overall smartphone market growth which resulted in an increase in revenue of $89.6 million. In addition, Sound Solutions contributed an increase of $134.0 million in acquisition-related revenue in the first half of 2012 as compared to the first half of 2011. The increase in 2012 revenue was partially offset by $30.8 million as a result of OEM market share shifts for the speaker and receiver product lines, $26.4 million related to pricing concessions for components serving the mobile consumer electronics and medical technology markets corresponding to normal product life cycle maturities within these markets and $25.0 million due to reduced demand within the telecommunications infrastructure market.

Costs of Goods and Services

2013 Versus 2012

Costs of goods and services for the year ended December 31, 2013 increased $75.9 million as compared to 2012, or 10.7%, of which $79.9 million was driven by the higher sales volume, $8.2 million was due to higher production transfer costs related to migration of operations into existing Asian lower-cost manufacturing facilities, $7.5 million was due to higher restructuring costs, and $6.9 million was due to asset impairment and inventory charges related to more mature product lines. Partially offsetting this increase was a $44.4 million impact of productivity initiatives, primarily due to lower conversion costs within MCE.

2012 Versus 2011

Costs of goods and services for the year ended December 31, 2012 increased $105.7 million as compared to 2011, or 17.5%, primarily due to the integration of Sound Solutions, reflecting a $116.9 million increase, because 2012 included a full year of costs as compared to a half year in 2011. In addition, increases of $9.5 million and $9.3 million due to the increase in sales volume within MCE and an increase in labor costs resulting from labor inflation in China and Malaysia, respectively, were offset by a $31.6 million decrease as a result of strategic pricing initiatives and lower conversion costs within MCE.

Gross Profit

2013 Versus 2012

Gross profit in 2013 increased $20.9 million, or 5.1%, as compared to 2012, driven principally by the increase in MEMs sales volumes. Gross profit margin decreased 120 basis points from 36.4% in 2012 to 35.2% in 2013 as operating leverage from the higher MEMs volumes was more than offset by higher production transfer costs of $8.2 million, additional restructuring charges of $7.5 million, asset impairment and inventory charges related to more mature product lines totaling $6.9 million and new product ramp up inefficiencies.

2012 Versus 2011

Gross profit in 2012 increased $29.0 million, or 7.7%, as compared to 2011, reflecting the benefit of increased sales volume, while gross profit margin decreased 200 basis points from 38.4% in 2011 to 36.4% in 2012. The decline in gross profit margin was attributed to new product ramp up costs and the integration of Sound Solutions, which more than offset the operating leverage achieved by our other product lines.

Selling and Administrative Expenses

2013 Versus 2012

Selling and administrative expenses increased $13.2 million, or 4.9%, in 2013 from $270.9 million in 2012, due principally to higher labor costs of $5.0 million mainly due to inflation, higher restructuring charges of $2.9 million incurred in connection with various cost savings initiatives and an overall increase to support the higher sales volume. As a percentage of revenue, selling and administrative expenses decreased 80 basis points as compared to the prior year. Included in selling and administrative expenses were corporate allocations of $23.6 million and $26.1 million for the years ended December 31,

Table of Contents

2013 and 2012, respectively, which represents administration of treasury, employee compensation and benefits, public and investor relations, internal audit, corporate income tax, supply chain and legal services.

2012 Versus 2011

Selling and administrative expenses increased $39.3 million, or 17%, in 2012 from $231.6 million in 2011 in order to support higher sales volume. Year over year, selling and administrative expenses as a percentage of revenue increased 60 basis points, as we experienced higher acquisition-related amortization and restructuring charges in 2012 compared to 2011, partially offset by one-time transaction costs of approximately $13.0 million incurred in 2011, in connection with the Sound Solutions acquisition. Included in selling and administrative expenses were corporate allocations of $26.1 million and $21.8 million for the years ended December 31, 2012 and 2011, respectively.

Restructuring Charges

We undertake restructuring programs from time to time to better align our operations with current market conditions. Such activities include targeted facility consolidations, headcount reductions and other measures to further optimize operations. It is likely that we will have restructuring charges in the future as we execute on our strategy to consolidate our manufacturing footprint. Details regarding restructuring programs undertaken during the reporting period are as follows:

2013

In 2013, we incurred charges totaling $16.3 million, relating to programs to integrate activities within the consumer electronics business, to reduce headcount within our German and North American operations that serve the telecom infrastructure market in order to better align the business with current market dynamics and to continue the migration of our U.K.-based capacitor production into our existing lower-cost Asian manufacturing facilities.

2012

In 2012, we incurred charges totaling $5.9 million, relating to the integration of our dynamic speaker and receiver businesses, continuation of the consolidation of the oscillator facility, and the initiation of a new program to migrate our U.K.-based capacitor production to lower-cost existing facilities in Asia.

2011

In 2011, in response to the slow global economic environment and, in particular, the weakened telecommunications market, we incurred charges totaling $1.8 million in connection with two U.S. facility consolidations in the capacitor and oscillator business.

For further details on restructuring charges, including classification of the amounts as cost of goods and services and selling and administrative expenses, see Note 8. Restructuring Activities of the notes to the Combined Financial Statements.

Research and Development

Research and development costs are a component of selling and administrative expense. For the years ended December 31, 2013, 2012 and 2011, research and development costs, as a percentage of revenue, was 6.8%, 6.9% and 6.7%, respectively. Shorter product life cycles due to the technological nature of our business, as well as continued design efforts for new customers, drove continuous product innovation and improvement over these periods as evidenced by several new product introductions by our customers and the continued growth in the handset market, particularly in 2012.

Table of Contents

Operating Earnings

2013 Versus 2012

Operating earnings in 2013 increased $7.8 million, or 5.7%, when compared to 2012 as the increase in sales volume more than offset higher restructuring charges of $10.4 million, $7.3 million of higher production transfer costs related to migration of operations into existing Asian lower-cost manufacturing facilities, and $6.9 million of asset impairment and inventory charges related to more mature product lines. Operating margin decreased 40 basis points, as operating leverage from the higher MEMs volume was offset by these increased costs relating to restructuring, production transfers and asset impairment and inventory charges.

2012 Versus 2011

Operating earnings in 2012 decreased $10.3 million, or 7.1%, when compared to 2011, and operating margin declined 270 basis points to 12.2% in 2012 from 14.9% in 2011. Higher restructuring costs, the integration of Sound Solutions, including higher acquisition-related amortization expense, and new product ramp up costs drove the decline in operating results. These costs were partially offset by operating leverage of our other product lines, as well as the 2011 incurrence of one-time transaction costs of $13.0 million related to the Sound Solutions acquisition.

Income Taxes

We are subject to income taxes in the United States and numerous foreign jurisdictions. Significant judgment is required in determining the provision for income taxes and income tax assets and liabilities, including evaluating uncertainties in the application of accounting principles and complex tax laws.

In our Combined Financial Statements, income tax expense and deferred tax balances have been calculated on a stand-alone basis although our operations have historically been included in the tax returns filed by our Former Parent. In the future, as a stand-alone entity, we will file tax returns on our own behalf and our deferred taxes and effective tax rate may differ from those in historical periods.

The effective tax rates for the years ended December 31, 2013, 2012 and 2011 were (4.2)%, (0.2)% and 6.7%, respectively. For the years ended December 31, 2013, 2012 and 2011, the non-U.S. income tax rates were (5.3)%, (1.2)% and 3.9%, respectively.

We reflect a low or negative effective tax rate due to a non-U.S. operation where income is taxed at a low rate due to a significant tax holiday granted to us by Malaysia effective through December 31, 2021 subject to our satisfaction of certain conditions that we expect to continue to satisfy, and where the tax benefit of losses that are expected to be realized accrue in higher tax rate jurisdictions. The benefit of this incentive in Malaysia for the years ended December 31, 2013, 2012 and 2011 is estimated to be approximately $32.0 million, $45.0 million and $25.5 million, respectively. We also have tax incentives in other jurisdictions that are not material to our overall tax rate. The combined effective tax rate is also impacted by the valuation allowance applied against U.S. losses.

Table of Contents

Segment Results of Operations

The summary that follows provides a discussion of the results of operations of both reportable segments (Mobile Consumer Electronics ("MCE") and Specialty Components ("SC")). See Note 15. Segment Information of the notes to the Combined Financial Statements for a reconciliation of segment revenue, segment earnings before interest, taxes, depreciation and amortization (EBITDA), and operating margin to our combined results.

We use the terms "EBITDA" and "EBITDA margin", defined as net earnings plus (i) depreciation and amortization expense, (ii) interest expense and (iii) income taxes, and EBITDA as a percentage of revenue, respectively. EBITDA and EBITDA margin are not presented in accordance with GAAP and may not be comparable to similarly titled measures used by other companies. We use EBITDA and EBITDA margin as supplements to our GAAP results of operations as these measures remove from operating results the impact of items that, in our opinion, do not reflect our core operating performance. The costs of certain shared resources are allocated between segments based on each segment's estimated usage of the shared resources. Other indirect items that are maintained at the corporate level and are not allocated to the segments include executive and functional compensation costs and other administrative expenses relating to the corporate headquarters.

Mobile Consumer Electronics

| (in thousands) | Years Ended December 31, | | | % Change [1] | |
|---|---|---|---|---|---|
| | 2013 | 2012 | 2011 | 2013 vs. 2012 | 2012 vs. 2011 |
| Revenue | $777,171 | $670,358 | $509,916 | 15.9 % | 31.5 % |
| Operating earnings | $122,530 | $102,742 | $106,224 | 19.3 % | (3.3 )% |
| Other income (expense) | (493 ) | (2,334 ) | (477 ) | n/m | n/m |
| Depreciation and amortization | 100,257 | | | | |

**ARTICLE VII.**
**AWARD OF RESTRICTED STOCK**

7.1. *Eligibility*. Subject to the Award Limit, Restricted Stock may be awarded to any Employee who the Administrator determines is a key Employee, or any Independent Director or any Consultant who the Administrator determines should receive such an Award.

7.2. *Award of Restricted Stock*.

(a) The Administrator may from time to time, in its absolute discretion:

(i) Determine which Employees are key Employees, and select from among the Key Employees, Independent Directors or Consultants (including Employees, Independent Directors or Consultants who have previously received Awards under the Plan) such of them as in its opinion should be awarded Restricted Stock; and

(ii) Determine the purchase price, if any, and other terms and conditions applicable to such Restricted Stock, consistent with the Plan.

(b) The Administrator shall establish the purchase price, if any, and form of payment for Restricted Stock. In all cases, legal consideration shall be required for each issuance of Restricted Stock.

(c) Upon the selection of an Employee, Independent Director or Consultant to be awarded Restricted Stock, the Administrator shall instruct the Secretary of the Company to issue such Restricted Stock and may impose such conditions on the issuance of such Restricted Stock as it deems appropriate.

7.3. *Automatic Independent Directors Awards*.

(a) Any individual who first becomes an Independent Director during the term of the Plan shall, on the date of his or her initial election or appointment to be an Independent Director, automatically be granted a Restricted Stock award covering 3,000 shares; *provided*, that if such individual s initial appointment or election to be an Independent Director occurs at any time other than an annual meeting at which members of the class of directors to which such individual becomes a member are standing for re-election, such individual shall instead receive a Restricted Stock award covering 3,000 shares, less 250 shares for each calendar quarter ended since the last annual meeting at

B-13

which members of the class of directors to which such individual is elected were standing for re-election. Notwithstanding the foregoing, in no event shall any former Employee receive a Restricted Stock award pursuant to this Section 7.3(a).

(b) On the date of each annual meeting of the shareholders during the term of the Plan, beginning with the annual meeting at which the Plan is submitted for shareholder approval, each Independent Director who is standing for re-election to the Board at that particular annual meeting of shareholders shall automatically be granted a Restricted Stock award covering 3,000 shares of Common Stock; *provided*, that such individual continues to serve as an Independent Director as of such date.

(c) All of the shares of Common Stock subject to each Restricted Stock award granted pursuant to this Section 7.3 shall initially be subject to forfeiture upon the Independent Director s Termination of Directorship. The shares of Common Stock subject to each such Restricted Stock award shall vest, and the forfeiture restrictions shall lapse, with respect to 250 of the shares of Common Stock upon the last business day of each calendar quarter occurring after the date of grant; *provided*, that unless otherwise determined by the Board prior to an Independent Director s Termination of Directorship, in no event shall an Independent Director vest in any additional shares of Common Stock following his or her Termination of Directorship.

(d) The grants authorized by this Section 7.3 are subject to shareholder approval of (i) the Plan and (ii) an amendment to the Company s Articles of Association increasing the authorized number of shares of Common Stock by at least 1,000,000 shares.

7.4. *Rights as Shareholders*.

Subject to Section 7.5, upon delivery of the shares of Restricted Stock to the escrow holder pursuant to Section 7.7, the Holder shall have, unless otherwise provided by the Administrator, all the rights of a shareholder with respect to said shares, subject to the restrictions in his or her Award Agreement, including the right to receive all dividends and other distributions paid or made with respect to the shares; *provided*, *however*, that, in the discretion of the Administrator, any extraordinary distributions with respect to the Common Stock shall be subject to the restrictions set forth in Section 7.5.

7.5. *Restriction*. All shares of Restricted Stock issued under the Plan (including any shares received by Holders thereof with respect to shares of Restricted Stock as a result of stock dividends, stock splits or any other form of recapitalization) shall, in the terms of each individual Award Agreement, be subject to such restrictions as the Administrator shall provide, which restrictions may include, without limitation, restrictions concerning voting rights and transferability and restrictions based on duration of employment, directorship or consultancy with the Company, Company performance and individual performance; *provided*, *however*, that, unless the Administrator otherwise provides in the terms of the Award Agreement or otherwise, no share of Restricted Stock granted to a person subject to Section 16 of the Exchange Act shall be sold, assigned or otherwise transferred until at least six months and one day have elapsed from the date on which the Restricted Stock was issued, and *provided*, *further*, that, except with respect to shares of Restricted Stock granted to Covered Employees that are expected to qualify as performance-based compensation for purposes of Section 162(m)(4)(C) of the Code, by action taken after the Restricted Stock is issued, the Administrator may, on such terms and conditions as it may determine to be appropriate, remove any or all of the restrictions imposed by the terms of the Award Agreement. Restricted Stock may not be sold or encumbered until all restrictions are terminated or expire. If no consideration was paid by the Holder upon issuance, a Holder s rights in unvested Restricted Stock shall lapse, and such Restricted Stock shall be surrendered to the Company without consideration, upon Termination of Employment, Termination of Directorship, or Termination of Consultancy, as applicable; and, *provided*, *however*, that the Administrator in its sole and absolute discretion may provide that such rights shall not lapse in the event of a Termination of Employment, Termination of Directorship or

B-14

Termination of Consultancy, as applicable, following a change of ownership or control (within the meaning of Treasury Regulation Section 1.162-27(e)(2)(v) or any successor regulation thereto) of the Company or because of the Holder s death or disability; and, *provided*, *further*, except with respect to shares of Restricted Stock granted to Covered Employees, the Administrator in its sole and absolute discretion may provide that no such lapse or surrender shall occur in the event of a Termination of Employment, Termination of Directorship, or Termination of Consultancy, as applicable, without cause or following any Change in Control or because of the Holder s retirement, or otherwise.

7.6. *Repurchase of Restricted Stock*. The Administrator shall provide in the terms of each individual Award Agreement that the Company shall have the right to repurchase from the Holder the Restricted Stock then subject to restrictions under the Award Agreement immediately upon a Termination of Employment, Termination of Directorship, or Termination of Consultancy, as applicable, at a cash price per share equal to the price paid by the Holder for such Restricted Stock; *provided*, *however*, that the Administrator in its sole and absolute discretion may provide that no such right of repurchase shall exist in the event of a Termination of Employment, Termination of Directorship or Termination of Consultancy, as applicable, following a change of ownership or control (within the meaning of Treasury Regulation Section 1.162-27(e)(2)(v) or any successor regulation thereto) of the Company or because of the Holder s death or disability; and, *provided*, *further*, that, except with respect to shares of Restricted Stock granted to Covered Employees, the Administrator in its sole and absolute discretion may provide that no such right of repurchase shall exist in the event of a Termination of Employment, Termination of Directorship, or Termination of Consultancy, as applicable, without cause or following any Change in Control or because of the Holder s retirement, or otherwise.

7.7. *Escrow*. The Secretary of the Company or such other escrow holder as the Administrator may appoint shall retain physical custody of each certificate representing Restricted Stock until all of the restrictions imposed under the Award Agreement with respect to the shares evidenced by such certificate expire or shall have been removed.

7.8. *Legend*. In order to enforce the restrictions imposed upon shares of Restricted Stock hereunder, the Administrator shall cause a legend or legends to be placed on certificates representing all shares of Restricted Stock that are still subject to restrictions under Award Agreements, which legend or legends shall make appropriate reference to the conditions imposed thereby.

7.9. *Section 83(b) Election*. If a Holder makes an election under Section 83(b) of the Code, or any successor section thereto, to be taxed with respect to the Restricted Stock as of the date of transfer of the Restricted Stock rather than as of the date or dates upon which the Holder would otherwise be taxable under Section 83(a) of the Code, the Holder shall deliver a copy of such election to the Company immediately after filing such election with the Internal Revenue Service.

**ARTICLE VIII.**

**PERFORMANCE AWARDS, DIVIDEND EQUIVALENTS, DEFERRED STOCK, STOCK PAYMENTS, RESTRICTED STOCK UNITS**

8.1. *Eligibility*. Subject to the Award Limit, one or more Performance Awards, Dividend Equivalent awards, Deferred Stock awards, Stock Payment awards, and/or Restricted Stock Unit awards may be granted to any Employee whom the Administrator determines is a key Employee, or any Independent Director or any Consultant whom the Administrator determines should receive such an Award.

8.2. *Performance Awards*.

(a) Any key Employee, Independent Director or Consultant selected by the Administrator may be granted one or more Performance Awards. The value of such Performance Awards may be linked to any one or more of the Performance Criteria or other specific performance criteria determined appropriate by the Administrator, in each case on a specified date or dates or over any period or periods determined by the Administrator. In making such determinations, the Administrator shall consider (among such other factors as it deems relevant in light of the specific type of award) the contributions, responsibilities and other compensation of the particular key Employee, Independent Director or Consultant.

(b) Without limiting Section 8.2(a), the Administrator may grant Performance Awards to any Covered Employee in the form of a cash bonus payable upon the attainment of objective Performance Goals which are established by the Administrator, in each case on a specified date or dates or over any period or periods determined by the Administrator. Any such bonuses paid to Covered Employees shall be based upon objectively determinable bonus formulas established in accordance with the provisions of Section 3.2. The maximum aggregate amount of all Performance Awards granted to a Covered Employee under this Section 8.2(b) during any fiscal year shall not exceed the Award Limit. Unless otherwise specified by the Administrator at the time of grant, the Performance Criteria with respect to a Performance Award payable to a Covered Employee shall be determined on the basis of generally accepted accounting principles.

8.3. *Dividend Equivalents*.

(a) Any key Employee, Independent Director or Consultant selected by the Administrator may be granted Dividend Equivalents based on the dividends declared on Common Stock, to be credited as of dividend payment dates, during the period between the date a Stock Appreciation Right, Deferred Stock, Performance Award or Restricted Stock Unit award is granted and the date such Stock Appreciation Right, Deferred Stock, Performance Award or Restricted Stock Unit award vests, is exercised, is distributed or expires, as determined by the Administrator. Such Dividend Equivalents shall be converted to cash or additional shares of Common Stock by such formula and at such time and subject to such limitations as may be determined by the Administrator.

(b) Any Holder of an Option who is an Employee, Independent Director or Consultant selected by the Administrator may be granted Dividend Equivalents based on the dividends declared on Common Stock, to be credited as of dividend payment dates, during the period between the date an Option is granted and the date such Option vests, is exercised, or expires, as determined by the Administrator. Such Dividend Equivalents shall be converted to cash or additional shares of Common Stock by such formula and at such time and subject to such limitations as may be determined by the Administrator.

(c) Dividend Equivalents granted with respect to Options intended to be qualified performance-based compensation for purposes of Section 162(m) of the Code shall be payable, with respect to pre-exercise periods, regardless of whether such Option is subsequently exercised.

8.4. *Stock Payments*. Any key Employee, Independent Director or Consultant selected by the Administrator may receive Stock Payments in the manner determined from time to time by the Administrator. The number of shares shall be determined by the Administrator and may be based upon the Performance Criteria or other specific performance criteria determined appropriate by the Administrator, determined on the date such Stock Payment is made or on any date thereafter.

8.5. *Deferred Stock*. Any key Employee, Independent Director or Consultant selected by the Administrator may be granted an award of Deferred Stock in the manner determined from time to time by the Administrator. The number of shares of Deferred Stock shall be determined by the Administrator and may be linked to the satisfaction of one or more Performance Goals or other specific performance goals as the Administrator determines to be appropriate at the time of the grant, in each case on a specified date or dates or over any period or periods determined by the Administrator. Common Stock underlying a Deferred Stock award will not be issued until the Deferred Stock award has vested, pursuant to a vesting schedule or performance criteria set by the Administrator. Unless otherwise provided by the Administrator, a Holder of Deferred Stock shall have no rights as a Company shareholder with respect to such Deferred Stock until such time as the Award has vested and the Common Stock underlying the Award has been issued.

8.6. *Restricted Stock Units*. Any key Employee, Independent Director or Consultant selected by the Administrator may be granted an award of Restricted Stock Units in the manner determined from time to time by the Administrator. The Administrator is authorized to make awards of Restricted Stock Units in such amounts and subject to such terms and conditions as determined by the Administrator. The Administrator shall specify the date or dates on which the Restricted Stock Units shall become fully vested and nonforfeitable, and may specify such conditions to vesting as it deems appropriate, and may specify that such Restricted Stock Units become fully vested and nonforfeitable pursuant to the satisfaction of one or more Performance Goals or other specific performance goals as the Administrator determines to be appropriate at the time of the grant, in each case on a specified date or dates or over any period or periods determined by the Administrator. The Administrator shall specify the distribution dates applicable to each award of Restricted Stock Units which shall be no earlier than the vesting dates or events of the award and may be determined at the election of the Employee, Independent Director or Consultant, subject to compliance with Section 409A of the Code. On the distribution dates, the Company shall issue to the Holder one unrestricted, fully transferable share of Common Stock for each Restricted Stock Unit distributed.

8.7. *Term*. The term of a Performance Award, Dividend Equivalent award, Deferred Stock award, Stock Payment award and/or Restricted Stock Unit award shall be set by the Administrator in its discretion.

8.8. *Exercise or Purchase Price*. The Administrator may establish the exercise or purchase price of a Performance Award, shares of Deferred Stock, shares distributed as a Stock Payment award or shares distributed pursuant to a Restricted Stock Unit award.

8.9. *Exercise upon Termination of Employment, Termination of Consultancy or Termination of Directorship*. A Performance Award, Dividend Equivalent award, Deferred Stock award, Stock Payment award and/or Restricted Stock Unit award is exercisable or distributable only while the Holder is an Employee, Consultant or Independent Director, as applicable; *provided*, *however*, that the Administrator in its sole and absolute discretion may provide that the Performance Award, Dividend Equivalent award, Deferred Stock award, Stock Payment award and/or Restricted Stock Unit award may be exercised or distributed subsequent to a Termination of Employment, Termination of Directorship or Termination of Consultancy following a change of control or ownership (within the meaning of Section 1.162-27(e)(2)(v) or any successor regulation thereto) of the Company; and, *provided*, *further*, that, except with respect to Performance Awards granted to Covered Employees, the Administrator in its sole and absolute discretion may provide that Performance Awards may be exercised or paid following a Termination of Employment, Termination of Directorship or Termination of Consultancy without cause, or following a Change in Control, or because of the Holder s retirement, death or disability, or otherwise.

**8.10.** ***Form of Payment.*** Payment of the amount determined under Section 8.2 or 8.3 above shall be in cash, in Common Stock or a combination of both, as determined by the Administrator. To the extent any payment under this Article VIII is effected in Common Stock, it shall be made subject to satisfaction of all provisions of Section 6.3.

**ARTICLE IX.**

**STOCK APPRECIATION RIGHTS**

9.1. *Grant of Stock Appreciation Rights*. A Stock Appreciation Right may be granted to any key Employee, Independent Director or Consultant selected by the Administrator. A Stock Appreciation Right may be granted: (a) in connection and simultaneously with the grant of an Option, or (b) independent of an Option. A Stock Appreciation Right shall be subject to such terms and conditions not inconsistent with the Plan as the Administrator shall impose and shall be evidenced by an Award Agreement.

9.2. *Coupled Stock Appreciation Rights*.

(a) A Coupled Stock Appreciation Right ( *CSAR* ) shall be related to a particular Option and shall be exercisable only when and to the extent the related Option is exercisable.

(b) A CSAR may be granted to the Holder for no more than the number of shares subject to the simultaneously granted Option to which it is coupled.

(c) A CSAR shall entitle the Holder (or other person entitled to exercise the Option pursuant to the Plan) to surrender to the Company unexercised a portion of the Option to which the CSAR relates (to the extent then exercisable pursuant to its terms) and to receive from the Company in exchange therefor an amount determined by multiplying (i) the difference obtained by subtracting the exercise price per share of the CSAR from the Fair Market Value of a share of Common Stock on the date of exercise of the CSAR by (ii) the number of shares of Common Stock with respect to which the CSAR shall have been exercised, subject to any limitations the Administrator may impose.

9.3. *Independent Stock Appreciation Rights*.

(a) An Independent Stock Appreciation Right ( *ISAR* ) shall be unrelated to any Option and shall have a term set by the Administrator. An ISAR shall be exercisable in such installments as the Administrator may determine. An ISAR shall cover such number of shares of Common Stock as the Administrator may determine; *provided*, *however*, that unless the Administrator otherwise provides in the terms of the ISAR or otherwise, no ISAR granted to a person subject to Section 16 of the Exchange Act shall be exercisable until at least six months have elapsed following the date on which the ISAR was granted. The exercise price per share of Common Stock subject to each ISAR shall be set by the Administrator; *provided*, that such exercise price per share shall not be less than 100% of the Fair Market Value of a share of Common Stock on the date the ISAR is granted. An ISAR is exercisable only while the Holder is an Employee, Independent Director or Consultant; *provided*, that the Administrator may determine that the ISAR may be exercised subsequent to Termination of Employment, Termination of Directorship or Termination of Consultancy without cause, or following a Change in Control of the Company, or because of the Holder s retirement, death or disability, or otherwise.

(b) An ISAR shall entitle the Holder (or other person entitled to exercise the ISAR pursuant to the Plan) to exercise all or a specified portion of the ISAR (to the extent then exercisable pursuant to its terms) and to receive from the Company an amount determined by multiplying (i) the difference obtained by subtracting the exercise price per share of the ISAR from the Fair Market Value of a share of Common Stock on the date of exercise of the ISAR by (ii) the number of shares of Common Stock with respect to which the ISAR shall have been exercised, subject to any limitations the Administrator may impose.

9.4. *Payment and Limitations on Exercise*.

(a) Payment of the amounts determined under Section 9.2(c) and 9.3(b) above shall be in cash, shares of Common Stock (based on its Fair Market Value as of the date the Stock Appreciation

Right is exercised), or a combination of both, as determined by the Administrator. The Company shall not be required to issue or deliver any certificate or certificates for shares of stock issuable upon the exercise of any Stock Appreciation Right prior to fulfillment of the conditions set forth in Section 6.3 above.

(b) Holders of Stock Appreciation Rights may be required to comply with any timing or other restrictions with respect to the settlement or exercise of a Stock Appreciation Right, including a window-period limitation, as may be imposed in the discretion of the Administrator.

**ARTICLE X.**

**ADMINISTRATION**

10.1. *Compensation Committee*. The Compensation Committee (or another committee or a subcommittee of the Board assuming the functions of the Committee under the Plan) shall consist solely of two or more Independent Directors appointed by and holding office at the pleasure of the Board, each of whom is intended to qualify as both a non-employee director as defined by Rule 16b-3 and an outside director for purposes of Section 162(m) of the Code. Appointment of Committee members shall be effective upon acceptance of appointment. Committee members may resign at any time by delivering written notice to the Board. Vacancies in the Committee may be filled by the Board.

10.2. *Duties and Powers of Committee*. It shall be the duty of the Committee to conduct the general administration of the Plan in accordance with its provisions. The Committee shall have the power to interpret the Plan and the Award Agreements, and to adopt such rules for the administration, interpretation and application of the Plan as are consistent therewith, to interpret, amend or revoke any such rules and to amend any Award Agreement provided that the rights or obligations of the Holder of the Award that is the subject of any such Award Agreement are not affected adversely. Any such grant or award under the Plan need not be the same with respect to each Holder. Any such interpretations and rules with respect to Incentive Stock Options shall be consistent with the provisions of Section 422 of the Code. In its absolute discretion, the Board may at any time and from time to time exercise any and all rights and duties of the Committee under the Plan except with respect to matters which under Rule 16b-3 or Section 162(m) of the Code, or any regulations or rules issued thereunder, are required to be determined in the sole discretion of the Committee. Notwithstanding the foregoing, the full Board, acting by a majority of its members in office, shall conduct the general administration of the Plan with respect to Awards granted to Independent Directors.

10.3. *Majority Rule; Unanimous Written Consent*. The Committee shall act by a majority of its members in attendance at a meeting at which a quorum is present or by a memorandum or other written instrument signed by all members of the Committee.

10.4. *Compensation; Professional Assistance; Good Faith Actions*. Members of the Committee shall receive such compensation, if any, for their services as members as may be determined by the Board. All expenses and liabilities which members of the Committee incur in connection with the administration of the Plan shall be borne by the Company. The Committee may, with the approval of the Board, employ attorneys, consultants, accountants, appraisers, brokers or other persons. The Committee, the Company and the Company s officers and Directors shall be entitled to rely upon the advice, opinions or valuations of any such persons. All actions taken and all interpretations and determinations made by the Committee or the Board in good faith shall be final and binding upon all Holders, the Company and all other interested persons. No members of the Committee or Board shall be personally liable for any action, determination or interpretation made in good faith with respect to the Plan or Awards, and all members of the Committee and the Board shall be fully protected by the Company in respect of any such action, determination or interpretation.

10.5. *Delegation of Authority Grant Awards*. To the extent permitted by applicable law, the Committee may from time to time delegate to a committee of two or more members of the Board the authority to grant or amend Awards; *provided*, *however*, that the Committee may not delegate its authority to grant Awards to, or amend the Awards of, individuals: (a) who are senior executives of the Company who are subject to Section 16 of the Exchange Act, (b) who are Covered Employees, or (c) who are members of the Board to whom authority to grant or amend Awards has been delegated hereunder. Any delegation hereunder shall be subject to the restrictions and limits that the Committee specifies at the time of such delegation of authority and may be rescinded at any time by the Committee. At all times, any committee appointed under this Section 10.5 shall serve in such capacity at the pleasure of the Committee.

**ARTICLE XI.**

**MISCELLANEOUS PROVISIONS**

11.1. *Transferability of Awards.*

(a) Except as otherwise provided in Section 11.1(b):

(i) No Award under the Plan may be sold, pledged, assigned or transferred in any manner other than by will or the laws of descent and distribution or, subject to the consent of the Administrator, pursuant to a DRO, unless and until such Award has been exercised, or the shares underlying such Award have been issued, and all restrictions applicable to such shares have lapsed;

(ii) No Award or interest or right therein shall be liable for the debts, contracts or engagements of the Holder or his successors in interest or shall be subject to disposition by transfer, alienation, anticipation, pledge, hypothecation, encumbrance, assignment or any other means whether such disposition be voluntary or involuntary or by operation of law by judgment, levy, attachment, garnishment or any other legal or equitable proceedings (including bankruptcy), and any attempted disposition thereof shall be null and void and of no effect, except to the extent that such disposition is permitted by the preceding sentence; and

(iii) During the lifetime of the Holder, only the Holder may exercise an Option or other Award (or any portion thereof) granted to him under the Plan, unless it has been disposed of pursuant to a DRO; after the death of the Holder, any exercisable portion of an Option or other Award may, prior to the time when such portion becomes unexercisable under the Plan or the applicable Award Agreement, be exercised by his personal representative or by any person empowered to do so under the deceased Holder s will or under the then applicable laws of descent and distribution.

(b) Notwithstanding Section 11.1(a), the Administrator, in its sole discretion, may determine to permit a Holder to transfer a Non-Qualified Stock Option to any one or more Permitted Transferees (as defined below), subject to the following terms and conditions: (i) a Non-Qualified Stock Option transferred to a Permitted Transferee shall not be assignable or transferable by the Permitted Transferee other than by will or the laws of descent and distribution; (ii) any Non-Qualified Stock Option which is transferred to a Permitted Transferee shall continue to be subject to all the terms and conditions of the Non-Qualified Stock Option as applicable to the original Holder (other than the ability to further transfer the Non-Qualified Stock Option); and (iii) the Holder and the Permitted Transferee shall execute any and all documents requested by the Administrator, including, without limitation documents to (A) confirm the status of the transferee as a Permitted Transferee, (B) satisfy any requirements for an exemption for the transfer under applicable federal and state securities laws and (C) evidence the transfer. For purposes of this Section 11.1(b), *Permitted Transferee* shall mean, with respect to a Holder, any child, stepchild, grandchild, parent, stepparent, grandparent, spouse, former spouse, sibling, niece, nephew, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law, including adoptive relationships, any person sharing the Holder s household (other than a tenant or employee), a trust in which these persons (or the Holder) control the management of assets, and any other entity in which these persons (or the Holder) own more than fifty percent of the voting interests, or any other transferee specifically approved by the Administrator after taking into account any state or federal tax or securities laws applicable to transferable Non-Qualified Stock Options.

11.2. *Amendment, Suspension or Termination of the Plan.* Except as otherwise provided in this Section 11.2, the Plan may be wholly or partially amended or otherwise modified, suspended or terminated at any time or from time to time by the Administrator. However, without approval of the Company s shareholders given within twelve (12) months before or after the action by the Administrator, no action of the Administrator may, except as provided in Section 11.3, (i) increase the limits imposed in Section 2.1 on the maximum number of shares which may be issued under the Plan, or (ii) decrease the exercise price of any outstanding Option or Stock Appreciation Right granted under the Plan. Except as provided in Section 11.11, no amendment, suspension or termination of the Plan shall, without the consent of the Holder, alter or impair any rights or obligations under any Award theretofore granted or awarded, unless the Award itself otherwise expressly so provides. No Awards may be granted or awarded during any period of suspension or after termination of the Plan, and in no event may any Award be granted under the Plan after the first to occur of the following events:

(a) The expiration of ten (10) years from the date the Plan is adopted by the Board; or

(b) The expiration of ten (10) years from the date the Plan is approved by the Company s shareholders.

11.3. *Changes in Common Stock or Assets of the Company, Acquisition or Liquidation of the Company and Other Corporate Events.*

(a) Subject to Section 11.3(e), in the event that the Administrator determines that any dividend or other distribution (whether in the form of cash, Common Stock, other securities or other property), recapitalization, reclassification, stock split, reverse stock split, reorganization, merger, consolidation, split-up, spin-off, combination, repurchase, liquidation, dissolution, or sale, transfer, exchange or other disposition of all or substantially all of the assets of the Company, or exchange of Common Stock or other securities of the Company, issuance of warrants or other rights to purchase Common Stock or other securities of the Company, or other similar corporate transaction or event, in the Administrator s sole discretion, affects the Common Stock such that an adjustment is determined by the Administrator to be appropriate in order to prevent dilution or enlargement of the benefits or potential benefits intended to be made available under the Plan or with respect to an Award, then the Administrator shall, in such manner as it may deem equitable, adjust any or all of:

(i) The number and kind of shares of Common Stock (or other securities or property) with respect to which Awards may be granted or awarded (including, but not limited to, adjustments of the limitations in Section 2.1 on the maximum number and kind of shares which may be issued under the Plan, and adjustments of the Award Limit);

(ii) The number and kind of shares of Common Stock (or other securities or property) subject to outstanding Awards;

(iii) The number and kind of shares of Common Stock (or other securities or property) for which automatic grants are subsequently to be made to new and continuing Independent Directors pursuant to Section 7.3;

(iv) The number and kind of shares of Common Stock (or other securities or property) for which each automatic grant made to new and continuing Independent Directors pursuant to Section 7.3 will subsequently become vested on the last business day of each calendar quarter; and

(v) The grant or exercise price with respect to any Award.

(b) Subject to Sections 11.3(c) and 11.3(e), in the event of any transaction or event described in Section 11.3(a) or any unusual or nonrecurring transactions or events affecting the Company, any affiliate of the Company, or the financial statements of the Company or any affiliate, or of changes in applicable laws, regulations or accounting principles, the Administrator, in its sole and absolute discretion, and on such terms and conditions as it deems appropriate, either by the terms of the Award or by action taken prior to the occurrence of such transaction or event and either automatically or upon the Holder s request, is hereby authorized to take any one or more of the following actions whenever the Administrator determines that such action is appropriate in order to prevent dilution or enlargement of the benefits or potential benefits intended to be made available under the Plan or with respect to any Award under the Plan, to facilitate such transactions or events or to give effect to such changes in laws, regulations or principles:

(i) To provide for either the purchase of any such Award for an amount of cash equal to the amount that could have been attained upon the exercise of such Award or realization of the Holder s rights had such Award been currently exercisable or payable or fully vested or the replacement of such Award with other rights or property selected by the Administrator in its sole discretion;

(ii) To provide that the Award cannot vest, be exercised or become payable after such event;

(iii) To provide that such Award shall be exercisable as to all shares covered thereby, notwithstanding anything to the contrary in Section 5.3 or the provisions of such Award;

(iv) To provide that such Award be assumed by the successor or survivor corporation, or a parent or subsidiary thereof, or shall be substituted for by similar options, rights or awards covering the stock of the successor or survivor corporation, or a parent or subsidiary thereof, with appropriate adjustments as to the number and kind of shares and prices;

(v) To make adjustments in the number and type of shares of Common Stock (or other securities or property) subject to outstanding Awards, and/or in the terms and conditions of (including the grant, exercise or purchase price), and the criteria included in, outstanding options, rights and awards and options, rights and awards which may be granted in the future; and

(vi) To provide that, for a specified period of time prior to such event, the restrictions imposed under an Award Agreement upon some or all shares of Restricted Stock, Restricted Stock Units or Deferred Stock may be terminated, and, in the case of Restricted Stock, some or all shares of such Restricted Stock may cease to be subject to repurchase under Section 7.6 or forfeiture under Section 7.5 after such event.

(c) Notwithstanding any other provision of the Plan, in the event of a Change in Control, each outstanding Award shall be assumed or an equivalent Award substituted by the successor corporation or a parent or subsidiary of the successor corporation. In the event that the successor corporation refuses to assume or substitute for the Award, the Administrator may cause any or all of such Awards to become fully exercisable immediately prior to the consummation of such transaction and all forfeiture restrictions on any or all of such Awards to lapse. If an Award is exercisable in lieu of assumption or substitution in the event of a Change in Control, the Administrator shall notify the Holder that the Award shall be fully exercisable for a period of fifteen (15) days from the date of such notice, and the Award shall terminate upon the expiration of such period. For the purposes of this Section 11.3(c), an Award shall be considered assumed if, following the Change in Control, the Award confers the right to purchase or receive, for each share of Common Stock subject to the Award immediately prior to the Change in Control, the consideration (whether stock, cash, or other securities or property) received in the Change in Control by holders of Common Stock for each share held on the effective date of the transaction (and if holders were offered a choice of consideration, the type of consideration chosen by the holders of a majority of the outstanding shares); *provided*, *however*, that if such consideration received in the Change in Control was not solely common stock of the successor corporation or its parent, the Administrator may, with the consent of the successor corporation, provide for the consideration to be received upon the exercise of the Award, for each share of Common Stock subject to an Award, to be solely common stock of the successor corporation or its parent equal in fair market value to the per share consideration received by holders of Common Stock in the Change in Control.

(d) Subject to Sections 11.3(e), 3.2 and 3.3, the Administrator may, in its discretion, include such further provisions and limitations in any Award, agreement or certificate, as it may deem equitable and in the best interests of the Company.

(e) With respect to Awards which are granted to Covered Employees and are intended to qualify as performance-based compensation under Section 162(m)(4)(C), no adjustment or action described in this Section 11.3 or in any other provision of the Plan shall be authorized to the extent that such adjustment or action would cause such Award to fail to so qualify under Section 162(m)(4)(C), or any successor provisions thereto. No adjustment or action described in this Section 11.3 or in any other provision of the Plan shall be authorized to the extent that such adjustment or action would cause the Plan to violate Section 422(b)(1) of the Code. Furthermore, no such adjustment or action shall be authorized to the extent such adjustment or action would result in short-swing profits liability under Section 16 or violate the exemptive conditions of Rule 16b-3 unless the Administrator determines that the Award is not to comply with such exemptive conditions. The number of shares of Common Stock subject to any Award shall always be rounded down to the next whole number.

(f) The existence of the Plan, the Award Agreement and the Awards granted hereunder shall not affect or restrict in any way the right or power of the Company or the shareholders of the Company to make or authorize any adjustment, recapitalization, reorganization or other change in the Company s capital structure or its business, any merger or consolidation of the Company, any issue of stock or of options, warrants or rights to purchase stock or of bonds, debentures, preferred or prior preference stocks whose rights are superior to or affect the Common Stock or the rights thereof or which are convertible into or exchangeable for Common Stock, or the dissolution or liquidation of the company, or any sale or transfer of all or any part of its assets or business, or any other corporate act or proceeding, whether of a similar character or otherwise.

(g) No action shall be taken under this Section 11.3 which shall cause an Award to fail to comply with Section 409A of the Code or the Treasury Regulations thereunder, to the extent applicable to such Award.

11.4. *Approval of Plan by Shareholders.* The Plan will be submitted for the approval of the Company s shareholders within twelve (12) months after the date of the Board s initial adoption of the Plan. No Awards may be granted or awarded prior to shareholder approval of (i) the Plan and (ii) an amendment to the Company s Articles of Association increasing the authorized number of shares of Common Stock by at least 1,000,000 shares. In addition, if the Board determines that Awards other than Options or Stock Appreciation Rights which may be granted to Covered Employees should continue to be eligible to qualify as performance-based compensation under Section 162(m)(4)(C) of the Code, the Performance Criteria must be disclosed to and approved by the Company s shareholders no later than the first shareholder meeting that occurs in the fifth year following the year in which the Company s shareholders previously approved the Plan.

11.5. *Tax Withholding.* The Company or any Subsidiary shall have the authority and the right to deduct or withhold, or require a Holder to remit to the Company, an amount sufficient to satisfy federal, state, local and foreign taxes required by law to be withheld with respect to any taxable event concerning a Holder arising as a result of this Plan. The Administrator may in its discretion and in satisfaction of the foregoing requirement allow a Holder to elect to have the Company withhold shares of Common Stock otherwise issuable under an Award (or allow the return of shares of Common Stock) having a Fair Market Value equal to the sums required to be withheld. Notwithstanding any other provision of the Plan, the number of shares of Common Stock which may be withheld with respect to the issuance, vesting, exercise or payment of any Award (or which may be repurchased from the Holder of such Award within six months (or such other period as may be determined by the Administrator) after such shares of Common Stock were acquired by the Holder from the Company) in order to satisfy the Holder s federal, state, local and foreign income and payroll tax liabilities with respect to the issuance, vesting, exercise or payment of the Award shall be limited to the number of shares which have a Fair Market Value on the date of withholding or repurchase equal to the aggregate amount of such liabilities based on the minimum statutory withholding rates for federal, state, local and foreign income tax and payroll tax purposes that are applicable to such supplemental taxable income.

11.6. *Prohibition on Repricing*. Subject to Section 11.3, the Administrator shall not, without the approval of the shareholders of the Company authorize the amendment of any outstanding Award to reduce its price per share. Furthermore, no Award shall be canceled and replaced with the grant of an Award having a lesser price per share without the further approval of shareholders of the Company.

11.7. *Effect of Plan upon Options and Compensation Plans.* The adoption of the Plan shall not affect any other compensation or incentive plans in effect for the Company or any Subsidiary. Nothing in the Plan shall be construed to limit the right of the Company: (a) to establish any other forms of incentives or compensation for Employees, Directors or Consultants of the Company or any Subsidiary, or (b) to grant or assume options or other rights or awards otherwise than under the Plan in connection with any proper corporate purpose including, without limitation, the grant or assumption of options in connection with the acquisition by purchase, lease, merger, consolidation or otherwise, of the business, stock or assets of any corporation, partnership, limited liability company, firm or association.

11.8. *Compliance with Laws.* The Plan, the granting and vesting of Awards under the Plan and the issuance and delivery of shares of Common Stock and the payment of money under the Plan or under Awards granted or awarded hereunder are subject to compliance with all applicable federal and state laws, rules and regulations (including but not limited to state and federal securities law and federal margin requirements) and to such approvals by any listing, regulatory or governmental authority as may, in the opinion of counsel for the Company, be necessary or advisable in connection therewith. Any securities delivered under the Plan shall be subject to such restrictions, and the person acquiring such securities shall, if requested by the Company, provide such assurances and representations to the Company as the Company may deem necessary or desirable to assure compliance with all applicable legal requirements. To the extent permitted by applicable law, the Plan and Awards granted or awarded hereunder shall be deemed amended to the extent necessary to conform to such laws, rules and regulations.

11.9. *Titles*. Titles are provided herein for convenience only and are not to serve as a basis for interpretation or construction of the Plan.

11.10. *Governing Law.* The Plan and any agreements hereunder shall be administered, interpreted and enforced under the internal laws of the State of Hawaii without regard to conflicts of laws thereof.

11.11. *Section 409A.* To the extent that the Administrator determines that any Award granted under the Plan is subject to Section 409A of the Code, the Award Agreement evidencing such Award shall incorporate the terms and conditions required by Section 409A of the Code. To the extent applicable, the Plan and Award Agreements shall be interpreted in accordance with Section 409A of the Code and Department of Treasury regulations and other interpretive guidance issued thereunder, including without limitation any such regulations or other guidance that may be issued after the Effective Date. Notwithstanding any provision of the Plan to the contrary, in the event that following the Effective Date the Administrator determines that any Award may be subject to Section 409A of the Code and related Department of Treasury guidance (including such Department of Treasury guidance as may be issued after the Effective Date), the Administrator may adopt such amendments to the Plan and the applicable Award Agreement or adopt other policies and procedures (including amendments, policies and procedures with retroactive effect), or take any other actions, that the Administrator determines are necessary or appropriate to (a) exempt the Award from Section 409A of the Code and/or preserve the intended tax treatment of the benefits provided with respect to the Award, or (b) comply with the requirements of Section 409A of the Code and related Department of Treasury guidance.

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PROXY

MAUI LAND & PINEAPPLE COMPANY, INC.

120 KANE STREET, P. O. BOX 187

KAHULUI, MAUI, HAWAII 96733-6687

THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS FOR THE ANNUAL MEETING TO BE HELD MAY 8, 2006

The undersigned hereby makes, constitutes and appoints DAVID C. COLE, FRED W. RICKERT and ADELE H. SUMIDA and each of them as attorneys and proxies of the undersigned, with full power of substitution, for and in the name of the undersigned to represent the undersigned at the Annual Meeting of Shareholders of Maui Land & Pineapple Company, Inc. (the Company ) to be held at 8:30 a.m. on Monday, May 8, 2006, at the Ritz Carlton, Kapalua, Salon 1, in Lahaina, Hawaii, and any postponements or adjournments thereof, and to vote all shares of the stock of the Company standing in the name of the undersigned with all the powers the undersigned would possess if personally present at such meeting. This Proxy may be revoked by the undersigned at any time. The undersigned directs that this Proxy be voted as follows:

1. To elect the nominees listed below as Class One Directors to serve for a three-year term or until their successors have been elected and qualified:

DAVID C. COLE WALTER A. DODS JR. FRED E. TROTTER III

____ FOR ____ WITHHOLD AUTHORITY FOR ALL

INSTRUCTION: To withhold authority to vote for any individual nominee, write that nominee s name in the space provided below:

______________________________________________________________________________

2. To ratify the selection of Deloitte & Touche LLP as the Independent Registered Public Accounting Firm of the Company for the fiscal year 2006.

____ FOR ____ AGAINST ____ ABSTAIN

3. To amend the Company s Articles of Association to authorize an additional 1,000,000 shares of Common Stock.

____ FOR ____ AGAINST ____ ABSTAIN

4) To approve the Maui Land & Pineapple Company, Inc. 2006 Equity and Incentive Award Plan. (The implementation of this Proposal No. 4 is also conditioned upon shareholder approval of Proposal No. 3.)

____ FOR ____ AGAINST ____ ABSTAIN

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THIS PROXY WILL BE VOTED AS DIRECTED. IF THE PROXY IS PROPERLY SIGNED AND RETURNED AND NO DIRECTIONS ARE GIVEN, THE VOTE WILL BE IN FAVOR OF ALL PROPOSALS ABOVE. DISCRETIONARY AUTHORITY IS HEREBY CONFERRED AS TO ALL OTHER MATTERS THAT MAY COME BEFORE THE MEETING.

The undersigned hereby acknowledges receipt of the Notice of Annual Meeting and accompanying Proxy Statement.

Date:____________, 2006

Please sign EXACTLY as name(s) appears at left:

If the proxy is signed by an attorney-in-fact, executor, administrator, trustee or guardian, give full title.

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Vote by Internet or Telephone or Mail

24 Hours a Day, 7 Days a Week

Internet and telephone voting is available through 11:59 PM Eastern Time the day prior to the annual meeting day.

Your Internet or telephone vote authorizes the named proxies to vote your shares in the same manner as if you marked, signed and returned your proxy card.

**Internet**

http://www.proxyvoting.com/xxx

Use the internet to vote your proxy. Have your proxy card in hand when you access the web site.

OR

**Telephone**

1-866-540-5760

Use any touch-tone telephone to vote your proxy. Have your proxy card in hand when you call.

OR

**Mail**

Mark, sign and date your proxy card and return it in the enclosed postage-paid envelope.

**If you vote your proxy by Internet or by telephone, you do NOT need to mail back your proxy card.**