

CTI INDUSTRIES CORP  
Form 10-K  
April 16, 2019

Table of Contents

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

---

**FORM 10-K**

**(Mark One)**

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

**For the fiscal year ended December 31, 2018**

**OR**

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

**Commission File Number**

**000-23115**

**CTI INDUSTRIES CORPORATION**

(Exact name of Registrant as specified in its charter)

Edgar Filing: CTI INDUSTRIES CORP - Form 10-K

Illinois 36-2848943  
(State or other jurisdiction of (I.R.S. Employer Identification Number)  
incorporation or organization)

22160 N. Pepper Road  
Lake Barrington, Illinois 60010  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (847) 382-1000

Securities Registered pursuant to sections 12(b) of the Act:

<u>Title of Each Class</u>	<u>Name of Each Exchange on Which Registered</u>
Common Stock, No Par	NASDAQ Capital Market

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      No

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

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

---

Table of Contents

Indicate by check mark whether the Registrant has submitted electronically 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 such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of 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.

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

Large accelerated filer      Accelerated filer      Non-accelerated filer      Smaller Reporting Company      Emerging Growth Company

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

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

Based upon the closing price of \$4.34 per share of the Registrant's Common Stock as reported on NASDAQ Capital Market tier of The NASDAQ Stock Market on June 30, 2018, the aggregate market value of the voting common stock held by non-affiliates of the Registrant was then approximately \$8,011,000. (The determination of stock ownership by non-affiliates was made solely for the purpose of responding to the requirements of the Form and the Registrant is not bound by this determination for any other purpose.)

The number of shares outstanding of the Registrant's Common Stock as of March 1, 2019 was 3,735,950 (excluding treasury shares).

DOCUMENTS INCORPORATED BY REFERENCE

Part of Form 10-K into Which  
Document Document Is Incorporated

---

Table of Contents

**TABLE OF CONTENTS**

**INDEX**

FORWARD LOOKING STATEMENTS

Part I

Item No. 1	<u>Description of Business</u>	1
Item No. 1B	<u>Unresolved Staff Comments</u>	15
Item No. 2	<u>Properties</u>	15
Item No. 3	<u>Legal Proceedings</u>	16

Part II

Item No. 5	<u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	17
Item No. 7	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	17
Item No. 7A	<u>Quantitative and Qualitative Disclosures Regarding Market Risk</u>	27
Item No. 8	<u>Financial Statements and Supplementary Data</u>	27
Item No. 9	<u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	28
Item No. 9A	<u>Controls and Procedures</u>	28
Item No. 9B	<u>Other Information</u>	29

Part III

Item No. 10	<u>Directors and Executive Officers of the Registrant</u>	29
Item No. 11	<u>Executive Compensation</u>	33
Item No. 12	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	36
Item No. 13	<u>Certain Relationships and Related Transactions</u>	38
Item No. 14	<u>Principal Accounting Fees and Services</u>	38

Part IV

Item No. 15	<u>Exhibits and Financial Statement Schedules</u>	39
-------------	---	----



Table of Contents

**FORWARD-LOOKING STATEMENTS**

This annual report includes both historical and “forward-looking statements” within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. We have based these forward-looking statements on our current expectations and projections about future results. Words such as “may,” “should,” “could,” “would,” “expect,” “plan,” “anticipate,” “believe,” “estimate,” “predict,” “potential,” “continue,” or similar words are intended to identify forward-looking statements, although not all forward-looking statements contain these words. Although we believe that our opinions and expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements, and our actual results may differ substantially from the views and expectations set forth in this annual report. We disclaim any intent or obligation to update any forward-looking statements after the date of this annual report to conform such statements to actual results or to changes in our opinions or expectations. These forward-looking statements are affected by factors, risks, uncertainties and assumptions that we make, including, without limitation, our participation in highly competitive markets, potential changes in the cost or availability of raw materials, our dependence on a limited number of suppliers, the possible inability to obtain an adequate supply of raw materials, our reliance on a limited number of key customers, the loss of one or more of our key customers, changing consumer demands, developments or changes in technology, risks of international operations and political environments, dependence on our intellectual property, compliance with federal, state or local regulations, the resolution of litigation or other legal proceedings to which we may become involved, restrictions included in the Company’s credit facility, the availability of funds under the Company’s credit facility, damage to or destruction of one or both of the Company’s principal plants, our ability to service our indebtedness, our ability to invest in needed plant or equipment.

**PART I**

**Item No. 1 – Description of Business**

**Business Overview**

We develop, produce and distribute a number of consumer products and sell these products throughout the United States and in over 30 other countries, and we produce film products for commercial and industrial uses in the United States. Many of our products utilize flexible films and, for a number of years, we have been a leading developer of innovative products which employ flexible films including novelty balloons, pouches and rolls of film for vacuum sealing and storage of products in the home as well as films for commercial packaging applications.

Our principal lines of products include:

**Novelty Products** consisting principally of foil and latex balloons and other inflatable toy items.

**Vacuum Sealing Containers and Sealing Devices** for home and consumer use to vacuum seal, store and preserve food and personal items.

**Flexible Films** for food and other commercial and packaging applications.

1

---



Table of Contents

In addition to these principal product lines, for the past several years, we have engaged in (i) the assembly and sale of Candy Blossoms (small gift bouquets of arranged candy items often including ribbons and/or a small foil balloon), (ii) the distribution in Mexico of party goods products, and (iii) the sale and distribution of home containers and organizing products (some of which we produce) to and through a related entity which distributes these products through a network of independent distributors.

We leverage our technology to design and develop proprietary products which we market and sell and which we develop for our customers. We have been engaged in the business of developing flexible film products for over 40 years and have acquired significant technology and know-how in that time. We currently hold several patents, related to flexible film products including specific films, zipper closures, valves and other features of these products.

We print, process and convert flexible film into finished products and we produce latex balloons and novelty items. Our principal production processes include:

Coating and laminating rolls of flexible film. Generally, we adhere polyethylene film to another film such as nylon or polyester.

Printing film and latex balloons. We print both plastic and latex films, with a variety of graphics, for use as packaging film or for balloons.

Converting printed film to balloons.

Converting film to flexible containers.

Producing latex balloons and other latex novelty items.

Assembling and inflating of novelty products and balloons and Candy Blossoms.

In 1978, we began manufacturing metalized balloons (often referred to as "foil" balloons), which are balloons made of a base material (usually nylon or polyester) often having vacuum deposited aluminum and polyethylene coatings. These balloons remain buoyant when filled with helium for much longer periods than latex balloons and permit the printing of graphic designs on the surface. In 1985, we began marketing latex balloons and, in 1988, we began manufacturing latex balloons. In 1999, we acquired an extrusion coating and laminating machine and began production of coated and laminated films, which we have produced since that time.

For more than 20 years, we have been engaged in the production of flexible containers for the storage of liquids, food products, household goods and other items, and in the coating, laminating and printing of flexible films for our novelty and container products and for the production of laminated and printed films we supply to others.

Table of Contents

We market and sell our foil and latex balloons and related novelty items throughout the United States, Canada and Mexico and in a number of other countries in Latin America and Europe. We supply directly to retail stores and chains and through distributors, who in turn sell to retail stores and chains. Our balloon and novelty products are sold to consumers through a wide variety of retail outlets including general merchandise, discount and drugstore chains, grocery chains, card and gift shops, and party goods stores, as well as through florists and balloon decorators.

Most of our foil balloons contain printed characters, designs and social expression messages, such as “Happy Birthday,” “Get Well” and similar items. For some of our balloon designs, we obtain licenses for well-known characters and print those characters and messages on our balloons.

We produce flexible containers and rolls of film for use as flexible containers in a variety of applications, including (i) zippered pouches with valves for vacuum sealing of food and household products and (ii) pouches and rolls of film for use with vacuum sealing machines to vacuum seal, store and protect food and household items. We market and sell flexible containers and rolls of film for consumer storage uses through retail chains and outlets throughout the United States, and we provide flexible containers to others for resale. We market and sell vacuum sealing machines for use with pouches and rolls of film for the vacuum storage of food and household products.

We provide customized laminated films and printed films to customers who utilize the film to produce bags or pouches for the packaging of food, liquids and other items. Commencing in 2014, we began assembling and producing Candy Blossoms - containers including candy items and, at times, air-inflated balloons. Since 2014, we have distributed home container and organizing products, some of which we produce, to and through a related entity which distributes those products through a network of independent distributors in the United States. During November 2018 we announced our intention to divest our interest in this business as not being strategic to the Company. In 2015, we commenced the distribution of party goods in Mexico.

In 2018, our revenues from our product lines, as a percent of total revenues were:

Novelty Products	61% of revenues
Vacuum Sealing Containers and Devices	16% of revenues
Flexible Film Products	4% of revenues
Other Products	19% of revenues

We are an Illinois corporation with our principal offices and plant at 22160 N. Pepper Road, Lake Barrington, Illinois.

**Business Strategies and Developments**

Our business strategies, and recent developments related to our business, include:

*Management.* During November 2018, our CEO, Mr. Stephen Merrick, retired from that role. Mr. Merrick continued as the Company's General Counsel and a member of the Board. Mr. Jeffrey Hyland, who joined CTI as President during 2017, became both CEO and President during November 2018.

3

---

Table of Contents

*Financing.* During December 2017, we secured new financing from PNC Bank, National Association, and immediately repaid all tranches of our prior credit facility including senior debt, term debt, and mezzanine debt. During 2018 we failed to comply with our financing requirements twice, during the first quarter and then again during November. Subsequent to December 31, 2018, during March 2019, we and our bank entered into a Forbearance Agreement. While this Forbearance Agreement addressed the immediate issues, it is a short-term solution. Until a long-term resolution is secured, we will treat all of our related debt as current and update comments related to liquidity and going concern.

*Strategy.* Our management determined to focus on achieving growth and profitability within the current scope of our core product lines – foil balloons, latex balloons, vacuum sealing products and systems and film products for commercial and packaging applications. We reviewed our operations and, during 2018, eliminated approximately \$3 million in operating costs on an annualized basis. We have identified substantial additional costs that can be eliminated during 2019 and 2020, and are taking action in those areas. We are also aggressively pursuing additional revenues in our core product lines both from existing and new customers in North America and Europe.

*Focus on our Core Assets and Expertise.* We have been engaged in the development, production and sale of film and container products for 40 years and have developed assets, technology and expertise which, we believe, enable us to develop, manufacture, purchase, market and sell innovative products of high quality within our areas of knowledge and expertise. We plan to focus our efforts on these core assets and areas of expertise – film novelty products, consumer vacuum storage systems, specialty film products, container products, laminated films and printed films – to develop new products, to market and sell our products and to build our revenues. It is in part for this reason that during November 2018 we announced our intention to divest our interest in Clever Container, an entity that sells organization products to consumers.

*Develop New Products, Product Improvements and Technologies.* We engage in research, design, innovation and development for the purpose of developing, and improving, products, materials, methods and technologies within our core product categories. We work to develop and identify new products, to improve existing products and to develop new technologies within our core product areas in order to enhance our competitive position and increase our sales. We seek to leverage our technology to develop innovative and proprietary products. In our novelty product lines, our development work includes new designs, new character licenses, new product developments, new materials and improved production methods. In our consumer storage product lines, we have developed new pouch closure systems and valves and new film methods for packaging applications. We have received several patents for these developments. We developed and introduced a line of resealable pouches with a valve and pump system for household storage and vacuum sealing of food items. We designed and introduced a line of vacuum sealing equipment for the vacuum sealing of pouches for food and household items and are engaged in development efforts to create new and enhanced vacuum sealing machines, accessories and related products. We work with customers to develop custom film products which serve the unique needs or requirements of the customer.

Table of Contents

*Develop New Channels of Distribution and New Sales Relationships.* We seek to organically develop new channels of distribution and new sales relationships, both for existing and new products. Over the past several years, we have developed new distributors and customers for our pouch and novelty products, in the United States and in Europe, Mexico, Latin America and Australia, expanding the scope and level of our international sales and activities. In 2013, we introduced a line of vacuum sealing systems for the storage and preservation of food and other items in the home under the Ziploc® Brand Vacuum Sealer System. We market and sell the vacuum sealing machines, pouches and rolls of film under the brand throughout the United States, Canada and Mexico. During recent years, we developed a relationship with a related company engaged in the sale of home containers and organization products and have become a supplier of products, some of which we produce, to that company. During 2015, we became a distributor in Mexico for a major party goods company.

*Enhance Our Productive Capacity.* We invest in new plant and equipment when appropriate to expand the range and volume of products we produce. During 2008 and 2009, we acquired, installed and commenced operation of equipment which enabled us to produce the pouches and rolls of film for our vacuum sealing storage business we developed. During 2010 and 2011, we designed, assembled and installed latex balloon production equipment which significantly enhanced our production capacity for latex balloons to support our growing sales of this product line. We significantly expanded our warehouse, packaging and fulfillment facilities and operations during 2013. During the first quarter of 2014, we acquired printing equipment which almost doubled printing capacity to support our growing sales of foil balloons. We acquired and installed a new latex balloon production machine in Mexico which became operational in August 2016; this machine has enhanced our latex balloon production capacity by approximately 30%. At the end of 2017 we initiated a repair and maintenance, and quality improvement, program. This program included the addition of two automated balloon converting machines during 2018 which enhanced our foil balloon capacity by 35% and supported our quality program.

*Product and Line Extensions.* Upon achieving our initial strategic goals, during 2019, we intend to pursue new product lines and product line extensions, through internal developments, purchase and acquisitions. We believe that the acquisition and integration of targeted opportunities could benefit our Company in a meaningful way.

## Table of Contents

### **Products**

*Foil Balloons.* We have designed, produced and sold foil balloons since 1979 and, we believe, are the second largest manufacturer of foil balloons in the United States. Currently, we produce several hundred foil balloon designs, in different shapes and sizes.

In addition to size and shape, a principal element of the Company's foil balloon products is the printed design or message contained on the balloon. These designs include figures and licensed characters many of which are well known. We recognize that consumer trends and preferences, and competing products, are constantly changing. In order to compete effectively in this product line we must constantly innovate and develop new designs, shapes and products.

*Latex Balloons.* Through our subsidiary in Guadalajara, Mexico, Flexo Universal, S. de R.L. de C.V. ("Flexo Universal"), we manufacture latex balloons in a wide variety of sizes and colors. Many of these balloons are marketed under the name Partyloons® and balloons are also marketed on a private label basis. We also manufacture toy balloon products including punch balls, water bombs and "Animal Twisties."

*Vacuum Sealing Pouches and Systems.* We produce, market and sell consumer vacuum storage pouches and systems for the vacuum storage of food and other household items. We produce (i) vacuum sealable bags and rolls of film for use with vacuum sealing devices for household storage and (ii) valved, resealable bags also for vacuum storage uses. Our valved, resealable bags function with a small hand or battery-powered pump to evacuate air from the bag when it is sealed. Since 2012, we have produced and marketed vacuum sealable bags and rolls of film under the Ziploc® brand. We also market vacuum sealing machines, produced for us, under the Ziploc® Brand Vacuum Sealer System. We have produced and marketed a line of valved, resealable bags under our Zipvac™ line and a line of valved, resealable bags under another brand.

*Packaging Films and Custom Film Products.* A large and increasing number of both consumer and commercial products are packaged in pouches or containers utilizing flexible films. Often such containers include printed labels and designs. We produce and sell films that may be utilized for the packaging of a wide variety of products and liquids. We laminate, extrusion coat and adhesive coat flexible films for these purposes and we provide flexographic printing for the films we produce. We can produce a variety of customized film products, and printing services, to meet the specific packaging needs of a wide variety of customers.

*Other Products.* Clever Container Company, an entity consolidated with our company as a variable interest entity, distributes home organization and container products to consumers. During November 2018 we announced our intention to divest our interest in Clever Container. Until December 2018, Clever Container engaged in the direct sale

of such products through a network of independent distributors. During December 2018, Clever Container changed its model to that of on-line sales only. During February 2019, we reached agreement in principle with two of our principal stockholders to exchange our equity interest in Clever Container for most of the equity ownership in CTI Europe GmbH, our Germany subsidiary, that we did not already own. In 2014, we began assembly and sale of our Candy Blossom product line. In 2015, we began to distribute party goods in Mexico.



Table of Contents

**Markets**

*Foil Balloons*

The foil balloon came into existence in the late 1970s. During the 1980s, the market for foil balloons grew rapidly. Initially, the product was sold principally to individual vendors, small retail outlets and at fairs, amusement parks, shopping centers and other outdoor facilities and functions. Foil balloons remain buoyant when filled with helium for extended periods of time and they permit the printing and display of graphics and messages. As a result, the product has significant appeal as a novelty and message item. Foil balloons became part of the "social expression" industry, carrying graphics designs, characters and messages like greeting cards. In the mid-1980s, we and other participants in the market began licensing character and cartoon images for printing on the balloons and directed marketing of the balloons to retail outlets including grocery, general merchandise, discount and drug store chains, card and gift shops, party goods stores as well as florists and balloon decorators. These outlets now represent the principal means for the sale of foil balloons throughout the United States and in a number of other countries, although individual vendors remain a means of distribution in a number of areas.

Foil balloons are now sold in virtually every region of the world. The United States, however, remains the largest market for these products.

Foil balloons are sold in the United States and foreign countries directly by producers to retail outlets and through distributors and wholesalers. Often the sale of foil balloons by the wholesalers/distributors is accompanied by related products including latex balloons, floral supplies, candy containers, mugs, plush toys, baskets and a variety of party goods.

*Latex Balloons*

For a number of years, latex balloons and related novelty/toy latex items have been marketed and sold throughout the United States and in many other countries. Latex balloons are sold as novelty/toy items, for decorative purposes, as part of floral designs and as party goods and favors. In addition to standard size and shape balloons, inflatable latex items include punch balls, water bombs, balloons to be twisted into shapes, and other specialty designs. Often, latex balloons include printed messages or designs.

Latex balloons are sold principally in retail outlets, including party goods stores, general merchandise stores, discount chains, gift stores and drugstore chains. Latex balloons are also purchased by balloon decorators and floral outlets for

use in decorative or floral designs. Printed latex balloons are sold both in retail outlets and for balloon decoration purposes including floral designs.

Latex balloons are sold both through distributors and directly to retail outlets by the producers.

7

---

## Table of Contents

### *Flexible Containers/Pouches*

The market for flexible containers and pouches is large and diverse. Many companies engaged in the production of food items package their products in flexible containers or pouches, and, therefore, represent a market for these containers.

Flexible containers and pouches are sold and utilized in the consumer market in numerous forms. They include simple open-top plastic bags, resealable bags and zippered bags. The market also includes containers and pouches of special design or purpose, including vacuumable bags for storage of food or household items or commercial uses.

We participate in a segment of the market for vacuum sealing and storage of food and household items. These products generally are sold in retail chain stores, and to some degree, in grocery stores, and, recently, in a direct sales channel. The product lines sold include (i) zippered, resealable bags, incorporating a valve through which air can be evacuated by a hand pump or other device; (ii) pouches or rolls of film which can be sealed by vacuum sealing devices and (iii) vacuum sealing devices.

### *Printed and Specialty Films*

The industry and market for printed and specialty films are fragmented and include many participants. There are hundreds of manufacturers of printed and specialty film products in the United States and in other markets. In many cases, companies who provide food and other products in film packages also produce or process the films used for their packages. The market for the Company's film products consists principally of companies who utilize the films for the packaging of their products, including food products and other items, usually by converting the film to a flexible container.

## **Marketing, Sales and Distribution**

### *Balloon Products*

We work in collaboration with our customers on designs, promotions, and other elements of marketing and selling. Our customers are typically retailers who sell our products to ultimate customers. These relationships generally can be terminated unilaterally by our customers. We must maintain good relationships with our customers if this sales model

is to be successful.

We market and sell our foil balloon, latex balloon and related novelty products throughout the United States and in a number of other countries. We maintain marketing, sales and support staff and a customer service department in the United States. Sales in the United Kingdom are conducted by CTI Balloons Ltd. (“CTI Balloons”), the Company's subsidiary located in Rugby, England. Sales in Europe are conducted by CTI Europe GmbH (“CTI Europe”), the Company’s subsidiary located in Heusenstamm, Germany. CTI Europe manages the operations of CTI Balloons. Flexo Universal, our subsidiary in Mexico, conducts sales and marketing activities for the sale of balloon products in Mexico, Latin America, and certain other markets. Sales in other foreign countries are made generally to distributors in those countries and are managed at the Company's principal offices.

8

---

## Table of Contents

We sell and distribute our balloon products (i) by our employed staff of sales and customer service personnel in the United States, Mexico, the UK and Germany, (ii) through a network of distributors and wholesalers in the United States, Mexico, the UK and Europe, (iii) through several groups of independent sales representatives, and (iv) to retail chains. Our balloon products are generally sold through retail outlets including grocery, general merchandise and drug store chains, card and gift shops, party goods stores as well as florists and balloon decorators.

We engage in a variety of advertising and promotional activities to promote the sale of our balloon products. We produce a complete catalog of our balloon products, and also prepare various flyers and brochures for special or seasonal products, which we disseminate to thousands of customers, potential customers and others. We participate in several trade shows for the gift, novelty, balloon and other industries and advertise in several trade and other publications. We maintain websites which show images of our products.

### *Flexible Containers/Pouches*

We market several lines of flexible containers or pouches for household use to vacuum seal, store and preserve food and other household items.

We developed and, for several years, we have produced and sold a line of pouches and rolls of film for use with vacuum sealing machines to vacuum seal food and household items. Initially, we marketed these products through various retail channels under our brand or on a private label basis. On December 14, 2011, the Company entered into a Trademark License Agreement with SC Johnson under which the Company is licensed to manufacture and sell a line of vacuum sealing machines and pouches under the Ziploc® Brand Vacuum Sealer System. The agreement was initially for a three year term expiring on December 31, 2014 and was extended to December 31, 2017 and then to December 31, 2019. The licensed product line includes vacuum sealing machines manufactured for the Company and pouches and rolls manufactured by the Company for use in the home to vacuum seal food items to preserve freshness and help prevent freezer burn.

During 2007, we introduced a line of re-sealable pouches incorporating a valve permitting the evacuation of air from the sealed pouch by use of a hand pump supplied with the pouches. This line of products has been marketed under the brand name ZipVac®.

### *Printed and Specialty Films*

We market and sell printed and laminated films directly and through independent sales representatives throughout the United States. We sell laminated and printed films to companies that utilize these films to produce packaging for a variety of products, including food products, in both solid and liquid form, such as cola syrup, coffee, juices and other items. We seek to identify and maintain customer relationships in which we provide added value in the form of technology or systems.

Table of Contents

*Other Products*

Other products are sold through both our internal sales force directly to customers and through independent sales representatives. These products are generally sold directly to consumers or to retail outlets.

**Production and Operations**

We conduct our operations at our facilities including: (i) our 68,000 square foot facility in Lake Barrington, Illinois, incorporating our headquarters office, production and warehouse space, (ii) our 118,000 square foot facility in Lake Zurich, Illinois consisting of warehouse, packaging and office space (iii) a 73,000 square foot facility in Guadalajara, Mexico, consisting of office, warehouse and production space, (iv) a 9,000 square foot facility in Rugby, England consisting of office and warehouse/assembly space, and (v) a 13,000 square foot facility in Heusenstamm, Germany (near Frankfurt), consisting of office and warehouse/assembly space.

Our production operations include (i) lamination and extrusion coating of films, (ii) slitting of film rolls, (iii) printing on film and on latex balloons, (iv) converting film to completed products including balloons, flexible containers and pouches, (v) producing latex balloon products, (vi) inflating of air-filled balloons, and (vii) assembling Candy blossoms. We perform all of the lamination, extrusion coating and slitting activities in our Lake Barrington, Illinois plant and produce all of our latex balloon products at our Guadalajara, Mexico plant. We print on films in Lake Barrington, Illinois and we print on latex balloons in Guadalajara, Mexico. We complete air-filling and assembly of balloons in all our facilities except Lake Barrington, Illinois. We assemble Candy blossoms in our Lake Zurich, Illinois facility.

We warehouse raw materials at our plants in Lake Barrington, Illinois and Guadalajara, Mexico and we warehouse finished goods at our facilities in Lake Barrington, Illinois; Lake Zurich, Illinois; Guadalajara, Mexico; Rugby, England and Heusenstamm, Germany. We maintain customer service and fulfillment operations at each of our warehouse locations. We conduct sales operations for the United States and for all other markets, except those handled by our Mexico, Germany and England facilities, at the Lake Barrington, Illinois facility. Sales for Mexico and Latin America are handled at our Guadalajara, Mexico facility; sales for the United Kingdom are handled at our Rugby, England facility; sales for Europe are conducted from our facilities in Heusenstamm, Germany. In addition to warehouse and sales activities at these locations, we engage in some assembly, balloon inflation and related activities.

We maintain a graphic arts and development department at our Lake Barrington, Illinois facility which designs our balloon products and graphics. Our creative department operates a networked, computerized graphic arts system for the production of these designs and of printed materials including catalogues, advertisements and other promotional materials. As many of our products are custom designed or created to fulfill promotional schedules, we sometimes

have excess inventory that must be sold at a discount or disposed of. Any such disposition will typically negatively impact our profit margin.



## Table of Contents

We conduct administrative and accounting functions at our headquarters in Lake Barrington, Illinois and at our facilities in Guadalajara, Mexico, Rugby, England and Heusenstamm, Germany.

### **Raw Materials**

The principal raw materials we use in manufacturing our products are (i) petroleum or natural gas-based films, (ii) petroleum or natural gas-based resin, (iii) latex, and (iv) printing inks. The cost of raw materials represents a significant portion of the total cost of our products, with the result that fluctuations in the cost of raw materials have a material effect on our profitability. During the past several years, we have experienced significant fluctuations in the cost of these raw materials. We do not have any long-term agreements for the supply of raw materials and may experience wide fluctuations in the cost of raw materials in the future. Further, although we have been able to obtain adequate supplies of raw materials in the past, there can be no assurance that we will be able to obtain adequate supplies of one or more of our raw materials in the future.

Many of the foil balloons we produce and sell are intended to be filled with helium in order to be buoyant. Over the past several years, the price of helium has fluctuated substantially and the availability of helium has, on occasion, been limited. During 2018, the availability of helium declined and the cost of helium increased. We don't know when to expect that situation to reverse. Limited availability and/or an increase in the cost of helium could adversely affect our sales of foil balloons in the future.

### **Competition**

The balloon and novelty industry is highly competitive, with numerous competitors. We believe there are presently five principal manufacturers of foil balloons whose products are sold in the United States including Anagram International, Inc., Pioneer Balloon Company, Convertidora International S.A. de C.V., and Betallic, LLC. Several companies market and sell foil balloons designed by them and manufactured by others for them. In addition, there are several additional foil balloon manufacturers in Europe and China who participate in our markets.

We compete for the sale of latex balloons in the United States, Canada, Mexico, Latin America, the United Kingdom, Australia and Europe. There are a number of other companies situated in the United States, Mexico, Asia, South America and Europe who manufacture latex balloons and with whom we compete in the markets in which we participate. The markets are highly competitive with respect to price, quality and terms.

Our company competes principally in the United States and Canada for the sale of vacuum sealing products. There are several companies who compete in those markets.

## Table of Contents

The market for films, packaging, flexible containers and custom products is fragmented, and competition in this area is difficult to gauge. However, there are numerous participants in this market and the Company can expect to experience intense quality and price competition.

Many of the companies in these markets offer products and services that are the same or similar to those offered by us and our ability to compete depends on many factors within and outside our control. There are a number of well-established competitors in each of our product lines, several of which possess substantially greater financial, marketing and technical resources and have established extensive, direct and indirect channels of distribution for their products and services. As a result, such competitors may be able to respond more quickly to new developments and changes in customer requirements, or devote greater resources to the development, promotion and sale of their products and services than we can. Competitive pressures include, among other things, price competition, new designs and product development and copyright licensing.

### **Patents, Trademarks and Copyrights**

We have developed or acquired a number of intellectual property rights which we believe are significant to our business. As of December 31, 2018, we held 8 issued patents in the United States and 3 issued patents in foreign countries. These patents are scheduled to expire at various times during the 2020s. While these intellectual property rights are helpful, their degree of protection is uncertain. Competitors may violate our intellectual property rights, forcing us to decide whether to challenge them. Such rights may or may not withstand challenge. Conversely, entities may charge us with violating their intellectual property rights. Failure to protect our rights, or conflict with the rights of one or more other entities, may negatively impact our financial and competitive position.

*Proprietary Designs and Copyright Licenses.* We design the shapes and graphic designs of most of our foil balloon products. We also maintain licenses on certain characters and designs for our balloon products.

*Trademarks.* We own five registered trademarks in the United States relating to our balloon products. Some of these trademarks are registered in foreign countries, principally in the European Union.

*Patent Rights.* We own, or have license rights under, or have applied for, patents related to our balloon products, certain film products and certain flexible container products. These include (i) several foil balloon design patents, (ii) patents and applications related to the design and structure of, and method of, inserting and affixing, zipper-closure systems in a bag, (iii) patents related to one-way valves for pouches, (iv) a patent related to methods of embossing film and utilizing such film to produce pouches with fitments, and (v) a patent related to vacuumable storage bags with fitments.



## Table of Contents

### **Research and Development**

We maintain a product development and research group for the development or identification of new products, product designs, product components and sources of supply. Research and development includes (i) creative product development and design, (ii) creative marketing, and (iii) engineering development. During each of the fiscal years ended December 31, 2018 and 2017, we estimate that the total amount spent on research and development activities was approximately \$375,000 and \$344,000, respectively.

### **Employees**

As of December 31, 2018, the Company had 99 full-time employees in the United States, of whom 18 are executive or supervisory, 3 are in sales, 59 are in manufacturing or warehouse functions and 19 are clerical. As of that same date, we had 16 full-time employees in England, of whom 3 are in sales, 9 are in warehousing and 4 clerical. At Flexo Universal, our Mexico subsidiary, as of December 31, 2018, we had 336 full-time employees, of whom 8 are executive or supervisory, 13 are in the warehouse, 6 are in sales, 297 are in manufacturing and 12 are clerical. As of December 31, 2018, the Company had 6 full-time employees in Germany, of whom two are executive or supervisory, 1 is in warehousing and 3 are clerical. The Company is not a party to any collective bargaining agreement in the United States, has not experienced any work stoppages, and believes that its relationship with its employees is satisfactory.

Beginning November 2018, the Company experienced severe difficulty in securing adequate seasonal workers in its US operations, forcing it to pay substantially higher costs in the form of overtime and a holiday premium. The Company expects its local labor market in the US (near Chicago) to continue to become more costly over time, which, if not changed, would negatively impact its future profitability.

### **Regulatory Matters**

Our manufacturing operations in the United States are subject to the U.S. Occupational Safety and Health Act ("OSHA"). We believe we are in material compliance with OSHA. The Company generates liquid, gaseous and solid waste materials in its operations in Lake Barrington, Illinois and the generation, emission or disposal of such waste materials are, or may be, subject to various federal, state and local laws and regulations regarding the generation, emission or disposal of waste materials. We believe we are in material compliance with applicable environmental rules and regulations. Several states have enacted laws limiting or restricting the release of helium filled foil balloons. We do not believe such legislation will have any material effect on our operations.

In August 2012, the U.S. Securities and Exchange Commission (SEC) issued a rule under Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act requiring companies to publicly disclose their use of conflict minerals that originated in the Democratic Republic of the Congo (DRC) or an adjoining country. Under the rule, issuers are required to conduct a reasonable country of origin inquiry and, if necessary, exercise due diligence process to ascertain the source of conflict minerals, defined as tantalum, tin, gold or tungsten, which are necessary to the functionality or production of their manufactured or contracted to be manufactured products. Companies are required to provide this disclosure on Form SD.

Table of Contents

An increasing number of regulations and actions relate to the integrity and security of individually identifiable data. Additionally, we require the effective use of data in running our business. While we are not aware of losses in the past, access of such data by unauthorized persons may expose us to costs, fines, penalties, and loss of customer confidence.

**International Operations**

We conduct operations in three locations outside of the United States:

Flexo Universal, a 99%-owned subsidiary in Guadalajara, Mexico. Flexo Universal maintains a plant, offices and warehouse in Guadalajara, Mexico where we produce latex and foil balloons and print latex balloons. Flexo Universal conducts sales, warehousing and fulfillment operations, servicing principally the Company and other customers in the United States, our subsidiaries in the United Kingdom and Europe, customers in Mexico and Latin America and certain customers in Europe.

CTI Balloons, a wholly-owned subsidiary located in Rugby, England. CTI Balloons maintains offices and a warehouse in Rugby, conducts certain packaging and inflation activities there and conducts sales, warehousing and fulfillment activities for customers principally in the United Kingdom.

CTI Europe, a majority-owned subsidiary located in Heusenstamm, Germany. CTI Europe maintains offices and a warehouse in Heusenstamm, Germany (near Frankfurt), conducts certain packaging and inflation activities there and conducts sales, warehousing and fulfillment activities for customers principally in Europe.

We rely, and are dependent, on our operations in Mexico for the supply of latex balloons in the United States, Mexico, Europe and other markets. Interruption of that supply would have a materially adverse effect on the business of the Company.

Table of Contents

Our domestic and international sales to outside customers and assets by area over the period 2017-2018 have been as follows:

	<b>United States</b>	<b>United Kingdom (UK)</b>	<b>Europe (Excluding UK)</b>	<b>Mexico</b>	<b>Consolidated</b>
Year ended 12/31/18					
Sales to outside customers	\$40,554,000	\$1,438,000	\$4,731,000	\$8,868,000	\$55,591,000
Total Assets	\$25,355,000	\$879,000	\$3,052,000	\$9,476,000	\$38,761,000

	<b>United States</b>	<b>United Kingdom (UK)</b>	<b>Europe (Excluding UK)</b>	<b>Mexico</b>	<b>Consolidated</b>
Year ended 12/31/17					
Sales to outside customers	\$41,165,000	\$1,908,000	\$4,142,000	\$9,022,000	\$56,237,000
Total Assets	\$27,784,000	\$923,000	\$2,989,000	\$8,288,000	\$39,984,000

**Available Information**

We maintain our corporate website at [www.ctiindustries.com](http://www.ctiindustries.com) and we make available, free of charge, through this website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports that we file with, or furnish to, the Securities and Exchange Commission (“SEC”), as soon as reasonably practicable after we electronically file that material with, or furnish it to, the SEC. You may also read and copy material filed by us with the SEC at the SEC’s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549, and you may obtain information on the operation of the Public Reference Room by calling the SEC in the U.S. at 1-800-SEC-0330. In addition, the SEC maintains an Internet website, [www.sec.gov](http://www.sec.gov), which contains reports, proxy and information statements and other information that we file electronically with the SEC. Our website also includes corporate governance information, including our Code of Ethics and our Board Committee Charters. The information contained on our website does not constitute a part of this report.

**Item No. 1B – Unresolved Staff Comments**

As of the filing of this Annual report on Form 10-K, we had no unresolved comments from the staff of the Securities and Exchange Commission.



**Item No. 2 – Properties**

We own our principal plant and offices located in Lake Barrington, Illinois, approximately 45 miles northwest of Chicago, Illinois. The facility includes approximately 68,000 square feet of office, manufacturing and warehouse space.

Table of Contents

In September 2012, we entered into a lease agreement, expiring on February 28, 2017 to rent approximately 118,000 square feet of warehouse and office space in Lake Zurich, Illinois. Effective March 1, 2017, this lease was renewed for three years, at a remaining basic rental cost per month of:

<u>Lease period</u>	Amount per month
March 1, 2018 – February 28, 2019	\$40,000
March 1, 2019 – February 29, 2020	\$42,000

In August 2015, CTI Balloons, entered into a 10-year lease agreement (which can be terminated early after 5 years) for approximately 9,000 square feet of office and warehouse space in Rugby, England at a cost of \$6,000 per month. This facility is utilized to warehouse balloon products and to manage and service the Company's operations in England.

In August 2011, Flexo Universal entered into a 5-year lease agreement, expiring July 31, 2016, for the lease of approximately 73,000 square feet of manufacturing, warehouse and office space in Guadalajara, Mexico at a cost of \$22,000 per month. The lease was extended to February 28, 2017. Effective March 1, 2017, Flexo Universal entered into a five-year lease for these premises at a cost of 493,090 Mexican Pesos per month (approximately \$26,000 per month).

On November 22, 2016, CTI Europe entered into a lease agreement for 13,000 square feet of office and warehouse space in Heusenstamm, Germany for a term commencing on February 1, 2017 and ending on February 1, 2022, at a rate per month of \$9,000.

We believe that our properties have been adequately maintained, are in generally good condition and are suitable for our business as presently conducted. We believe our existing facilities provide sufficient production capacity for our present needs and for our presently anticipated needs in the foreseeable future. We also believe that, with respect to leased properties, upon the expiration of our current leases, we will be able to either secure renewal terms or to enter into leases for alternative locations at market terms.

**Item No. 3 – Legal Proceedings**

The Company may be party to certain lawsuits or claims arising in the normal course of business. The ultimate outcome of these matters is unknown but, in the opinion of management, we do not believe any of these proceedings will have, individually or in the aggregate, a material adverse effect upon our financial condition, cash flows or future results of operation.

In July, 2017, God's Little Gift, Inc. (d\b\la) Helium and Balloons Across America and Gary Page ("Claimants") filed an action against the Company based on disputed compensation amounts over several years. This action was resolved by mutual agreement between the parties during January 2019. Mr. Page received 20,000 shares of CTI common stock, \$5,000 in cash, and a minimum payout in his monthly royalty calculation of \$7,667 beginning March 1, 2019 and ending August 1, 2021.

Table of Contents

**PART II**

**Item No. 5 – Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

**Market Information**

The Company's Common Stock was admitted to trading on the NASDAQ SmallCap Market (now the NASDAQ Capital Market) under the symbol CTIB on November 5, 1997.

The high and low sales prices for the last eight fiscal quarters according to the NASDAQ Stock Market's Stock Price History Report were:

	<b>High</b>	<b>Low</b>
January 1, 2017 to March 30, 2017	6.83	5.55
April 1, 2017 to June 30, 2017	6.20	5.55
July 1, 2017 to September 30, 2017	6.00	3.83
October 1, 2017 to December 31, 2017	4.50	3.25
January 1, 2018 to March 30, 2018	5.09	3.95
April 1, 2018 to June 30, 2018	4.95	3.56
July 1, 2018 to September 30, 2018	4.42	2.93
October 1, 2018 to December 31, 2018	4.31	2.75

As of December 31, 2018 there were approximately 42 holders of record of the Company's Common Stock. The Company's total number of beneficial owners of common stock of the Company was approximately 442.

The Company did not pay any cash dividends on its Common Stock during 2018 or 2017. Under the terms of the Company's current loan agreements, the amount of dividends the Company may pay is limited by the terms of the financial covenants.

**Item No. 7 – Management's Discussion and Analysis of Financial Condition and Results of Operations**

## Overview

The Company produces film products for novelty, packaging container and custom film product applications. These products include foil balloons, latex balloons and related latex toy products, films for packaging applications, flexible containers for packaging and storage applications and custom film products. We produce all of our film products for packaging and container applications at our facilities in Lake Barrington, Illinois. We produce all of our latex balloons and latex products at our facility in Guadalajara, Mexico. Substantially all of our film products for packaging applications and flexible containers for packaging and storage are sold to customers in the United States. We market and sell our novelty items – principally foil balloons and latex balloons – in the United States, Mexico, the United Kingdom and a number of additional countries. In addition, the Company assembles and sells Candy Blossoms (containers of arranged candy items) in the United States, distributes party goods in Mexico and provides home organization and container products to an affiliated company who markets and sells these products in the United States to a network of independent distributors. These additional products, and certain accessory products sold by the Company, are recorded as “Other Products” in the following product category table.

Table of Contents

Our revenues from each of our product categories in each of the past two years have been as follows:

Product Category	(000 Omitted)					
	\$	% of	\$	% of		
	2018	Net Sales	2017	Net Sales		
Foil Balloons	24,962	45 %	29,103	52 %		
Latex Balloons	8,793	16 %	9,400	17 %		
Vacuum Sealing Products	8,820	16 %	7,866	14 %		
Film Products	2,006	4 %	2,602	4 %		
Other Products	11,010	19 %	7,266	13 %		
<b>Total</b>	<b>55,591</b>	<b>100.0 %</b>	<b>56,237</b>	<b>100.0 %</b>		

Our primary expenses include the cost of products sold and selling, general and administrative expenses.

Cost of products sold primarily consists of expenses related to raw materials, labor, quality control and overhead expenses such as supervisory labor, depreciation, utilities expense and facilities expense directly associated with production of our products, warehousing and fulfillment expenses and shipping costs relating to the shipment of products to customers. Cost of products sold is impacted by the cost of the raw materials used in our products, the cost of shipping, along with our efficiency in managing the production of our products.

Selling, general and administrative expenses include the compensation and benefits paid to our employees, all other selling expenses, marketing, promotional expenses, travel and other corporate administrative expenses. These other corporate administrative expenses include professional fees, depreciation of equipment and facilities utilized in administration, occupancy costs, communication costs and other similar operating expenses. Selling, general and administrative expenses can be affected by a number of factors, including staffing levels and the cost of providing competitive salaries and benefits, the cost of regulatory compliance and other administrative costs.

Purchases by a limited number of customers represent a significant portion of our total revenues. During 2018 and 2017, respectively, sales to our top 10 customers represented 69% and 65% of net revenues. During 2018 and 2017, there were two customers to whom our sales represented more than 10% of net revenues.



Table of Contents

Our principal customer sales for 2018 and 2017 were:

Customer	Product	2018 Sales	% of 2018		2017 Sales	% of 2017	
			Revenues			Revenues	
Wal-Mart	Vacuum Sealing Products; Balloons; Candy Blossoms	\$13,610,000	24.5	%	\$9,524,000	16.9	%
Dollar Tree Stores	Balloons	\$13,772,000	24.8	%	\$15,481,000	27.5	%

The loss of one or both of these principal customers, or a significant reduction in purchases by one or both of them, could have a material adverse effect on our business.

We generally do not have agreements with our customers under which customers are obligated to purchase any specific or minimum amount of product from us.

**Year Ended December 31, 2018 Compared to Year Ended December 31, 2017**Net Sales

For the fiscal year ended December 31, 2018, consolidated net sales from the sale of all products were \$55,591,000 compared to consolidated net sales of \$56,237,000 for the year ended December 31, 2017, a decrease of 1%.

Sales of foil balloons were \$24,962,000 in 2018 and \$29,103,000 in 2017, a decrease of 14%. Our largest customer for foil balloons was Dollar Tree Stores. The remaining sales were made to hundreds of customers including distributors and retail stores or chains in the United States, Canada, Mexico, the United Kingdom, Europe and Latin America.

Sales of latex balloons were \$8,793,000 in 2018 and \$9,400,000 in 2017, a decrease of 6%.



Sales of vacuum sealing products including pouch and related products and vacuum sealing machines were \$8,820,000 in 2018 and \$7,866,000 in 2017, an increase of 12%. Our sales of vacuum sealing systems during 2018 and 2017 have been made principally to four retail chains in the United States. During the fourth quarter of 2018 we launched a new, smaller format machine to complement our existing line.

Sales of film products were \$2,006,000 in 2018 and \$2,602,000 in 2017, a decrease of 23%. Approximately 87% of these sales were to Rapak, L.L.C. but includes sales to six other customers.

Sales of other products increased to \$11,010,000 in 2018 from \$7,266,000 in 2017, an increase of 34%. This category includes (i) sales of helium and accessory items for our balloon products, (ii) sales of Candy Blossoms, (iii) sales by Clever Container Company, which engaged in the direct sale of container and organizing products through a network of independent distributors until December 2018, and directly online thereafter and (iv) sales of party goods in Mexico by Flexo Universal.

## Table of Contents

### Cost of Sales

Cost of sales increased to \$44,162,000 in 2018 from \$42,482,000 in 2017. The increase in labor cost, particularly during November and December 2018, was a primary reason for this increase. Additionally, the reduction in sales volume negatively impacted our ability to absorb fixed/overhead costs, and a product quality initiative during 2018 resulted in additional expenses during that process.

### General and Administrative Expenses

General and administrative expenses decreased to \$7,149,000 in 2018 from \$7,657,000 in 2017. Many of the cost reductions realized during 2018 were in the administrative and marketing areas, from personnel costs to consulting to outside services.

### Selling and Marketing

Selling expenses increased to \$3,665,000 in 2018 from \$3,638,000 in 2017. Marketing and advertising expenses decreased to \$1,253,000 in 2018, from \$1,971,000 in 2017. The primary savings was the net reduction of outside consulting services in this area.

### Other Income or Expense

During 2018, we incurred net interest expense of \$2,106,000 compared to net interest expense of \$1,576,000 during 2017. Total borrowings were higher during 2018, and interest rates in the United States increased during 2018, which impacted the Company's floating rate facilities. Additionally, penalty interest related to our first financial covenant violation increased our interest rate by 2%.

During 2018, we realized a foreign currency gain in the amount of \$47,000 compared to foreign currency loss in 2017 of \$145,000.

### Income Taxes

In 2018, the Company income tax expense, on a consolidated basis, totaled \$937,000, compared to \$712,000 in 2017. Due to changes in U.S. tax law, we recorded a valuation reserve during 2017 of \$0.6 million related to foreign tax credits that may no longer be useable in the future as a result of this legislation. Because we are not in compliance with the terms of our credit facility, operate under a forbearance agreement, and present this annual report with a going concern condition, we recorded an additional \$1.8 million in valuation allowance reserves to cover our carryforward assets broadly. Such reserves may be reversed if conditions warrant, or if those deferred tax asset carryforwards are utilized.

Table of Contents

Investment in Clever Container

During November 2018, the Company announced its intention to divest its interest in Clever Container. During February 2019, the Company agreed in principle to sell its 28.5% interest in Clever Container to Messrs. Schwan and Merrick (principal stockholders of CTI) in exchange for their 30% ownership (combined) of CTI Europe. Due to this transaction and an ongoing reduction in involvement between the entities, the Company intends to deconsolidate Clever Container during 2019. As a result of these subsequent events and expected deconsolidation, the Company performed a valuation with respect to its investment in Clever Container. The Company recognized an impairment of its equity interest in Clever Container in the amount of \$0.2 million in 2018.

**Financial Condition, Liquidity and Capital Resources**

Cash Provided By Operating Activities During fiscal 2018, cash used by operating activities amounted to \$1,228,000, compared to cash provided by operating activities during fiscal 2017 of \$1,259,000. Significant changes in working capital items affecting cash flow used in operating activities were:

Depreciation and amortization of \$1,264,000 compared to depreciation and amortization for 2017 of \$1,659,000.

An increase in inventories of \$1,170,000 compared to an increase of inventories of \$222,000 in 2017.

A decrease in accounts receivable of \$399,000 compared to a decrease in accounts receivable of \$3,878,000 in 2017.

An increase in prepaid expenses and other assets of \$112,000 compared to an increase in prepaid expenses and other assets of \$690,000 in 2017.

An increase in trade payables of \$1,262,000 compared to a decrease in trade payables of \$564,000 in 2017.

Cash Used In Investing Activities During fiscal 2018, cash used in investing activities amounted to \$460,000 compared to cash used in investing activities during fiscal 2017 of \$753,000.

Cash Provided By Financing Activities During fiscal 2018, cash provided by financing activities amounted to \$2,445,000, compared to cash provided by financing activities of \$302,000 during fiscal 2017.

Until December 2017, we had in place a series of credit facility and related agreements with BMO Harris Bank, N.A. and BMO Private Equity (U.S.), (collectively, "BMO"), in the aggregate amount of approximately \$17 million. During December 2017, we terminated those agreements and fully repaid all amounts owed to BMO under those agreements, including associated fees and costs related to termination, as we entered in new financing agreements with PNC Bank,

National Association (“PNC”). The “PNC Agreements” include a \$6 million term loan and an \$18 million revolving credit facility, with a termination date of December 2022.

Table of Contents

Available credit under the Revolving Credit facility is determined by eligible receivables and inventory at CTI Industries (U.S.) and Flexo Universal (Mexico). We notified PNC of our failure to meet two financial covenants as of March 31, 2018. On June 8, 2018, we entered into Waiver and Amendment No. 1 (the “Amendment 1”) to our PNC Agreements. The Amendment modified certain covenants, added others, waived our failure to comply as previously reported, and included an amendment fee and temporary increase in interest rate. During September 2018, we filed a preliminary prospectus on Form S-1 for a planned equity issuance. On October 8, 2018, we entered into Consent and Amendment No. 2 (the “Amendment 2”) to our PNC Agreements. Amendment 2 reduced the amount of new funding proceeds that must be used to repay the term loan from \$5 million to \$2 million and waived the calculation of financial ratios for the period ended September 30, 2018, in exchange for a new covenant committing to raise at least \$7.5 million in gross proceeds from our equity issuance by November 15, 2018 and pay an amendment fee. Market conditions ultimately forced us to postpone the offering, and thus no proceeds were received by the November 15, 2018 requirement.

We engaged PNC to resolve this failure to meet our amended covenant, and as of March 2019 have entered into a Forbearance Agreement. Under the terms of this agreement, identified prior non-compliance conditions are resolved and financial covenants as of March 31, 2019 will not be considered, with the next calculation for the period ending June 30, 2019. As forbearance is a temporary condition and we remain out of compliance with the terms of our facility, we have reclassified long-term bank debt to current liabilities on our balance sheet. See Note 3 for a related discussion of the impact of this event.

Available credit under the Revolving Credit facility is determined by eligible receivables and inventory at CTI Industries (U.S.) and Flexo Universal (Mexico).

Certain terms of the PNC Agreements include:

*Restrictive Covenants:* The Credit Agreement includes several restrictive covenants under which we are prohibited from, or restricted in our ability to:

- o Borrow money;
- o Pay dividends and make distributions;
- o Make certain investments;
- o Use assets as security in other transactions;
- o Create liens;
- o Enter into affiliate transactions;
- o Merge or consolidate; or
  - o Transfer and sell assets.

Table of Contents

*Financial Covenants:* The Credit Agreement includes a series of financial covenants we are required to meet including:

We are required to maintain a "Leverage Ratio", which is defined as the ratio of (a) Funded Debt (other than the Shareholder Subordinated Loan) as of such date of determination to (b) EBITDA (as defined in the PNC Agreements) for the applicable period then ended. The highest values for this ratio allowed by the PNC Agreements are:

Fiscal Quarter Ratio

December 31, 2017	4.75 to 1.00
March 31, 2018	4.50 to 1.00
June 30, 2018	4.25 to 1.00
September 30, 2018	not applicable
December 31, 2018	3.50 to 1.00
March 31, 2019	not applicable
June 30, 2019	3.00 to 1.00
September 30, 2019 and thereafter	2.75 to 1.00

We are required to maintain a "Fixed Charge Coverage Ratio", which is defined as the ratio of (a) EBITDA for such fiscal period, minus Unfinanced Capital Expenditures made during such period, minus distributions (including tax distributions) and dividends made during such period, minus cash taxes paid during such period to (b) all Debt Payments made during such period. This ratio must not exceed 1.1 : 1.0 for any quarterly calculation.

The credit agreement provides for interest at varying rates in excess of the prime rate, depending on the level of senior debt to EBITDA over time. We also entered into a swap agreement with PNC Bank to fix the interest for \$3 million over 3 years.

Failure to comply with these covenants has caused us to pay a higher rate of interest (by 2% per the Agreements), and other potential penalties may impact the availability of the credit facility itself, and thus might negatively impact our ability to remain a going concern. As described above in Notes 3 and 9, we believe that we were not in compliance with this credit facility as of December 31, 2018, and have entered into a forbearance agreement with our bank as of March 2019.

On September 30, 2016, John H. Schwan advanced to the Company the sum of \$530,000 and on the same date, Stephen M. Merrick advanced to the Company the sum of \$370,000 to provide short-term working capital to the Company to fund the Company's obligation to purchase and produce inventory for a substantial order for vacuum sealing systems to be delivered in November 2016. In consideration of such advances, the Company issued a

Promissory Note to Mr. Schwan in the principal amount of \$530,000 and to Mr. Merrick in the amount of \$370,000 dated September 30, 2016 and bearing interest at the rate of 6% per annum. The principal balance of these notes was paid in December 2016 and January 2017.

As of December 2017, Mr. Schwan was owed a total of \$1.1 million, with additional accrued interest of \$0.4 million, by the Company. As part of the December 2017 financing with PNC, Mr. Schwan executed a subordination agreement related to these amounts due him, as evidenced by a related note. During January 2019, Mr. Schwan converted \$0.6 million of these notes for approximately 181,000 shares of the Company's common stock at then market rate. The Company owed Mr. Schwan a total of \$1.6 million on these notes as of December 31, 2018.

*Current Assets.* As of December 31, 2018, the total current assets of the Company were \$33,011,000, compared to total current assets of \$32,291,000 at December 31, 2017.



## Table of Contents

*Current Liabilities.* Total current liabilities increased to \$30,209,000 as of December 31, 2018 from \$22,661,000 as of December 31, 2017. \$3.5 million in debt was reclassified to current liabilities as of December 31, 2018.

*Liquidity and Capital Resources; Working Capital.* As of December 31, 2018, and 2017, respectively, our current assets exceeded our current liabilities by \$2,802,000 and \$9,630,000 (\$3.5 million of noncurrent debt was reclassified to current liabilities as of December 31, 2018); we had cash and cash equivalents of \$428,000 and \$181,000 and the potential for additional credit under our PNC Agreements. Management believes that these available funds, our internally generated funds and the borrowing capacity under our revolving line of credit facility will be sufficient to meet working capital requirements for the remainder of 2019. We believe that the financial covenants in the PNC Agreements will be challenging for the Company to meet unless and until it begins performing at a higher level, and have experienced compliance failures that have resulted in a higher rate of interest or other penalties, which in the future could increase or result in the loss of the facility. At the time of this filing, we are not in compliance with the terms of this agreement, as amended, and have entered into a forbearance agreement with PNC that resolves identified prior instances of non-compliance but does not change the terms of the facility itself. Our failure to regain compliance with the terms of our agreement could negatively impact the value of the facility on our liquidity, and if left uncorrected, ultimately impact our ability to continue as a going concern.

Additionally, we have encountered difficulties with seasonal cash flow needs, including increasing costs associated with obtaining seasonal workers in the Chicago area. The failure to properly manage seasonal cash needs could put strain on the Company, up to and including our ability to continue as a going concern (see Note 3 for additional discussion).

*CTI Industries Corporation Stockholders' Equity.* Stockholders' equity was \$7,328,000 as of December 31, 2018 compared to \$11,364,000 as of December 31, 2017.

## **Seasonality**

In the foil balloon product line, sales have historically been seasonal with approximately 40% occurring in the period from December through March of the succeeding year and 24% being generated in the period July through October in recent years. Vacuum sealing product sales are also seasonal; approximately 60% of sales in this product line occur in the period from July through December.

## **Critical Accounting Policies**

The financial statements of the Company are based on the selection and application of significant accounting policies which require management to make various estimates and assumptions. The following are some of the more critical judgment areas in the application of our accounting policies that currently affect our financial condition and results of operation.

Table of Contents

*Revenue Recognition.* Substantially all of the Company's revenues are derived from the sale of products. With respect to the sale of products, revenue from a transaction is recognized when (i) persuasive evidence of an arrangement exists, (ii) delivery of the product has occurred, (iii) the price to the buyer has been fixed or is determinable, and (iv) collectability is reasonably assured. The Company generally recognizes revenue for the sale of products when the products have been shipped and invoiced. In some cases, product is provided on consignment to customers. In those cases, revenue is recognized when the customer reports a sale of the product.

The Company adopted Accounting Standards Codification (ASC) Topic 606, *Revenue from Contracts with Customers*. On January 1, 2018, we adopted ASC 606 using the modified retrospective method. The adoption of ASC 606 did not have a material impact on our consolidated financial position or results of operations, as our revenue arrangements generally consist of a single performance obligation to transfer promised goods at a fixed price.

Net sales include revenues from sales of products and shipping and handling charges, net of estimates for product returns. Revenue is measured at the amount of consideration the Company expects to receive in exchange for the transferred products. Revenue is recognized at the point in time when we transfer the promised products to the customer and the customer obtains control over the products. The Company recognizes revenue for shipping and handling charges at the time the goods are shipped to the customer, and the costs of outbound freight are included in cost of sales, as we have elected the practical expedient included in ASC 606.

The Company provides for product returns based on historical return rates. While we incur costs for sales commissions to our sales employees and outside agents, we recognize commission costs concurrent with the related revenue, as the amortization period is less than one year and we have elected the practical expedient included in ASC 606. We do not incur incremental costs to obtain contracts with our customers. Our product warranties are assurance-type warranties, which promise the customer that the products are as specified in the contract. Therefore, the product warranties are not a separate performance obligation and are accounted for as described herein. Sales taxes assessed by governmental authorities are accounted for on a net basis and are excluded from net sales.

*Allowance for Doubtful Accounts.* We estimate our allowance for doubtful accounts based on an analysis of specific accounts, an analysis of historical trends, payment and write-off histories. Our credit risks are continually reviewed and management believes that adequate provisions have been made for doubtful accounts. However, unexpected changes in the financial condition of customers or changes in the state of the economy could result in write-offs which exceed estimates and negatively impact our financial results.

*Inventory Valuation.* Inventories are stated at the lower of cost or net realizable value. Cost is determined using standard costs which approximate costing determined on a first-in, first out basis. Standard costs are reviewed and adjusted at the time of introduction of a new product or design, periodically and at year-end based on actual direct and indirect production costs. On a periodic basis, the Company reviews its inventory levels for estimated obsolescence or unmarketable items, in reference to future demand requirements and shelf life of the products. As of December 31,

2018, the Company had established a reserve for obsolescence, marketability or excess quantities with respect to inventory in the aggregate amount of \$450,000. As of December 31, 2017, the amount of the reserve was \$500,000. In addition, on a periodic basis, the Company disposes of inventory deemed to be obsolete or unsaleable and, at such time, charges reserve for the value of such inventory. We record freight income as a component of net sales and record freight costs as a component of cost of goods sold.

Table of Contents

*Valuation of Long-Lived Assets.* We evaluate whether events or circumstances have occurred which indicate that the carrying amounts of long-lived assets (principally property and equipment and goodwill) may be impaired or not recoverable. Significant factors which may trigger an impairment review include: changes in business strategy, market conditions, the manner of use of an asset, underperformance relative to historical or expected future operating results, and negative industry or economic trends. We apply the provisions of generally accepted accounting principles in the United States of America (“U.S. GAAP”) U.S. GAAP, under which goodwill is evaluated at least annually for impairment. We performed a quantitative assessment for the year ended December 31, 2018 in which we considered the assets and liabilities of the Company as one operating segment, both recognized and unrecognized, as well as the cash flows necessary to operate the business relating to the assets and liabilities. We conducted a quantitative assessment of our goodwill in our consolidated balance sheet for the year ended December 31, 2017. From this quantitative assessment and from the quantitative assessment for December 31, 2018, we determined the fair value of the subsidiary exceeds the carrying amount initially recorded, and was therefore not impaired.

*Foreign Currency Translation.* All balance sheet accounts are translated using the exchange rates in effect at the balance sheet date. Statements of operations amounts are translated using the average exchange rates for the year-to-date periods. The gains and losses resulting from the changes in exchange rates during the period have been reported in other comprehensive income or loss, except that, on November 30, 2012, the Company determined that it does have an expectation of receiving payment with respect to indebtedness of Flexo Universal to the Company, and accordingly, as of and after that date foreign currency gains and losses with respect to such indebtedness will be reported in the statement of operations.

*Stock-Based Compensation.* We follow U.S. GAAP which requires all stock-based payments to employees, including grants of employee stock options, to be recognized in the consolidated financial statements based on their grant-date fair values.

We use the Black-Scholes option pricing model to determine the fair value of stock options which requires us to estimate certain key assumptions. In accordance with the application of U.S. GAAP, we incurred employee stock-based compensation cost of \$172,000 for the year ended December 31, 2018. At December 31, 2018, we had \$193,000 of unrecognized compensation cost relating to stock options.

*Income Taxes and Deferred Tax Assets.* Income taxes are accounted for as prescribed in U.S. GAAP. Under the asset and liability method of U.S. GAAP, the Company recognizes the amount of income taxes currently payable. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities, and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years these temporary differences are expected to be recovered or settled.



Table of Contents

We evaluate all available positive and negative evidence in each tax jurisdiction regarding the recoverability of any asset recorded in our Consolidated Balance Sheets and provide valuation allowances to reduce our deferred tax assets to an amount we believe is more likely than not to be realized. We regularly review our deferred tax assets for recoverability considering historical profitability, our ability to project future taxable income, the expected timing of the reversals of existing temporary differences and tax planning strategies. If we continue to operate at a loss in certain jurisdictions or are unable to generate sufficient future taxable income within the defined lives of such assets, we could be required to increase our valuation allowance against all or a significant portion of our deferred tax assets. This increase in valuation allowance could result in substantial increases in our effective tax rate and could have a material adverse impact on our operating results. Conversely, if and when our operations in some jurisdictions become sufficiently profitable before what we have estimated in our current forecasts, we would be required to reduce all or a portion of our current valuation allowance and such reversal would result in an increase in our earnings in such period.

Because we are out of compliance with the terms of our credit facility and operating under a forbearance agreement, and have related going concern disclosure, we established a valuation allowance reserve for substantially all of our deferred tax assets. In light of this, as of December 31, 2018, the Company had net deferred tax assets of \$135,000 representing the amount the Company may recover in future years from future taxable income. As of December 31, 2017, the amount of the net deferred tax asset was \$1,102,000. Each quarter and year-end, management makes a judgment to determine the extent to which the deferred tax asset will be recovered from future taxable income. This value was reduced, in large part, due to changes in US tax law effective 2018 which will impact the value of future deductions.

*Fair Value Measurements.* U.S. GAAP defines fair value, establishes a framework for measuring fair value, establishes a fair value hierarchy based on the quality of inputs used to measure fair value and enhances disclosure requirements for fair value measurements. U.S. GAAP clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. U.S. GAAP also requires that a fair value measurement reflect the assumptions market participants would use in pricing an asset or liability based upon the best information available. In February 2008, the FASB issued guidance now codified in U.S. GAAP which provides for delayed application of certain guidance related to non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually).

**Item No. 7A – Qualitative and Quantitative Disclosures Regarding Market Risk**

Not applicable.

**Item No. 8 – Financial Statements and Supplementary Data**

Reference is made to the Consolidated Financial Statements contained in Part IV hereof.



Table of Contents

**Item No. 9 – Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

**Item No. 9A – Controls and Procedures**

**Disclosure Controls and Procedures**

As required by Rule 13a-15(b) under the Exchange Act, we conducted an evaluation, under the supervision and with the participation of our management, including our Principal Executive Officer and Principal Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of December 31, 2018, the end of the period covered by this report. Based upon that evaluation, the Principal Executive Officer and Principal Financial Officer concluded that our disclosure controls and procedures were not effective as of December 31, 2018 as described below, to ensure that the information required to be disclosed by us in the reports that we file or submit under Security Exchange Act of 1934, as amended, (a) is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (b) is accumulated and communicated to our management, including officers, as appropriate, to allow for timely decisions regarding required disclosure. There were no material changes in our internal control over financial reporting during the fourth quarter of 2018 that have materially affected or are reasonably likely to materially affect our internal controls over financial reporting.

**Management's Report on Internal Control over Financial Reporting**

Management is responsible for establishing and maintaining adequate internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles. Internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. generally accepted accounting principles, and that receipts and expenditures are being made only in accordance with authorizations of the management and the Board; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of Company assets that could have a material effect on the financial statements.

Our management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control – Integrated Framework issued by the Committee Sponsoring Organizations of the Treadway Commission. This evaluation included review of the documentation of controls, evaluation of the design effectiveness of controls, testing of the operation effectiveness of controls and a conclusion on this evaluation. Although there are inherent limitations in the effectiveness of any system of internal controls over financial reporting, based on our evaluation, management has concluded our internal controls over financial reporting were not effective as of December 31, 2018. The Company’s capabilities, processes, and controls for development of certain financial statement estimates are not sufficient to ensure that such estimates take into account all potential financial outcomes and their probabilities, are based on sufficient persuasive and objective evidence, and result in recognition of amounts that are appropriate and consistent with the requirements of U.S. GAAP. In particular, we determined review and monitoring controls with respect to the reporting of our deferred tax assets and related tax provision that are not designed or operating at a level of precision sufficient to ensure prevention of material misstatements. These deficiencies resulted in audit adjustments with respect to our consolidated financial statements for the period ended December 31, 2018 in the areas of investment impairment, inventory reserves, and deferred tax asset valuation allowances. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. Management has determined that certain subsequent events were not properly captured in its analyses of the items above, and further that these deficiencies constitute a material weakness.

#### **Plan for Remediation of Material Weakness**

Management has adjusted its processes in order to more effectively capture potential impacts of subsequent events, or other events, particularly with respect to its analysis of deferred tax assets. Additional closing procedures have been established and will be evaluated for effectiveness in the future.

Table of Contents

This annual report does not include an attestation report of the company’s registered public accounting firm regarding internal control over financial reporting. Management’s report was not subject to attestation by the company’s registered public accounting firm pursuant to temporary rules of the Securities and Exchange Commission that permit the company to provide only management’s report in this annual report.

**Item No. 9B – Other Information**

None

**PART III**

**Item No. 10 – Directors, Executive Officers and Corporate Governance of the Registrant**

The members of our Board of Directors (the “Board”), and our executive officers, together with their respective ages and certain biographical information are set forth below. Directors hold office until the next annual meeting of our stockholders and until their successors have been duly elected and qualified. Our executive officers are elected by and serve at the designation and appointment of the Board.

<b>Name</b>	<b>Age</b>	<b>Position</b>
John H. Schwan	75	Chairman of the Board of Directors
Jeffrey S. Hyland	59	President, Chief Operating Officer, and Director
Stephen M. Merrick	77	General Counsel, Secretary and Director
Bret Tayne	60	Director
Stanley M. Brown	73	Director
John I. Collins	59	Director
John M. Klimek	60	Director
Frank J. Cesario	49	Chief Financial Officer
Samuel Komar	62	Vice President of Sales and Marketing
Jana Schwan	42	Vice President of Operations

The following is a brief account of the business experience of each of our directors and executive officers during the past five years or more.

*John H. Schwan.* Mr. Schwan has been an officer and director of the Company since January 1996. He was Chief Executive Officer of the Company until December 1, 2017, when he became Chairman of the Board of Directors. From January 1990 to March 2006, Mr. Schwan was principal owner and President of Rapak, L.L.C. From 1980 to 1990, Mr. Schwan was an owner and President of Packaging Systems Inc. Mr. Schwan has over 40 years of general management experience, including manufacturing, marketing and sales. Mr. Schwan served in the U.S. Army from 1966 to 1972, 1<sup>st</sup> Air Cavalry Division in Vietnam from 1968 to 1969 and was awarded the Combat Infantry Badge, Air Medal, two Bronze Stars with a V for valor and a purple heart. Mr. Schwan is currently serving on the boards of Leave No Veteran Behind, Armed Forces Council of Chicago, and was the interim president of the Pritzker Military Library. Mr. Schwan has a BA Degree from North Park University Chicago, Illinois.

*Jeffrey S. Hyland.* Mr. Hyland joined as President and Director of the Company on December 1, 2017, and added the role of Chief Executive Officer during November 2018. Mr. Hyland joined the Company from being Managing Director at Berkeley Research Group and prior to that an Executive Director at Capstone Advisory Group, both leading, global consulting firms. Mr. Hyland is experienced in providing consulting and C-suite responsibilities including areas in organizational leadership, strategic planning, refinancing, mergers and acquisitions, cost management, sales/marketing, operational efficiencies and financial management. He is a CPA with a B.S. in Accounting from the University of Illinois and a Masters of Management (MBA) in Marketing, Finance and Hospital & Health Services Management from Kellogg School of Management at Northwestern University.

*Stephen M. Merrick.* Mr. Merrick has been an officer of the Company since January 1996 and a director of the Company for more than 35 years. He has served as Chief Executive Officer, President and Chief Financial Officer of the Company prior to his current role of General Counsel. Mr. Merrick was engaged in the practice of law for more than 40 years. Mr. Merrick is also an officer and Director of Reliv International, Inc. (NASDAQ - RELV), a manufacturer and direct marketer of nutritional supplements and food products. Mr. Merrick received a BS Degree from Northwestern University in 1963 and a Juris Doctor Degree from Northwestern University School of Law in 1966. Mr. Merrick brings to the Company over 35 years of experience with the Company, 40 years of legal practice experience and an extensive background in general management and corporate finance.

*Bret Tayne.* Mr. Tayne has been a director of the Company since 1997. He has been President of Everede Tool Company and Intrepid Tool Industries since 1992 and 1999, respectively. From 1988 to 1992, Mr. Tayne was Executive Vice President of Unifin, a commercial finance company. Mr. Tayne received a BA Degree from Tufts University and an MBA from Northwestern University. Mr. Tayne brings over 20 years of general management, finance, sales, product, and marketing experience to the Company.

*Stanley M. Brown.* Mr. Brown was appointed as a director of the Company in January 1996. During the period from January 1989 to February 2012, Mr. Brown was director of venture capital and private company investments for a private, Chicago-based investment group, where he participated in investments, organization and management of several privately held businesses engaged in production, sales and services. Mr. Brown brings to the Board over 40 years of leadership and technical knowledge and experience, as well as over 20 years of management experience with production and service enterprises. From 1968 to 1989, Mr. Brown was with the United States Navy as a naval aviator, achieving squadron command and the rank of Captain. He received a BA Degree from Fordham University

and participated in post-graduate work in Naval architecture.

Table of Contents

*John I. Collins.* Mr. Collins has served as a director of the Company since 2004. From 2010 to the present, Mr. Collins has served as Senior Vice President, Strategy, and Risk Management for Alloya Corporate Federal Credit Union, a \$3 billion wholesale financial institution serving over 1,500 credit unions nationally. From 2003 to 2009, he was Chief Administrative Officer of Members United Corporate Federal Credit Union and from 2001 to 2003 was Chief Financial Officer of Mid-States Corporate Federal Credit Union. From 1991 to 2001, he served as Executive Vice President/Chief Financial Officer of Great Lakes Credit Union with responsibility for accounting, finance, information systems, investment management, lending and credit cards operations. Mr. Collins received a BA Degree in Economics, English and History from Ripon College and an MBA in Finance and Management from Emory University. Mr. Collins brings to the Company expertise, training and more than 20 years of experience in accounting, corporate finance, and corporate financial management.

*John M. Klimek.* Mr. Klimek has been a member of the Board of Directors since 2013. Mr. Klimek has been a practicing attorney in Illinois since 1984 specializing in corporate and securities law. From August 2004 to July 2018, Mr. Klimek was employed by HFR Asset Management, LLC, Chicago, Illinois, a hedge fund management company, most recently as President. Mr. Klimek brings strong financial, business and market acumen as well as compliance expertise and negotiating skills to the CTI Board. He holds a Juris Doctor and a BS Degree in Accountancy, both from the University of Illinois, Champaign-Urbana. He is also a director of Reliv International, Inc. (NASDAQ – RELV).

*Frank Cesario.* Mr. Cesario joined the Company in November 2017 as Chief Financial Officer. He brings nearly 20 years of CFO and controller experience at manufacturing entities. Prior to joining CTI, Mr. Cesario served in similar roles with Nanophase Technologies Corporation and ISCO International, Inc., publicly traded global suppliers of advanced materials and telecommunications equipment, respectively, as well as Turf Ventures LLC, a privately held chemicals distributor. He began his career with KPMG Peat Marwick and then served in progressively responsible finance positions within Material Sciences Corporation and Outokumpu Copper, Inc. Mr. Cesario holds an MBA (Finance) from DePaul University and a B.S. (Accountancy) from the University of Illinois, and is a registered CPA in the State of Illinois.

*Samuel Komar.* Mr. Komar has been employed by the Company since March of 1998, and was named Vice-President of Sales & Marketing in March of 2008. Mr. Komar has worked in sales and sales management for more than 25 years. Mr. Komar received a Bachelor of Science Degree in Business Administration and Marketing from Indiana University.

*Jana Schwan.* Ms. Schwan has been employed by the Company in various operational, purchasing, and product development capacities since September 2002, and was named Vice President of Operations in 2017.

Jana Schwan is the daughter of John Schwan.

Except as disclosed in this Item 10 or Item 13 (Certain Relationships and Related Transactions, and Director Independence), there are no arrangements or understandings with major stockholders, customers, suppliers or others pursuant to which any of our directors or members of senior management were selected as such. In addition, there are no family relationships among our executive officers and directors.

Our future success depends, in significant part, on the continued service of certain key executive officers, managers, and others in various aspects of our business. We may not be able to find an appropriate replacement for any of our key personnel. Any loss or interruption of our key personnel's service to the Company could adversely affect our ability to implement our business plan.

### **Corporate Governance**

The business and affairs of the Company are managed under the direction of the Board of Directors in accordance with the Illinois Business Corporation Act and the Articles of Incorporation and By-laws of the Company, as amended. Members of the Board of Directors are kept informed of the Company's business through discussions with the Chairman of the Board of Directors, the Chief Executive Officer, the President and other officers, by reviewing materials provided to them and by participating in meetings of the Board of Directors and its committees.

During 2018, the Board of Directors had seven members. The Board has determined that each of Stanley M. Brown, Bret Tayne, John I. Collins, and John M. Klimek, presently directors of the Company, are independent based upon the application of the rules and standards of the NASDAQ Stock Market.

The Board of Directors met nine times during 2018. Each of the Directors was present for at least 75% of such meetings.

Table of Contents

**Board Leadership Structure**

John H. Schwan has been appointed Chairman of the Board of Directors. In his role as Chairman, he presides over the meetings of the Board of Directors and communicates with the Chief Executive Officer, the President and the independent members of the Board. Jeffrey S. Hyland, Chief Executive Officer and President of the Company, and Stephen M. Merrick, General Counsel, are also members of the Board of Directors. Mr. Hyland is responsible for senior management functions of the Company, providing leadership in sales, marketing, operations, finance, and financial reporting, while Mr. Merrick is responsible for compliance and legal affairs of the Company. Both Mr. Merrick and Mr. Hyland report to the Board of Directors. The Board of Directors believes that this combination and allocation of roles between the two principal executive officers of the Company, each of whom are also members of the Board of Directors, provides the most efficient and effective leadership model for the Company, providing perspective and direction with regard to business strategies and plans to both the Board and management. The Company has no bylaw or policy in place that mandates that an officer serve as Chairman of the Board. The Board of Directors periodically evaluates its leadership structure.

John I. Collins has been designated as the lead independent director. Mr. Collins is responsible for (i) communicating regularly with the Chief Executive Officer and other officers of the Company on behalf of the Board of Directors, and particularly the independent members of the Board of Directors, and (ii) calling separate meetings of the independent directors of the Company. At such meetings, only independent directors are present and the independent directors are free to discuss any aspect of the Company's business and risk management without the influence of interested directors or management.

All members of the Company's Audit, Compensation and Nominating and Governance Committees have been determined to be independent based on application of the rules and standards of the NASDAQ Stock Market.

**Board Role in Risk Oversight**

The Board of Directors plays an active role, as a whole and at the committee level, in overseeing management of the Company's risks. The Board regularly reviews information regarding our credit, liquidity and operations, as well as the risks associated with each. The Audit Committee oversees management of financial risks through regular meetings with the Company's independent registered public accounting firm and the Company's Chief Executive Officer, President and Chief Financial Officer. The Company's Compensation Committee evaluates and addresses risks relating to executive compensation, our incentive compensation plans and other compensatory arrangements. The Nominating and Governance Committee manages risks associated with the independence of the Board of Directors and potential conflicts of interest. While each committee is responsible for evaluating certain risks and overseeing the management of those risks, the entire Board of Directors is regularly informed through management and committee reports to the full Board about these and other operational risks.



## **Committees of the Board of Directors**

The Board of Directors has standing Audit, Compensation and Nominating and Governance Committees.

### **Audit Committee**

Since 2000, the Company has had a standing Audit Committee, which is presently composed of Mr. Tayne (Chairman), Mr. Collins and Mr. Klimek. Each of the members of the Audit Committee is independent based on the application of the rules and standards of the NASDAQ Stock Market and Rule 10a-3(b) under the Securities Exchange Act of 1934. Mr. Collins has been designated as, and is, the Company's "Audit Committee Financial Expert" in accordance with Item 407(d)(5) of Regulation S-K and meets the requirements for an audit committee expert as set forth in that item. The Audit Committee has primary responsibility meetings with management and independent auditors to discuss the Company's financial statements. The Company's Board of Directors has adopted a written charter, as amended, for the Company's Audit Committee, a copy of which has been posted and can be viewed on the Company's Internet website at <http://www.ctiindustries.com> under the section entitled "Investor Relations." In addition, the Audit Committee has adopted a complaint monitoring procedure to enable confidential and anonymous reporting to the Audit Committee of concerns regarding, among other things, questionable accounting or auditing matters. The Audit Committee has primary responsibility for:

Appointing, compensating, and retaining our registered independent public accounting firm;

Overseeing the work performed by any outside accounting firm;

Assisting the Board of Directors in fulfilling its responsibility by reviewing the financial reports provided by us to the SEC, our stockholders, or to the general public, as well as the Company's internal financial and accounting controls; and

Recommending, establishing, and monitoring procedures designed to improve the quality and reliability of the disclosure of our financial condition and results of operations.

The Audit Committee met four times during 2018.

Table of Contents

**Compensation Committee**

The Compensation Committee is composed of Stanley M. Brown (Chairman), John I. Collins and John M. Klimek. The Board has determined that each of the members of the Compensation Committee is independent as defined in the listing standards for the NASDAQ Stock Market. The Compensation Committee reviews and acts on the Company's executive compensation and employee benefit and retirement plans, including their establishment, modification and administration. It also recommends to the Board of Directors the compensation of the Chief Executive Officer and certain other executive officers. The Compensation Committee has a charter which has been posted and can be viewed on the Company's Internet website at <http://www.ctiindustries.com> under the section entitled "Investor Relations." The Compensation Committee met one time during 2018.

**Nominating and Governance Committee**

In 2005, the Company established a Nominating and Governance Committee. The Nominating and Governance Committee consists of three directors, John Klimek (Chairman), Stanley Brown and Bret Tayne. The Nominating and Governance Committee does not have a charter. The Board of Directors has determined that each of the members of the Nominating and Governance Committee is independent as defined in the listing standards for the NASDAQ Stock Market.

The Nominating and Governance Committee has not adopted a formal policy with regard to consideration of director candidates recommended by security holders. The Company believes that continuing service of qualified incumbent members of the Board of Directors promotes stability and continuity at the Board level, contributes to the Board's ability to work as a collective body and provides the benefit of familiarity and insight into the Company's affairs. Accordingly, the process of the Nominating and Governance Committee for identifying nominees reflects the Company's practice of re-nominating incumbent directors who continue to satisfy the criteria for membership on the Board. For vacancies that are anticipated on the Board of Directors, the Nominating and Governance Committee intends to seek out and evaluate potential candidates from a variety of sources that may include recommendations by security holders, members of management, the Board of Directors, consultants and others. The minimum qualifications for potential candidates for the Board of Directors include demonstrated business experience, decision-making abilities, personal integrity and a good reputation.

While diversity is not a leading factor in the Nominating Committee's evaluation of potential candidates and there is no formal policy for considering diversity when nominating a potential director, it is a consideration that is evaluated along with other qualifications of potential candidates. In light of the foregoing, it is believed that a formal policy and procedure with regard to consideration of director candidates recommended by security holders is not necessary in order for the Nominating and Governance Committee to perform its duties.

The Nominating Committee did not meet in 2018. All of the independent directors of the Board of Directors participated in the nominating process and, in separate session, voted in favor of recommending to the Board of Directors the nomination of each of the nominees for election as directors.

### **Section 16(a) Beneficial Ownership Reporting Compliance**

Section 16(a) of the Securities Exchange Act of 1934 requires the Company's officers and directors, and persons who own more than ten percent of a registered class of the Company's equity securities, to file reports of ownership and changes in ownership with the Securities and Exchange Commission and with the NASDAQ Stock Market. Officers, directors and greater than ten-percent shareholders are required by SEC regulation to furnish the Company with copies of all Section 16(a) forms they file.

Based solely on a review of such forms furnished to the Company, the Company believes that during calendar year 2018, all Section 16(a) filing requirements applicable to the officers, directors and ten-percent beneficial shareholders were satisfied.

### **Code of Ethics**

The Company has adopted a code of ethics that applies to its senior executive and financial officers. The Company's Code of Ethics seeks to promote (i) honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships, (ii) full, fair, accurate, timely and understandable disclosure of information to the Commission, (iii) compliance with applicable governmental laws, rules and regulations, (iv) prompt internal reporting of violations of the Code to pre-designated persons, and (v) accountability for adherence to the Code. A copy of the Code of Ethics has been posted and may be viewed on the Company's Internet website at <http://www.ctiindustries.com> under the heading "Investor Relations." The Company will provide to any person without charge upon request a copy of the Code of Ethics. You may make such request by sending a written request to the Corporate Secretary at 22160 N. Pepper Road, Lake Barrington, Illinois 60010 and providing a return address.

Table of Contents**Item No. 11 – Executive Compensation**

The following table sets forth summary compensation information with respect to the Principal Executive Officer and other named executive officers, collectively referred to as our Named Executive Officers.

**SUMMARY COMPENSATION TABLE**

Name/Title	Year	Salary	Option Awards (1)	Non-Equity Incentive Plan Compensation (2)	All other compensation (3)	Total
Jeffrey S. Hyland Chief Executive Officer, President <sup>(4)</sup>	2018	\$238,578	\$164,806	\$ -	\$ 13,387	\$416,771
	2017	\$18,692	\$38,853	\$ -	\$ -	\$57,545
Stephen M. Merrick General Counsel (Formerly Chief Executive Officer) <sup>(5)</sup>	2018	\$177,577	\$2,090	\$ -	\$ -	\$179,667
	2017	\$240,968	\$2,090	\$ 17,332	\$ -	\$260,390
Frank J. Cesario Chief Financial Officer <sup>(6)</sup>	2018	\$147,000	\$-	\$ -	\$ -	147,000
	2017	\$20,192	\$-	\$ -	\$ -	20,192
Samuel Komar Vice President Sales & Marketing	2018	\$152,000	\$503	\$ -	\$ -	\$152,503
	2017	\$165,928	\$900	\$ 12,573	\$ 4,426	\$183,827

(1) Reflects the compensation expense recognized in 2018 and 2017 for stock option awards under ASC Topic 718 as reported in the Company's audited financial statements.

(2) Amounts determined under the Company's incentive compensation program.

(3) Amounts for 2017 include matching 401(k) contributions and life insurance premiums for Samuel Komar of \$2,757 and \$1,669, respectively; amounts for 2018 include company portion of health insurance for Jeffrey Hyland

(4) Mr. Hyland joined the Company in December 2018 as President. He added the role of Chief Executive Officer during November 2018.

Mr. Merrick was President until the hiring of Mr. Hyland, at which point he became Chief Executive Officer.

(5) During November 2018, Mr. Merrick became General Counsel as Mr. Hyland took the Chief Executive Officer role.

(6) Mr. Cesario joined the Company as Chief Financial Officer during November 2017.

**Narrative Disclosure for Summary Compensation Table**

## Employment Agreements with Our Named Executive Officers

On December 1, 2017, the Company and Jeffrey S. Hyland entered into an Employment Agreement employing Mr. Hyland as President of the Company. The agreement is for a three-year term automatically renewable for successive one-year terms unless terminated by either party at the end of any term. The agreement provides for Mr. Hyland to receive a base annual salary of \$243,000 and a one-time signing bonus of \$75,000 payable on or before February 28, 2018. Mr. Hyland will be entitled to participate in the Company's Incentive Compensation Plan and other employee benefit plans maintained by the Company. The agreement includes covenants requiring Mr. Hyland to maintain the confidentiality of confidential information of the Company, non-competition for a period of 24 months after termination of employment, and assignment of rights in work product and inventions.

The Employment Agreement also provides for Mr. Hyland to receive grants under the Company's 2009 Incentive Stock Plan of (i) 25,000 shares of restricted stock vesting at the rate of 5,000 shares immediately and 5,000 shares vesting each year for four years after the award date and (ii) incentive stock options to purchase up to 65,000 shares of common stock at the price per share of \$3.79 (the closing price on November 30, 2017) with the right to exercise the options vesting as to 10,834 shares on May 1, 2018 and on May 1 of each of 2019, 2020, 2021 and 2022, and as to 10,830 shares on December 1, 2022. In addition, as an inducement grant, the agreement provides for the Company to issue to Mr. Hyland non-qualified options to purchase up to 260,000 shares at the price of \$3.79 per share. These options are on substantially the same vesting terms as the incentive stock options and will vest as to 43,342 shares on the same vesting dates as the incentive stock options. The incentive and non-qualified options require that Mr. Hyland be employed full-time by the Company at the time of vesting and for the entirety of the period from the date of grant. The restricted stock and options will fully vest upon a change in control.

## Table of Contents

The Employment Agreement also provides for certain compensation to Mr. Hyland upon the termination of his employment without cause or upon a change in control, as further described herein.

### **Information Relating to Cash Incentives**

The Board of Directors has adopted an Incentive Compensation Plan providing for annual incentive compensation to be paid to executive and managerial employees of the Company. Under the Plan, designated Named Executive Officers and several other executive officers and managers may receive incentive compensation payments, determined on a quarterly and annual basis, based upon the income of the Company before provision for income tax or for incentive compensation if the net income exceeds a threshold amount of profit for any quarter of \$100,000 and, for the year, of \$250,000. The benefits under the Plan are divided into two Pools of compensation. Pool I (representing the largest pool of incentive compensation) covers senior executive officers and managers who participate in the pool of incentive compensation based upon a percentage allocation recommended by the Compensation Committee and determined by the Board of Directors each year. Pool II covers other executives and managers who are selected to participate in proportions determined by management. Under the Plan, the award to each participant in Pool I represents a percent of income and the Pool II award, in the aggregate, represents a percent of income. The Compensation Committee recommends the amount of the incentive compensation awards which, in the aggregate, may not exceed sixteen percent of the net income of the Company (before provision for income tax or incentive compensation under the Plan). Further, the amount of incentive compensation to any participant may not exceed the annual base compensation of the participant. The Compensation Committee believes such incentive compensation motivates participants to achieve strong profitability which is viewed as the most significant element of corporate performance, provides rewards for strong corporate performance and aligns the incentive with the interests of the shareholders. Incentive compensation participation levels are generally determined during the first quarter of each fiscal year.

In determining the executives who participate in the incentive compensation awards in Pool I each year, and the relative amount of the award to each participant, the Compensation Committee considers and takes into account (i) the position of the executive, (ii) the level of responsibility and authority of the executive, (iii) the performance of the executive, and (iv) the extent to which the executive is in a position to affect the financial results and profitability of the Company.

### **Long-Term Equity Incentives**

From time to time, upon the recommendation and action of the Compensation Committee and Board of Directors, stock options or grants under the 2009 Incentive Stock Plan have been awarded to officers, directors, or management personnel of the Company. At the Company's Annual Meeting of Shareholders held in May 2009, the Company's 2009 Incentive Stock Plan was approved by the shareholders.

The Board of Directors adopted and approved a new incentive option plan in April 2018 which was submitted to, and approved by, our stockholders at the annual meeting of stockholders on June 8, 2018 (the "Plan"). Under the Plan, the Compensation Committee of the Board of Directors is authorized to issue incentive options, non-statutory options, restricted stock awards and stock grants to officers, directors, management personnel and consultants of the Company. The Board of Directors determined that no further options would be granted under the 2009 Incentive Stock Plan.

Stock and option grants under the Plan will be determined from time to time by the Compensation Committee in consultation with management. The actual grant for each executive is determined by taking into consideration (i) individual performance, (ii) corporate performance and (iii) prior grants to, or stock ownership of the Company by, the executive or director. Generally, stock options are granted with an exercise price equal to or greater than the closing price of the Company's common stock on the NASDAQ Stock Market on the date of the grant.

Stock options awarded to Jeffrey S. Hyland are described in the summary of his Employment Agreement.

No stock options or grants were awarded or issued during 2018 or 2017, except the options and grants awarded to Mr. Hyland as described in his Employment Agreement.

### **Retirement Benefits**

The Company maintains a 401(k) employee savings plan in which all salaried employees are eligible to participate. The plan is a tax qualified retirement plan.

Under the 401(k) Plan, employees may contribute up to 15% of their eligible compensation to the Plan and the Company will contribute a matching amount to the Plan each year. Participating employees may direct the investment of individual and company contributions into one or more of the investment options offered by the Plan. Under the terms of the Plan, the Company has made a matching contribution equal to 100% of employee contributions that do not exceed 1% of eligible compensation plus 50% of employee contributions between 1% and 5% of eligible compensation. During 2017, the Board of Directors determined to cease matching contributions under the 401(k) Plan for the balance of the year. The Company's contributions to the 401(k) plan totaled approximately \$47,000 in 2017, which is allocated to participants subject to the vesting requirements of the Plan.

Table of Contents**Outstanding Equity Awards**

The following chart sets forth all outstanding equity awards to Named Executive Officers of the Company as of December 31, 2017. All awards are in the form of options to purchase Common Stock of the Company.

**OUTSTANDING EQUITY AWARDS**

Name	Option Awards Number of Securities Underlying Unexercised Options (#)		Option Exercise Price (\$)	Option Expiration Date
	Exercisable	Unexercisable		
Jeffrey S. Hyland	64,176	285,824	\$ 3.79	12/1/2022 (1)
Stephen M. Merrick	6,000	4,000	\$ 5.57	12/30/2020 (2)
Samuel Komar	2,175	1,450	\$ 5.06	12/30/2020 (3)

(1) Includes 25,000 shares of Restricted Stock, 10,000 of which are vested and 15,000 that vest through December 2021; 65,000 Incentive Stock Options of which 10,834 are vested and 54,166 will vest through December 2022; and 260,000 Non-Qualified stock options, of which 43,342 are vested and 216,658 will vest through December 2022.

(2) The stock option granted vests in one-fifth increments on each of June 30, 2016, June 30, 2017, June 30, 2018, June 30, 2019, and June 30, 2020.

**EQUITY COMPENSATION PLAN INFORMATION**

The following table sets forth the common stock of the Company authorized for issuance under the Company's equity compensation plans as of December 31, 2018.



Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans
Equity compensation plans by security holders	471,144	\$ 3.95	300,000
Equity compensation plans not approved by security holders	-	-	-
Total	471,144	\$ 3.95	300,000

#### **Payments Upon Termination or Change of Control**

The Employment Agreement among the Company and Jeffrey S. Hyland provides that, in the event of the termination of his employment by the Company without cause at the expiration of any term of the agreement or of the termination of the agreement by Mr. Hyland for good cause, he shall be entitled to receive severance pay of one-year base salary, payable in equal installments for such year. Further, in the event of a change of control, if Mr. Hyland's employment is terminated within one year of the change of control by him for good cause or by the Company without cause or due to failure to renew, he will be entitled to receive, as a lump sum, within 60 days following the termination date a severance payment equal to his base salary for the year.

Table of Contents**Director Compensation**

The following table sets forth the compensation of directors of the Company during the year ended December 31, 2018:

**DIRECTOR COMPENSATION**

<b>Name</b>	<b>Director's Fees</b>	<b>Option Awards<sup>(1)</sup></b>	<b>All other compensation</b>	<b>Total</b>
Stanley M. Brown	\$ 21,063	\$ -	\$ 22,000	<sup>(2)</sup> \$43,063
Bret Tayne	\$ 17,063	\$ -	\$ -	\$17,063
John I. Collins	\$ 17,063	\$ -	\$ -	\$17,063
John M. Klimek	\$ 17,063	\$ -	\$ -	\$17,063

<sup>(1)</sup> Reflects the compensation expense recognized in 2018 for stock option awards under ASC Topic 718 as reported in the Company's audited financial statements.

<sup>(2)</sup> Reflects consulting fees paid for services in connection with investor relations activities.

**Narrative Description of Director Compensation**

Non-management members of the Board of Directors receive a monthly fee of \$1,250 plus \$500 for each meeting of the Board of Directors or any Committee of the Board attended.

**Agreements Between Third Parties and Directors**

There are no agreements or arrangements by which any directors or nominees are to receive compensation or other payments from third parties in return for serving on the Board of Directors.

**Item No. 12 – Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

The Board of Directors knows of no other matters to be presented for shareholder action at the Annual Meeting. On matters which may be raised at the Annual Meeting that are not covered by this Proxy Statement, the persons named in the proxy will have full discretionary authority to vote.

Table of Contents**BENEFICIAL OWNERSHIP OF SHARES BY MANAGEMENT****AND SIGNIFICANT SHAREHOLDERS**

The following table provides information concerning the beneficial ownership of the Company's Common Stock by each director and nominee for director, certain executive officers, and by all directors and officers of the Company as a group as of April 1, 2019. In addition, the table provides information concerning the current beneficial owners, if any, known to the Company to hold more than 5 percent of the outstanding Common Stock of the Company.

The amounts and percentage of stock beneficially owned are reported based on regulations of the Securities and Exchange Commission ("SEC") governing the determination of beneficial ownership of securities. Under the rules of the SEC, a person is deemed to be a "beneficial owner" of a security if that person has or shares "voting power," which includes the power to dispose of or to direct the disposition of such security. A person is also deemed to be a beneficial owner of any securities of which that person has a right to acquire beneficial ownership within 60 days after April 1, 2019. Under these rules, more than one person may be deemed a beneficial owner of the same securities and a person may be deemed a beneficial owner of securities in which he has no economic interest. The percentage of Common Stock beneficially owned is based on 3,735,950 shares of Common Stock outstanding as of April 1, 2019.

<b>Name and Address of Beneficial Owner <sup>(1)</sup></b>	<b>Amount of Beneficial Ownership <sup>(2)</sup></b>	<b>Percent of Common Stock</b>
John H. Schwan	1,009,439 <sup>(3)</sup>	27.0%
Stephen M. Merrick	832,800 <sup>(4)</sup>	22.3%
Jeffrey S. Hyland	118,352 <sup>(5)</sup>	3.2%
Frank J. Cesario	2,000	*
Samuel Komar	5,225 <sup>(6)</sup>	*
Bret Tayne	15,841 <sup>(7)</sup>	*
Stanley M. Brown	4,592 <sup>(8)</sup>	*
Jana Schwan	7,900 <sup>(9)</sup>	*
John Collins	5,900 <sup>(10)</sup>	*
John M. Klimek	8,632 <sup>(11)</sup>	*
All Current Directors and Executive Officers as a group (10 persons)	2,010,681	53.8%

\*Less than one percent

(1)

Edgar Filing: CTI INDUSTRIES CORP - Form 10-K

Except as otherwise indicated, the address of each shareholder listed above is c/o CTI Industries Corporation, 22160 North Pepper Road, Lake Barrington, Illinois 60010.

A person is deemed to be the beneficial owner of securities that can be acquired within 60 days from the date set forth above through the exercise of any option, warrant or right. Shares of Common Stock subject to options, (2) warrants or rights that are currently exercisable or exercisable within 60 days are deemed outstanding for purposes of computing the percentage ownership of the person holding such options, warrants or rights, but are not deemed outstanding for purposes of computing the percentage ownership of any other person.

(3) Includes options to purchase 6,000 shares of Common Stock at \$5.57 per share granted under the Company's 2009 Stock Option Plan.

(4) Includes 793,467 shares held in the name of The Merrick Company LLC of which Mr. Merrick is a principal owner and options to purchase 6,000 shares of Common Stock at \$5.57 per share granted under the Company's 2009 Stock Option Plan.

(5) Includes options to purchase 21,668 shares of Common Stock at \$3.79 per share granted under his Employment Agreement and options to purchase 86,684 shares of Common Stock at \$3.79 per share granted under his Employment Agreement.

(6) Includes options to purchase 725 shares of Common Stock at \$5.06 per share granted under the Company's 2009 Stock Option Plan.

(7) Includes options to purchase 2,175 shares of Common Stock at \$5.06 per share granted under the Company's 2009 Stock Option Plan.

(8) Includes options to purchase 1,631 shares of Common Stock at \$5.06 per share granted under the Company's 2009 Stock Option Plan.

(9) Includes options to purchase 2,175 shares of Common Stock at \$5.06 per share granted under the Company's 2009 Stock Option Plan.

(10) Includes options to purchase 2,175 shares of Common Stock at \$5.06 per share granted under the Company's 2009 Stock Option Plan.

(11) Includes options to purchase 5,000 shares of Common Stock at \$5.75 per share and options to purchase 2,175 shares of Common Stock at \$5.06 per share granted under the Company's 2009 Stock Option Plan.

Table of Contents

**Item No. 13 – Certain Relationships and Related Transactions**

Stephen M. Merrick, General Counsel and former Chief Executive Officer of the Company, is of counsel to a law firm from which the Company received legal services during the year. Mr. Merrick is both a director and a shareholder of the Company. Legal fees paid to this firm were \$88,000 and \$154,000 for the years ended December 31, 2018 and 2017, respectively.

During the period from January 2003 to the present, John H. Schwan, Chairman of the Board, has made loans to the Company which have outstanding balances of \$1,597,000 and \$1,507,000 as of December 31, 2018 and 2017, respectively. During 2018 and 2017, interest expense to this individual on these outstanding loans was \$93,000 and \$94,000, respectively. During January 2018, \$0.6 million of this balance was exchanged for approximately 181,000 shares of common stock at the market price at that time.

During 2010, two entities owned by officers and principal shareholders of the Company (John H. Schwan and Stephen M. Merrick) provided financing for Flexo Universal, the Company's Mexico subsidiary, for the acquisition and construction of latex balloon production and related equipment. The entities included Venture Leasing L.L.C., ("VLUS"), an Illinois limited liability company which is 100% owned by an entity owned by Mr. Schwan and Mr. Merrick, and Venture Leasing Mexico S. A. de R. L ("VLM"), a Mexico company which is also owned 100% by entities owned by Mr. Schwan and Mr. Merrick. Title to the equipment remained in the name of VLM. VLM leased the equipment to Flexo Universal under a lease under which Flexo Universal paid to VLM rental payments at the rate of approximately \$9,000 per month and had the right to purchase the equipment from VLM at the expiration of the lease at fair market value. During 2016, the lease expired and Flexo Universal purchased the equipment from VLM. The Company has not provided any guarantees related to VLUS or VLM and no creditors of the variable interest entities have recourse to the general credit of the Company as a result of including VLUS & VLM in the consolidated financial statements. The accounts of VLM and VLUS have been consolidated with the accounts of the Company for 2018 and 2017 and going forward.

John H. Schwan and Stephen M. Merrick, also through an investment entity, own, in aggregate, a 50% interest in Clever Container Company L.L.C., an Illinois limited liability company. The Company acquired a 28.5% interest in Clever Container from third parties in 2016. During 2018 and 2017, Clever Container purchased various products from the Company in the amount of \$858,000 and \$954,000, respectively. As of December 31, 2018 and 2017, the balance of accounts receivable from Clever Container to the Company were \$1,352,000 and \$988,000, respectively. During 2018 and 2017, the results of Clever Container were consolidated with the financial statements of the Company.

Relationships and transactions in which the Company and its directors and executive officers or their immediate family members are participants or have conflicts of interest are reviewed and approved by the Audit Committee. While the Audit Committee has not adopted a written policy for the review and approval of related party transactions,

in determining whether to approve or ratify any such transaction, the Audit Committee considers, in addition to such other factors it may deem appropriate in the circumstances, whether (i) the transaction is fair and reasonable to the Company, (ii) under all of the circumstances, the transaction is in, or not inconsistent with, the Company's best interests, and (iii) the transaction will be on terms no less favorable to the Company than could have been obtained in an arms' length transaction with an unrelated third party. The Audit Committee, in its discretion, may request information from any party to facilitate its consideration of matter. The Audit Committee does not allow a director to participate in any review, approval or ratification of any transaction if he or she, or his or her immediate family member, has a direct or indirect material interest in the transaction.

#### Item No. 14 – Principal Accountant Fees and Services

The following table sets forth the amount of fees billed by Plante & Moran PLLC, our independent registered public accounting firm, for professional services during the years ended December 31, 2018 and 2017:

	<b>Dec. 31, 2018</b>	<b>Dec. 31, 2017</b>
Audit Fees <sup>(1)</sup>	\$242,618	\$280,327
Other Audit Related Fees <sup>(2)</sup>	3,525	9,989
All Other Fees <sup>(3)</sup>	23,750	51,581
Total Fees	\$269,893	\$341,897

(1)Includes the annual financial statement audit and limited quarterly reviews and expenses.

(2)Includes fees and expenses for other audit related activity provided by Plante & Moran PLLC.

(3)Primarily represents tax services, which include preparation of tax returns and other tax consulting services.

All audits, tax and other services to be performed by Plante & Moran PLLC for the Company must be pre-approved by the Audit Committee. The Audit Committee reviews the description of services and an estimate of the anticipated costs to perform those services. Services not previously approved cannot commence until such approval has been granted. Pre-approval is granted usually at regularly scheduled meetings. If unanticipated items arise between meetings of the Audit Committee, the Audit Committee has delegated approval authority to the Chairman of the Audit Committee, in which case the Chairman communicates such pre-approvals to the full Committee at its next meeting.

The Audit Committee of the Board of Directors reviews all relationships with its independent auditors, including the provision of non-audit services, which may relate to the independent registered public accounting firm's independence. The Audit Committee of the Board of Directors considered the effect of Plante & Moran's tax services in assessing the

independence of the independent registered public accounting firm and concluded that the provision of such services by Plante & Moran was compatible with the maintenance of that firm's independence in the conduct of its auditing function.



Table of Contents

**PART IV**

**Item No. 15 – Exhibits and Financial Statement Schedules**

The Consolidated Financial Statements filed as part of this report on Form 10-K are listed on the accompanying

1. Index to Consolidated Financial Statements and Consolidated Financial Statement Schedules.

2. Financial schedules required to be filed by Item 8 of this form, and by Item 15(d) below:

Schedule II Valuation and qualifying accounts

All other financial schedules are not required under the related instructions or are inapplicable and therefore have been omitted.

3. Exhibits:

Exhibit

Document

Number

- |      |  |
|------|--|
| 3.1  | <u>Restated Articles of Incorporation (Incorporated by reference to Exhibit A to Registrant's Schedule 14A Definitive Proxy Statement filed April 29, 2015).</u>   |
| 3.2  | <u>Amended and Restated By-Laws of CTI Industries Corporation (Incorporated by reference to Exhibit 3.2, contained in Registrant's Form 8-K filed on March 17, 2017).</u>  |
| 4.1  | <u>Form of CTI Industries Corporation's common stock certificate (Incorporated by reference to Exhibit 4.1 contained in Registrant's Report on Form 10-K dated March 31, 2017).</u>                                      |
| 10.1 | <u>CTI Industries Corporation 2009 Stock Incentive Plan (Incorporated by reference to Schedule A contained in Registrant's Schedule 14A Definitive Proxy Statement, as filed with the Commission on April 30, 2009).</u> |
| 10.2 | <u>CTI Industries Corporation 2018 Stock Incentive Plan (Incorporated by Reference to Schedule A contained in Registrant's 14A Definitive Proxy Statement, as filed with the Commission on April 30, 2018)</u>           |
| 10.3 | <u>Lease Agreement between Schultz Bros. Co. and the Company dated September 19, 2012 (Incorporated by reference to Exhibit 10.8 contained in Registrant's Report on Form 10-Q dated November 14, 2012).</u>             |

Table of Contents

- 10.4 Stock Purchase Warrant to Purchase Common Stock of CTI Industries Corporation (Incorporated by reference to Exhibit 10.5 contained in Registrant’s Report on Form 10-Q dated August 22, 2016).
- 10.5 Registration Rights Agreement between [Purchaser] and the Company (Incorporated by reference to Exhibit 10.6 contained in Registrant’s Report on Form 10-Q dated August 22, 2016).
- 10.6 Promissory Note between CTI Industries and Stephen M. Merrick dated September 30, 2016 (Incorporated by reference to Exhibit 10.1 contained in Registrant’s Report on Form 10-Q dated November 14, 2016).
- 10.7 Promissory Note between CTI Industries and John H. Schwan dated September 30, 2016 (Incorporated by reference to Exhibit 10.2 contained in Registrant’s Report on Form 10-Q dated November 14, 2016).
- 10.8 Employment Agreement between Jeffrey S. Hyland and the Company dated December 1, 2017 (Incorporated by reference to Exhibit 10.38 contained in Registrant’s Report on Form 10-K filed on April 2, 2018).
- 10.9 Revolving Credit, Term Loan, and Security Agreement dated December 14, 2017 (Incorporated by reference to Exhibit 10.1, contained in Registrant’s Form 8-K filed on December 19, 2017).
- 10.10 Revolving Credit Note dated December 14, 2017 (Incorporated by reference to Exhibit 10.2, contained in Registrant’s Form 8-K filed on December 19, 2017).
- 10.11 Term Note dated December 14, 2017 (Incorporated by reference to Exhibit 10.3, contained in Registrant’s Form 8-K filed on December 19, 2017).
- 10.12 Promissory Note dated December 14, 2017 (Incorporated by reference to Exhibit 10.4, contained in Registrant’s Form 8-K filed on December 19, 2017).
- 10.13 Real Property Mortgage dated December 14, 2017 (Incorporated by reference to Exhibit 10.5, contained in Registrant’s Form 8-K filed on December 19, 2017).
- 10.14 Subordination Agreement dated December 14, 2017 (Incorporated by reference to Exhibit 10.6, contained in Registrant’s Form 8-K filed on December 19, 2017).
- 10.15 Waiver and Amendment No. 1 to Revolving Credit, Term Loan and Security Agreement dated June 12, 2018 (Incorporated by reference to Exhibit 10.1, contained in Registrant’s Form 8-K filed on June 12, 2018)
- 10.16 Consent and Amendment No. 2 to Revolving Credit, Term Loan and Security Agreement dated October 8, 2018 (Incorporated by reference to Exhibit 10.1, contained in Registrant’s form 8-K filed on October 12, 2018)

Table of Contents

- 10.17 Subscription Agreement among Registrant and John H. Schwan dated December 21, 2018 (Incorporated by reference to Exhibit 10.1, contained in Registrant's form 8-K filed on January 17, 2019)
- 10.18 Settlement Agreement and Release dated January 21, 2019 (filed herewith as Exhibit 10.19)
- 10.19 Amendment No.1 to Agreement among CTI, GLG, Page and H One dated January 21, 2019 (filed herewith as Exhibit 10.19)
- 10.20 Amendment No. 3 and Forbearance Agreement to Revolving Credit, Term Loan and Security Agreement dated March 4, 2019 (Incorporated by reference to Exhibit 10.1, contained in Registrant's form 8-K filed on March 8, 2019)
- 14 Code of Ethics (Incorporated by reference to Exhibit contained in the Registrant's Form 10-K/A Amendment No. 2, as filed with the Commission on October 13, 2004).
- 21 Subsidiaries (description incorporated in Form 10-K under Item No. 1).
- 23.1 Consent of Independent Registered Public Accounting Firm, Plante & Moran, PLLC.
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and rule 15d-14(a) of the Securities Exchange Act, as amended (filed herewith).
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and rule 15d-14(a) of the Securities Exchange Act, as amended (filed herewith).
- 32 Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 99 Audited financial statements of the Company's subsidiary, Flexo Universal, S. de R.L. de C.V. for the year ended December 31, 2018.
- 101 Interactive Data Files, including the following materials from the Company's Annual Report on Form 10-K for the year ended December 31, 2018, formatted in XBRL: (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Operations, (iii) the Consolidated Statements of Cash Flows, and (iv) the Notes to Consolidated Financial Statements.

- (a) The Exhibits listed in subparagraph (a)(3) of this Item 15 are attached hereto unless incorporated by reference to a previous filing.
- (b) The Schedule listed in subparagraph (a)(2) of this Item 15 is attached hereto.

Table of Contents

**SIGNATURES**

In accordance with Section 13 or 15(d) of the Exchange Act the Registrant caused this report to be signed on its behalf by the undersigned thereunto duly authorized on April 15, 2019.

CTI INDUSTRIES CORPORATION

By: /s/ Jeffrey S. Hyland  
 Jeffrey S. Hyland, President, Chief Executive

Officer and Director

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the Registrant in the capacities and on the dates indicated.

<b>Signatures</b>	<b>Title</b>	<b>Date</b>
<u>/s/ Jeffrey S. Hyland</u>	President, Chief Executive	April 15, 2019
Jeffrey S. Hyland	Officer and Director	
<u>/s/ Frank J. Cesario</u>	Chief Financial Officer	April 15, 2019
Frank J. Cesario		
<u>/s/ John H. Schwan</u>	Chairman of the Board of	April 15, 2019
<u>John H. Schwan</u>	Directors	
<u>/s/ Stephen M. Merrick</u>	Director	April 15, 2019
Stephen M. Merrick		
<u>/s/ Stanley M. Brown</u>	Director	April 15, 2019
Stanley M. Brown		
<u>/s/ Bret Tayne</u>	Director	April 15, 2019
Bret Tayne		

/s/ John I. Collins

Director

April 15, 2019

John I. Collins

/s/ John Klimek

Director

April 15, 2019

John Klimek

Table of Contents

CTI Industries Corporation  
and Subsidiaries

Consolidated Financial Statements

Years ended December 31, 2018 and 2017

**Contents**

Consolidated Financial Statements:

<u>Report of Independent Registered Public Accounting Firm</u>	F-1
<u>Consolidated Balance Sheets as of December 31, 2018 and 2017</u>	F-2
<u>Consolidated Statements of Comprehensive Income for the years ended December 31, 2018 and 2017</u>	F-3
<u>Consolidated Statements of Stockholders' Equity as of December 31, 2018 and 2017</u>	F-4
<u>Consolidated Statements of Cash Flows for the years ended December 31, 2018 and 2017</u>	F-5
<u>Notes to Consolidated Financial Statements for the years ended December 31, 2018 and 2017</u>	F-6

Financial Statement Schedule:

<u>Schedule II – Valuation and Qualifying Accounts for the years ended December 31, 2018 and 2017</u>	F-28
---	------

All other schedules for which a provision is made in the applicable accounting regulation of the Securities and Exchange Commission are not required under the related instructions or are inapplicable and, therefore, have been omitted.

Table of Contents

**Report of Independent Registered Public Accounting Firm**

To the Stockholders and Board of Directors of CTI Industries Corporation and Subsidiaries

***Opinion on the Consolidated Financial Statements***

We have audited the accompanying consolidated balance sheets of CTI Industries Corporation and Subsidiaries (the “Company”) as of December 31, 2018, and 2017, and the related consolidated statements of comprehensive income, stockholders' equity, and cash flows for each of the years in the two-year period ended December 31, 2018 and 2017 and the related notes and financial Schedule II – Valuation and Qualifying Accounts (collectively referred to as the “consolidated financial statements”). We did not audit the 2018 or 2017 financial statements of Flexo Universal S. de R.L. de C.V., a 99.82 percent owned subsidiary, whose statements reflect total assets and revenue constituting 27 percent and 18 percent of the related consolidated totals, respectively, as of and for the year ended December 31, 2018, and total assets and revenue constituting 21 percent and 16 percent of the related consolidated totals as of and for the year ended December 31, 2017. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Flexo Universal S. de R.L. de C.V., is based solely on the report of the other auditors. In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2018, and 2017 and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2018 and 2017 in conformity with accounting principles generally accepted in the United States of America.

Continuation as a Going Concern

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 3 to the consolidated financial statements, the Company has suffered net losses from operations and liquidity limitations that raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 3. The financial statements do not include any adjustments that might result from the outcome of this uncertainty

***Basis for Opinion***

The Company's management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on the Company's consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (“PCAOB”) and are required to be

independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

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

Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Plante & Moran, PLLC

We have served as the Company's auditor since 2007.

Chicago, Illinois  
April 15, 2019

F-1

---



Table of Contents**CTI Industries Corporation and Subsidiaries  
Condensed Consolidated Balance Sheets**

	<b>December 31, 2018</b>	<b>December 31, 2017</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents (VIE \$57,000 and \$2,000, respectively)	\$428,150	\$ 181,026
Accounts receivable, (less allowance for doubtful accounts of \$85,000 and \$114,000, respectively)	10,830,555	11,235,834
Inventories, net (VIE \$340,000 and \$498,000, respectively)	20,007,488	18,865,932
Prepaid expenses (VIE \$127,000 and \$80,000, respectively)	858,158	887,885
Other current assets	886,383	1,120,808
<b>Total current assets</b>	<b>33,010,734</b>	<b>32,291,485</b>
Property, plant and equipment:		
Machinery and equipment	23,807,985	23,439,781
Building	3,367,082	3,367,082
Office furniture and equipment (VIE \$303,000 and \$268,000, respectively)	2,649,280	2,591,159
Intellectual property	783,179	752,044
Land	250,000	250,000
Leasehold improvements	409,188	402,963
Fixtures and equipment at customer locations	518,450	518,450
Projects under construction	150,272	121,241
	31,935,436	31,442,720
Less : accumulated depreciation and amortization (VIE \$104,000 and \$36,000, respectively)	(28,120,455)	(26,886,139)
<b>Total property, plant and equipment, net</b>	<b>3,814,981</b>	<b>4,556,581</b>
Other assets:		
Goodwill (VIE \$440,000 and \$440,000, respectively)	1,473,176	1,473,176
Net deferred income tax asset	135,094	1,102,467
Other assets	326,849	560,329
<b>Total other assets</b>	<b>1,935,119</b>	<b>3,135,972</b>
<b>TOTAL ASSETS</b>	<b>\$38,760,834</b>	<b>\$39,984,038</b>
<b>LIABILITIES AND EQUITY</b>		
Current liabilities:		
Checks written in excess of bank balance (VIE \$7,000 and \$16,000, respectively)	\$636,142	\$454,850
Trade payables (VIE \$62,000 and \$144,000, respectively)	6,679,670	5,414,497
Line of credit (VIE \$267,000 and \$338,000, respectively)	16,582,963	13,783,930

Edgar Filing: CTI INDUSTRIES CORP - Form 10-K

Notes payable - current portion	4,432,320	942,533
Notes payable affiliates - current portion	10,821	9,615
Capital Lease - current portion	-	7,562
Accrued liabilities (VIE \$89,000 and \$92,000, respectively)	1,866,796	2,047,893
<b>Total current liabilities</b>	<b>30,208,712</b>	<b>22,660,880</b>
<b>Long-term liabilities:</b>		
Notes payable - affiliates	199,122	212,545
Notes payable, net of current portion (VIE \$27,000 and \$83,000, respectively)	399,912	4,951,581
Notes payable - officers, subordinated	1,597,019	1,507,362
Deferred gain (non current)	100,340	207,410
Deferred income tax liability	-	-
<b>Total long-term debt, net of current portion</b>	<b>2,296,393</b>	<b>6,878,898</b>
<b>Total long-term liabilities</b>	<b>2,296,393</b>	<b>6,878,898</b>
<b>Equity:</b>		
<b>CTI Industries Corporation stockholders' equity:</b>		
Preferred Stock -- no par value, 3,000,000 shares authorized, 0 shares issued and outstanding	-	-
Common stock - no par value, 15,000,000 shares authorized, 3,578,885 shares issued and 3,535,227 shares outstanding	13,898,494	13,898,494
Paid-in-capital	2,506,437	2,271,261
Accumulated earnings	(2,865,486 )	720,223
Accumulated other comprehensive loss	(6,050,347 )	(5,365,364 )
Less: Treasury stock, 43,658 shares	(160,784 )	(160,784 )
<b>Total CTI Industries Corporation stockholders' equity</b>	<b>7,328,314</b>	<b>11,363,830</b>
Noncontrolling interest	(1,072,585 )	(919,570 )
<b>Total Equity</b>	<b>6,255,729</b>	<b>10,444,260</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$38,760,834</b>	<b>\$39,984,038</b>

See accompanying notes to condensed consolidated unaudited financial statements

Table of Contents**CTI Industries Corporation and Subsidiaries  
Condensed Consolidated Statements of Comprehensive Income**

	<b>For the Year Ended December 31,</b>	
	2018	2017
Net Sales	\$55,591,102	\$56,236,560
Cost of Sales	44,162,124	42,481,710
Gross profit	11,428,978	13,754,850
Operating expenses:		
General and administrative	7,149,128	7,657,338
Selling	3,664,985	3,638,241
Advertising and marketing	1,253,444	1,971,420
Gain on sale of assets	(94,106 )	(140,494 )
Loss on impairment of equity	220,000	
Other operating income		(1,416 )
Total operating expenses	12,193,451	13,125,089
(Loss) Income from operations	(764,473 )	629,761
Other (expense) income:		
Interest expense	(2,106,227 )	(1,576,229 )
Interest income	21,763	
Change in fair value of warrants		19,999
Foreign currency loss	46,919	(144,855 )
Total other expense, net	(2,037,545 )	(1,701,085 )
Net (loss) before taxes	(2,802,018 )	(1,071,324 )
Income tax expense	936,706	711,533
Net (loss)	(3,738,724 )	(1,782,857 )
Less: Net (loss) income attributable to noncontrolling interest	(153,015 )	(179,754 )
Net loss attributable to CTI Industries Corporation	\$(3,585,709 )	\$(1,603,103 )
Other Comprehensive Income (Loss)		
Foreign currency adjustment	(684,983 )	228,514

Edgar Filing: CTI INDUSTRIES CORP - Form 10-K

Comprehensive Income (Loss)	\$ (4,270,692 )	\$ (1,374,589 )
Basic loss per common share	\$ (1.00 )	\$ (0.45 )
Diluted loss per common share	\$ (1.00 )	\$ (0.44 )
Weighted average number of shares and equivalent shares of common stock outstanding:		
Basic	3,578,885	3,568,885
Diluted	3,578,885	3,616,244

See  
 accompanying  
 notes to  
 condensed  
 consolidated  
 unaudited  
 financial  
 statements

F-3

---

Table of Contents**CTI Industries Corporation and Subsidiaries  
Consolidated Statements of Stockholders' Equity**

	CTI Industries Corporation			Accumulated (Deficit) Earnings	Accumulated Other Comprehensive Loss	Less Treasury Stock		Noncontrolling Interest	Total
	Common Stock Shares	Amount	Paid-in Capital		Loss	Shares	Amount		
Balance, December 31, 2016	3,568,885	\$13,898,494	\$2,250,235	\$2,323,326	\$(5,593,878)	(43,658)	\$(160,784)	(739,816)	\$
Stock Option Expense			\$21,026						\$
Net Income				(1,603,103)				(179,754)	\$
Other comprehensive income, net of taxes									
Foreign currency translation					228,514				\$
Balance, December 31, 2017	3,568,885	\$13,898,494	\$2,271,261	\$720,223	\$(5,365,364)	(43,658)	\$(160,784)	(919,570)	\$
Stock Issued	10,000								
Stock Option Expense			171,576						
Net Income Arbitration Settlement - note 17			\$63,600	\$(3,585,709)				(153,015)	\$
Other comprehensive income, net of taxes									

Foreign  
currency  
translation

(684,983 )

Balance

December 31, 2018    \$3,578,885    \$13,898,494    \$2,506,437    \$(2,865,486)    \$(6,050,347)    \$(43,658)    \$(160,784)    \$(1,072,585)

See accompanying notes to consolidated financial statements

F-4

---

Table of Contents**CTI Industries Corporation and Subsidiaries  
Condensed Consolidated Statements of Cash Flows**

	For the Year ended December 31,	
	2018	2017
Cash flows from operating activities:		
Net (loss) income	\$(3,738,724)	\$(1,782,857)
Depreciation and amortization	1,264,424	1,546,413
Amortization of debt discount	-	112,622
Change in fair value of warrants	-	(19,999 )
Loss on impairment of equity	220,000	-
Stock based compensation	171,576	-
Amortization of deferred gain on sale/leaseback	(109,801 )	(109,976 )
Provision for losses on accounts receivable	(28,296 )	(29,227 )
Provision for losses on inventories	(98,179 )	(295,430 )
Deferred income taxes	967,373	594,223
Change in assets and liabilities:		
Accounts receivable	399,414	3,878,170
Inventories	(1,169,583)	(222,491 )
Prepaid expenses and other assets	(112,392 )	(690,015 )
Trade payables	1,262,441	(564,333 )
Accrued liabilities	(256,130 )	(1,157,701)
Net cash (used in) provided by operating activities	\$(1,227,877)	\$1,259,399
Cash flows from investing activities:		
Purchases of property, plant and equipment	(459,542 )	(753,199 )
Net cash used in investing activities	\$(459,542 )	\$(753,199 )
Cash flows from financing activities:		
Change in checks written in excess of bank balance	181,292	(1,233,825)
Net change in revolving line of credit	2,802,076	2,466,652
Repayment of long-term debt (related parties \$17,000 and \$0)	(1,074,767)	(8,663,000)
Cash paid for deferred financing fees	(22,755 )	(299,824 )
Contributions received by Variable Interest Entity	495,993	515,912
Proceeds from issuance of stock	63,600	0
Proceeds from issuance of debt		7,507,362
Proceeds from issuance of note receivable		8,740
Net cash (used in) provided by financing activities	\$2,445,439	\$302,017
Effect of exchange rate changes on cash	(510,896 )	(1,190,234)

Edgar Filing: CTI INDUSTRIES CORP - Form 10-K

Net increase (decrease) in cash and cash equivalents	247,124	(382,017 )
Cash and cash equivalents at beginning of period	181,026	563,043
Cash and cash equivalents at end of period	\$428,150	\$ 181,026
Supplemental disclosure of cash flow information:		
Cash payments for interest	2,011,827	1,426,743
Cash payments for taxes	165,000	300,000
Supplemental Disclosure of non-cash investing and financing activity		
Interest Accrued not paid	\$86,000	\$65,000
Property, Plant & Equipment acquisitions funded by liabilities	\$39,358	\$ 186,409

See accompanying notes to condensed consolidated unaudited financial statements

F-5

---



Table of Contents

Notes to Consolidated Financial Statements Years Ended  
December 31, 2018 and 2017

**1. Nature of Business**

*Nature of Operations*

CTI Industries Corporation, its United Kingdom subsidiary (CTI Balloons Limited), its Mexican subsidiary (Flexo Universal, S. de R.L. de C.V.), its German subsidiary (CTI Europe GmbH) and CTI Supply, Inc. (collectively, the “Company”) (i) design, manufacture and distribute metalized and latex balloon products throughout the world and (ii) operate systems for the production, lamination, coating and printing of films used for food packaging and other commercial uses and for conversion of films to flexible packaging containers and other products.

**2. Summary of Significant Accounting Policies**

*Principles of Consolidation*

The consolidated financial statements include the accounts of CTI Industries Corporation, its wholly owned subsidiaries CTI Balloons Limited and CTI Supply, Inc. and its majority owned subsidiaries, Flexo Universal and CTI Europe, as well as the accounts of Venture Leasing S. A. de R. L., Venture Leasing L.L.C., and Clever Container Company, L.L.C. (Clever Container). The last three entities have been consolidated as variable interest entities. All significant intercompany accounts and transactions have been eliminated upon consolidation.

*Variable Interest Entities*

The determination of whether or not to consolidate a variable interest entity under generally accepted accounting principles in the United States of America (U.S. GAAP) requires a significant amount of judgment concerning the degree of control over an entity by its holders of variable interest. To make these judgments, management has conducted an analysis of the relationship of the holders of variable interest to each other, the design of the entity, the expected operations of the entity, which holder of variable interests is most “closely associated” to the entity and which

holder of variable interests is the primary beneficiary required to consolidate the entity. Upon the occurrence of certain events, management reviews and reconsiders its previous conclusion regarding the status of an entity as a variable interest entity. Management continually reconsiders whether the Company is deemed to be a variable interest entity's primary beneficiary who consolidates such entity. The Company has three entities that have been consolidated as variable interest entities. (See Note 14)

***Foreign Currency Translation***

The financial statements of foreign subsidiaries are translated into U.S. dollars using the exchange rate at each balance sheet date for assets and liabilities, the historical exchange rate for stockholders' equity, and a weighted average exchange rate for each period for revenues and expenses. Translation adjustments are recorded in accumulated other comprehensive income (loss) as the local currencies of the subsidiaries are the functional currencies. Foreign currency transaction gains and losses are recognized in the period incurred and are included in the consolidated statements of operations.

Table of Contents

*Use of Estimates*

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, management makes estimates and assumptions that affect the amounts reported of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period in the financial statements and accompanying notes. Actual results may differ from those estimates. The Company's significant estimates include valuation allowances for doubtful accounts, inventory valuation, deferred tax assets, goodwill and intangible asset valuation, and assumptions used as inputs in the Black-Scholes option-pricing model.

*Cash and Cash Equivalents*

Cash and cash equivalents include cash on hand, demand deposits and short-term investments with original maturities of three months or less.

*Accounts Receivable*

Trade receivables are carried at original invoice amount less an estimate for doubtful receivables based on a review of all outstanding amounts on a monthly basis. Management determines the allowance for doubtful accounts by identifying troubled accounts, evaluating the individual customer receivables through consideration of the customer's financial condition, credit history and current economic conditions and use of historical experience applied to an aging of accounts. A trade receivable is considered to be past due if any portion of the receivable balance is outstanding for a period over the customer's normal terms. Trade receivables are written off when deemed uncollectible. Recoveries of trade receivables previously written off are recorded when received.

*Inventories*

Inventories are stated at the lower of cost or net realizable value. Cost is determined using standard costs which approximates costing determined on a first-in, first-out basis, to reflect the actual cost of production of inventories.

Production costs of work in process and finished goods include material, labor and overhead. Work in process and finished goods are not recorded in excess of net realizable value.

F-7

---

Table of Contents***Property, Plant and Equipment***

Property and equipment are stated at cost. Expenditures for maintenance and repairs are charged to operations as incurred. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets. Leasehold improvements are amortized on a straight-line method over the lesser of the estimated useful life or the lease term. The estimated useful lives range as follows:

	(in years)
Building	25 -30
Machinery and equipment	3 -15
Projects that prolong the life and increase efficiency of machinery	3 -5
Light Machinery	5 -10
Heavy Machinery	10 -15
Office furniture and equipment	5 -8
Intellectual Property	9 -15
Leasehold improvements	5 -8
Furniture and equipment at customer locations	1 - 3

Light machinery consists of forklifts, scissor lifts, and other warehouse machinery. Heavy machinery consists of production equipment including laminating, printing and converting equipment. Projects in process represent those costs capitalized in connection with construction of new assets and/or improvements to existing assets including a factor for interest on funds committed to projects in process of \$14,000 and \$11,000 for the years ended December 31, 2018 and 2017, respectively. Upon completion, these costs are reclassified to the appropriate asset class.

***Stock-Based Compensation***

The Company has stock-based incentive plans which may grant stock option, restricted stock and unrestricted stock awards. The Company recognizes stock-based compensation expense based on the grant date fair value of the award and the related vesting terms. The fair value of stock-based awards is determined using the Black-Scholes model, which incorporates assumptions regarding the risk-free interest rate, expected volatility, expected option life, and dividend yield. See Note 17 for additional information.

***Fair Value Measurements***

U.S. GAAP defines fair value, establishes a framework for measuring fair value, and requires disclosures about fair value measurements required under other accounting pronouncements. See Note 5 for further discussion.

The Company accounts for derivative instruments in accordance with U.S. GAAP, which requires that all derivative instruments be recognized on the balance sheet at fair value. We may enter into interest rate swaps to fix the interest rate on a portion of our variable interest rate debt to reduce the potential volatility in our interest expense that would otherwise result from changes in market interest rates. Our derivative instruments are recorded at fair value and are included in accrued liabilities of our consolidated balance sheet. Our accounting policies for these instruments are based on whether they meet our criteria for designation as hedging transactions, which include the instrument's effectiveness, risk reduction and, in most cases, a one-to-one matching of the derivative instrument to our underlying transaction. As of December 31, 2018 and 2017, we had one derivative instrument accounted for as a hedge. Gains and losses from changes in fair values of derivatives that are not designated as hedges for accounting purposes are recognized in the consolidated statement of operations. We have no such derivative financial instruments as of December 31, 2018 and 2017. Changes in fair value for the respective periods were recognized in the consolidated statement of operations.

## Table of Contents

### *Goodwill*

The Company applies the provisions of U.S. GAAP, under which goodwill is tested at least annually for impairment. Goodwill on the accompanying balance sheets relates to the Company's acquisition of Flexo Universal in a prior year, the investment in CTI Europe in a prior year and the goodwill related to Clever Container, a variable interest entity in which CTI is the primary beneficiary. It is the Company's policy to perform impairment testing annually as of December 31, or as circumstances change. An annual impairment review was completed and no impairment was noted for the years ended December 31, 2018 and 2017 (see Note 15). While the Company believes that its estimates of future cash flows are reasonable, different assumptions regarding such cash flows could materially affect these evaluations.

### *Valuation of Long Lived Assets*

The Company evaluates whether events or circumstances have occurred which indicate that the carrying amounts of long-lived assets (principally property, plant and equipment) may be impaired or not recoverable. The significant factors that are considered that could trigger an impairment review include: changes in business strategy, market conditions, or the manner of use of an asset; underperformance relative to historical or expected future operating results; and negative industry or economic trends. In evaluating an asset for possible impairment, management estimates that asset's future undiscounted cash flows and appraised values to measure whether the asset is recoverable. The Company measures the impairment based on the projected discounted cash flows of the asset over its remaining life.

### *Deferred Financing Costs*

Deferred financing costs are amortized on a straight-line basis over the term of the loan. Upon a refinancing, existing unamortized deferred financing costs are expensed.

### *Income Taxes*

The Company accounts for income taxes using the liability method. As such, deferred income taxes reflect the net tax effects of temporary differences between carrying amounts of assets and liabilities for financial reporting purposes and the amount used for income tax purposes.

Deferred tax assets and liabilities are measured using enacted tax rates expected to be in effect when the anticipated reversal of these differences is scheduled to occur. Deferred tax assets are reduced by a valuation allowance when management cannot determine, in its opinion, that it is more likely than not that the Company will recover that recorded value of the deferred tax asset. The Company is subject to U.S. Federal, state and local taxes as well as foreign taxes in the United Kingdom, Germany and Mexico. U.S. income tax expense and foreign withholding taxes are provided on remittances of foreign earnings and on unremitted foreign earnings that are not indefinitely reinvested.

F-9

---



## Table of Contents

Unrecognized tax benefits are accounted for as required by U.S. GAAP which prescribes a more likely than not threshold for financial statement presentation and measurement of a tax position taken or expected to be taken in a tax return. See Note 11 for further discussion.

### ***Revenue Recognition***

On January 1, 2018, we adopted Accounting Standards Codification (ASC) Topic 606, *Revenue from Contracts with Customers* using the modified retrospective method. The adoption of ASC 606 did not have a material impact on our consolidated financial position or results of operations, as our revenue arrangements generally consist of a single performance obligation to transfer promised goods at a fixed price.

Net sales include revenues from sales of products and shipping and handling charges, net of estimates for product returns. Revenue is measured at the amount of consideration the Company expects to receive in exchange for the transferred products. Revenue is recognized at the point in time when we transfer the promised products to the customer and the customer obtains control over the products. The Company recognizes revenue for shipping and handling charges at the time the goods are shipped to the customer, and the costs of outbound freight are included in cost of sales, as we have elected the practical expedient included in ASC 606.

The Company provides for product returns based on historical return rates. While we incur costs for sales commissions to our sales employees and outside agents, we recognize commission costs concurrent with the related revenue, as the amortization period is less than one year and we have elected the practical expedient included in ASC 606. We do not incur incremental costs to obtain contracts with our customers. Our product warranties are assurance-type warranties, which promise the customer that the products are as specified in the contract. Therefore, the product warranties are not a separate performance obligation and are accounted for as described herein. Sales taxes assessed by governmental authorities are accounted for on a net basis and are excluded from net sales.

A disaggregation of product net sales is presented in Note 19.

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

The Company conducts product development and research activities which include (i) creative product development and (ii) engineering. During the years ended December 31, 2018 and 2017, research and development activities totaled \$375,000 and \$345,000, respectively.

*Advertising Costs*

The Company expenses advertising costs as incurred. Advertising expenses amounted to \$171,000 and \$119,000 for the years ended December 31, 2018 and 2017, respectively.

F-10

---

Table of Contents

**Note 3 – Liquidity and Going Concern**

The Company's primary sources of liquidity are cash and cash equivalents as well as availability under the Credit Agreement with PNC (see Note 9). As noted in Note 9, we initiated an equity issuance process and entered into an amendment with PNC that would have allowed us more flexibility in the use of any proceeds, but also committed us to raise at least \$7.5 million by November 15, 2018. That offering was ultimately terminated due to changes in market conditions. As that condition was not met, we are in violation of our Agreement, as amended.

As of March 2019, we entered into a forbearance agreement with PNC. Under the terms of this agreement, financial covenants as of March 31, 2019 will not be considered and all previously identified compliance failures will be waived, but we remain out of compliance with the terms of our credit facility, as amended.

In addition to the above, due to financial performance in 2016, 2017 and 2018, including net income/(losses) attributable to the Company of \$0.7 million, (\$1.6 million), and (\$3.6 million), respectively, we believe that substantial doubt about our ability to continue as a going concern exists at December 31, 2018.

Additionally, we have experienced challenges in maintaining adequate seasonal working capital balances, made more challenging by increases in financing and labor costs. These changes in cash flows have created strain within our operations, and have therefore increased our desire to incorporate additional funding resources.

Management's plans include:

- (1) Pursuing a strategically significant major capital event.
- (2) Working with our bank to resolve our compliance failure on a long-term basis.
- (3) Evaluating and potentially executing a sale/leaseback transaction of our facility in Lake Barrington, IL.
- (4) Continuing to monitor the equity market for the potential to complete the transaction attempted during 2018, and
- (5) Exploring alternative funding sources.

Management Assessment

Considering both quantitative and qualitative information, we continue to believe that our plans to obtain additional financing will provide us with an ability to finance our operations through 2019 and, if adequately executed, will

mitigate the substantial doubt about our ability to continue as a going concern.

F-11

---

Table of Contents

**4. New Accounting Pronouncements**

In February 2016, the FASB issued ASU 2016-02, *Leases* (Topic 842), aimed at making leasing activities more transparent and comparable. The new standard requires substantially all leases be recognized by lessees on their balance sheet as a right-of-use asset and corresponding lease liability, including today's operating leases. For public business entities, the standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. For all other entities, the standard is effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. Early application is permitted for all entities.

We will adopt the standard as required on January 1, 2019 and use that date as our date of initial application of the guidance. Consequently, we will not update previously reported financial information and the disclosures under the new standard will not be provided for dates and periods prior to January 1, 2019. We will elect all of the practical expedients available under the transition guidance. The new standard also provides practical expedients for ongoing accounting. We will elect the short-term lease recognition exemption for all leases that qualify. That means we will not recognize right of use assets or lease liabilities for those leases. We will also elect the practical expedient to not separate lease and non-lease components for all of our leases. We expect that this standard will have a material impact on our financial statements. While we continue to assess all of the effects of adoption, we currently believe the most significant effects relate to the recognition of new right of use assets and lease liabilities on our balance sheet for our real estate and equipment operating leases, and the significant new required disclosures regarding our leasing activities. We do not expect a significant change in our leasing activities between now and adoption.

On adoption, we expect to recognize additional operating lease liabilities of approximately \$3 million, with corresponding right of use assets for the same amount based on the present value of the remaining minimum rental payments under current leasing standards for existing operating leases.

**5. Fair Value Disclosures; Derivative Instruments**

U.S. GAAP clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. U.S. GAAP also requires that a fair value measurement reflect the assumptions market participants would use in pricing an asset or liability based upon the best information available.

U.S. GAAP establishes a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy categorizes assets and liabilities at fair value into one of three different levels depending on the observability of the inputs employed in the measurement. The three levels are defined as follows:

Level 1 – inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 – inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs are observable for the asset or liability, or unobservable but corroborated by market data, for substantially the full term of the financial instrument.

Level 3 – inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Table of Contents

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of the input that is significant to the fair value measurement. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

The interest rate swap entered into December 14, 2017 had a three-year term (ending December 14, 2020) and a notional amount of \$3 million. The Company purchased a 2.25% fixed rate in exchange for the variable rate on a portion of the notes payable under the PNC Agreements, which was 1.47% at time of execution (see Note 9). The fair value of the swap was insignificant as of December 31, 2018 and 2017. The contract is expected to terminate during 2019 at no cost or benefit to the Company under the agreement executed with PNC during March 2019.

**6. Other Comprehensive Loss****Accumulated  
Other  
Comprehensive  
Loss Balances  
as of December  
31, 2018**

	Foreign Currency Items	Accumulated Other Comprehensive Loss
Beginning balance	\$(5,365,364)	\$(5,365,364 )
Current period change	(684,983 )	(684,983 )
Ending balance	\$(6,050,347)	\$(6,050,347 )

**Accumulated Other Comprehensive Loss Balances as of December 31, 2017**

	Foreign Currency Items	Accumulated Other Comprehensive Loss
Beginning balance	\$(5,593,878)	\$(5,593,878 )
Current period change	228,514	228,514
Ending balance	\$(5,365,364)	\$(5,365,364 )

For the years ended December 31, 2018 and 2017, no tax benefit has been recorded on the foreign currency translation; as such amounts would result in a deferred tax asset and are not expected to reverse in the foreseeable future.

F-13

---



Table of Contents**7. Major Customers**

For the year ended December 31, 2018, the Company had two customers that accounted for approximately 24.8% and 24.5% of consolidated net sales. For the year ended December 31, 2017, those same two customers accounted for approximately 27.5% and 16.9% of consolidated net sales. At December 31, 2018, the outstanding accounts receivable balances due from these customers were \$2,160,000 and \$3,731,000, respectively. At December 31, 2017, the outstanding accounts receivable balances due from these customers were \$2,871,000 and \$3,088,000, respectively.

**8. Inventories**

Inventories are stated at the lower of cost or net realizable value. Cost is determined using standard costs which approximate costing determined on a first-in, first out basis. Standard costs are reviewed and adjusted periodically and at year end based on actual direct and indirect production costs. On a periodic basis, the Company reviews its inventory for estimated obsolescence or unmarketable items, primarily by reviewing future demand requirements and shelf life of the product.

Inventories are comprised of the following:

	<b>December 31,</b>	<b>December 31,</b>
	<b>2018</b>	<b>2017</b>
Raw materials	\$1,994,741	\$2,632,415
Work in Process	3,052,224	3,386,078
Finished Goods	14,934,581	13,347,620
In Transit	480,716	
Allowance for excess quantities	(454,774 )	(500,181 )
Total inventories	\$20,007,488	\$18,865,932

**9. Notes Payable and Capital Leases**

Long term debt consists of:

	<b>Dec. 31, 2018</b>	<b>Dec. 31, 2017</b>
Capital Lease with First American Equipment Finance, payable in monthly installments of \$2,890 (amortized over 5 years).		3,000
Capital Lease with Wells Fargo, payable in monthly installments of \$367 (amortized over 5 years).		2,000
Subordinated Notes (Officers) due on demand, interest at 4%, which consolidated prior Subordinated Notes (Officers). During January 2019, \$600,000 of this balance was exchanged for 181,000 shares of our common stock at then market value	1,597,000	1,507,000
Notes Payable (Affiliates) due 2015, interest at prime (3.25%) plus 0.25% (3.5%) at December 31, 2017 (see Note 12) (Related Party).	32,000	32,000
Promissory Note with Merrick Company due on demand, interest at 4.25% (Related Party).	39,000	76,000
Promissory Note with Schwan Leasing due on demand, interest at 4.25% (Related Party).	127,000	60,000
Notes Payable (Affiliates) due 2021, interest at 11.75% (see Note 12) (Related Party).	28,000	41,000
Term Loan with PNC, payable in monthly installments of \$100,000 amortized over 5 years, interest at 8.25%, balance due December 2022, which uses balloons and related equipment as collateral	4,700,000	6,000,000
Total long-term debt	6,523,000	7,721,000
Less current portion	(4,432,000)	(1,247,000)
Total Long-term debt, net of current portion	\$2,091,000	\$6,474,000

Table of Contents

Until December 2017, we had in place a series of credit facility and related agreements with BMO Harris Bank, N.A. and BMO Private Equity (U.S.), (collectively, “BMO”), in the aggregate amount of approximately \$17 million. During December 2017, we terminated those agreements and fully repaid all amounts owed BMO under those agreements, including the outstanding warrant note payable and associated fees and costs related to termination, as we entered in new financing agreements with PNC Bank, National Association (“PNC”). The “PNC Agreements” include a \$6 million term loan and an \$18 million revolving credit facility, with a termination date of December 2022.

Available credit under the Revolving Credit facility is determined by eligible receivables and inventory at CTI Industries (U.S.) and Flexo Universal (Mexico). We notified PNC of our failure to meet two financial covenants as of March 31, 2018. On June 8, 2018, we entered into Waiver and Amendment No. 1 (the “Amendment 1”) to our PNC Agreements. The Amendment modified certain covenants, added others, waived our failure to comply as previously reported, and included an amendment fee and temporary increase in interest rate. During September 2018, we filed a preliminary prospectus on Form S-1 for a planned equity issuance. On October 8, 2018, we entered into Consent and Amendment No. 2 (the “Amendment 2”) to our PNC Agreements. Amendment 2 reduced the amount of new funding proceeds that must be used to repay the term loan from \$5 million to \$2 million and waived the calculation of financial ratios for the period ended September 30, 2018, in exchange for a new covenant committing to raise at least \$7.5 million in gross proceeds from our equity issuance by November 15, 2018 and pay an amendment fee. Market conditions ultimately forced us to postpone the offering, and thus no proceeds were received by the November 15, 2018 requirement.

We engaged PNC to resolve this failure to meet our amended covenant, and as of March 2019 have entered into a forbearance agreement. Under the terms of this agreement, previously identified compliance failures will be waived and financial covenants as of March 31, 2019 will not be considered, with the next calculation due for the period ending June 30, 2019. We received a temporary over-advance of \$1.2 million, declining to zero over a six week period, under the terms of this agreement and paid a fee of \$250,000. As forbearance is a temporary condition and we remain out of compliance with the terms of our facility, we have reclassified long-term bank debt to current liabilities on our balance sheet. See Note 3 for a related discussion of the impact of this event.

Table of Contents

Available credit under the Revolving Credit facility is determined by eligible receivables and inventory at CTI Industries (U.S.) and Flexo Universal (Mexico).

Certain terms of the PNC Agreements include:

*Restrictive Covenants:* The Credit Agreement includes several restrictive covenants under which we are prohibited from, or restricted in our ability to:

- o Borrow money;
- o Pay dividends and make distributions;
- o Make certain investments;
- o Use assets as security in other transactions;
- o Create liens;
- o Enter into affiliate transactions;
- o Merge or consolidate; or
  - o Transfer and sell assets.

*Financial Covenants:* The Credit Agreement includes a series of financial covenants we are required to meet including:

We are required to maintain a "Leverage Ratio", which is defined as the ratio of (a) Funded Debt (other than the Shareholder Subordinated Loan) as of such date of determination to (b) EBITDA (as defined in the PNC Agreements) for the applicable period then ended. The highest values for this ration allowed by the PNC Agreements are:

Fiscal Quarter Ratio

December 31, 2017	4.75 to 1.00
March 31, 2018	4.50 to 1.00
June 30, 2018	4.25 to 1.00
September 30, 2018	not applicable
December 31, 2018	3.50 to 1.00
March 31, 2019	not applicable
June 30, 2019	3.00 to 1.00
September 30, 2019 and thereafter	2.75 to 1.00

o We are required to maintain a "Fixed Charge Coverage Ratio", which is defined as the ratio of (a) EBITDA for such fiscal period, minus Unfinanced Capital Expenditures made during such period, minus distributions (including tax

distributions) and dividends made during such period, minus cash taxes paid during such period to (b) all Debt Payments made during such period. This ratio must not exceed 1.1 : 1.0 for any quarterly calculation.

F-16

---

Table of Contents

The credit agreement provides for interest at varying rates in excess of the prime rate, depending on the level of senior debt to EBITDA over time. We also entered into a swap agreement with PNC Bank to fix the rate of interest for \$3 million of the notes over 3 years at 2.25%. This contract was made at market value upon December 14, 2017 execution and accounted for as a hedge. This contract is expected to terminate during 2019 at no cost or benefit to the Company under the terms of the forbearance agreement.

Failure to comply with these covenants has caused us to pay a higher rate of interest (by 2% per the Agreements), and other potential penalties may impact the availability of the credit facility itself, and thus might negatively impact our ability to remain a going concern. As described above in this Note as well as in Note 3, we believe that we were not in compliance with this credit facility as of December 31, 2018, and have entered into a forbearance agreement with our bank as of March 2019.

**10. Subordinated Debt – Related Parties**

As of December 2017, Mr. Schwan was owed a total of \$1.1 million, with additional accrued interest of \$0.4 million, by the Company. As part of the December 2017 financing with PNC, Mr. Schwan executed a subordination agreement related to these amounts due him, as evidenced by a related note representing the amount owed to Mr. Schwan. During January 2019, Mr. Schwan and the Company agreed to an exchange of \$0.6 million of his debt for approximately 181,000 shares of CTI common stock at the then market rate of \$3.32 per share. As of December 31, 2018, the balance of Mr. Schwan's note was approximately \$1.6 million, including accrued interest.

**11. Income Taxes**

The income tax provisions are comprised of the following:

	<b>Dec. 31 2018</b>	<b>Dec. 31 2017</b>
Current:		
Federal	\$165,000	\$(188,549)
State	-	(11,964 )
Foreign	(245,040 )	317,823
	\$(80,040 )	\$117,310
Deferred		
Federal	\$317,640	\$732,895
State	266,413	(79,598 )

Foreign	432,693	(59,074 )
	1,016,746	594,223
Total Income Tax Provision	\$936,706	\$711,533

F-17

---

Table of Contents

The 2017 tax provision included the impact of changes in deferred taxes of \$0.2 million resulting from the federal rate change from 34% to 21%.

The components of the net deferred tax asset at December 31 are as follows:

	<b>2018</b>	<b>2017</b>
Deferred tax assets:		
Federal and state net operating loss carryforwards	\$ 805,865	\$ 523,808
Foreign tax credit and other credits	469,408	592,993
Reserves and accruals	320,783	271,884
Unicap 263A adjustment	112,199	126,944
Other deferred tax assets	88,369	26,198
Foreign and VIE net operating loss carryforwards	566,765	569,147
Deferred Interest Expense	529,983	-
Total gross deferred tax assets	2,893,372	2,110,974
Deferred tax liabilities:		
Fixed assets and intangibles	(257,113 )	(273,746 )
Deferred state income tax	(91,691 )	(103,055 )
Total gross deferred tax liabilities	(348,804 )	(376,801 )
Less: valuation allowance	(2,409,474)	(631,706 )
Net deferred tax assets	135,094	1,102,467
Deferred Tax Asset Valuation Allowance		
Beginning Balance	631,706	45,000
Additions charged (credited) to expense	1,777,768	586,706
Balance at end of year	2,409,474	631,706

The Company has a net operating loss carryforward for federal income tax purposes of approximately \$1.0 million which will begin to expire in 2024, as well as federal tax credits of approximately \$0.5 million after \$0.1 million expired during 2018. It also has a net operating loss carryforward for state income tax purposes of approximately \$6.3 million, which will begin to expire in 2022. On December 22, 2017, the U.S. government enacted significant tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "Tax Act"). The Tax Act created a separate category of creditable foreign source income related to foreign branches. This may operate to prevent cross-crediting of foreign tax credit carryforwards generated by the Company in prior years with those attributable to branch income generated in future years. As a result of this new provision, the U.S. Foreign Tax Credit deferred tax asset has been fully offset by a valuation allowance recorded during 2017. Because we are out of compliance with the terms of our credit facility, are operating under a forbearance agreement, and substantial doubt exists regarding our ability to continue as a going concern, we have increased the valuation allowance to include substantially all of our tax carryforward assets, or \$1.8 million during the year ended December 31, 2018. It increased by \$0.6 million during the year ended December 31, 2017 as noted above.



F-18

---

Table of Contents

Income tax provisions differed from the taxes calculated at the statutory federal tax rate as follows:

	<b>Years Ended</b>	
	<b>December 31,</b>	
	<b>2018</b>	<b>2017</b>
Federal Taxes at statutory rate	\$(589,875 )	\$(372,364)
State income taxes, net of Federal tax effect	(298,917 )	(60,695 )
Nondeductible expenses	3,859	35,083
Foreign taxes	45,552	522,803
Change in valuation allowance	1,777,768	586,706
Other	(1,681 )	-
Income tax provision	\$936,706	\$711,533

The Company files tax returns in the U.S., and in the U.K, Germany and Mexico foreign tax jurisdictions and also in various state jurisdictions in the U.S. The tax years 2015 through 2017 remain open to examination. The Company's policy is to recognize interest and penalties related to uncertain tax positions in income tax expense. As of December 31, 2018 and 2017, the Company does not believe it has any uncertain tax positions.

**Tax Reform act of 2017**

On December 22, 2017, the SEC issued Staff Accounting Bulletin No. 118 (SAB 118) which addresses income tax accounting implications of the Tax Act. The purpose of SAB 118 was to address any uncertainty or diversity of view in applying ASC Topic 740, Income Taxes in the reporting period in which the Tax Act was enacted. SAB 118 addresses situations where the accounting is incomplete for certain income tax effects of the Tax Act upon issuance of a company's financial statements for the reporting period which includes the enactment date. SAB 118 allows for a provisional amount to be recorded if it is a reasonable estimate of the impact of the Tax Act. Additionally, SAB 118 allows for a measurement period to finalize the impacts of the Tax Act, not to extend beyond one year from the date of enactment. Estimates were used in determining the balances of deferred tax assets and liabilities subject to changes in tax laws included in the Tax Act.

**12. Employee Benefit Plan**

The Company has a defined contribution plan for substantially all employees. Profit sharing contributions may be made at the discretion of the Board of Directors. Under the plan, the maximum contribution for the Company is 4% of gross wages. Employer contributions to the plan totaled none and \$47,000 for the years ended December 31, 2018 and 2017, respectively. This reduction in contribution is the result of suspending the employer contribution during 2017.



Table of Contents

**13. Related Party Transactions**

Stephen M. Merrick, Chief Executive Officer of the Company until November 2018, is of counsel to a law firm from which the Company received legal services during the year. Mr. Merrick is both a director and a shareholder of the Company. Legal fees paid to this firm were \$88,000 and \$154,000 for the years ended December 31, 2018 and 2017, respectively.

John H. Schwan, Chairman of the Board, is the brother of Gary Schwan, one of the owners of Schwan Incorporated, which provides building maintenance services to the Company. The Company made payments to Schwan Incorporated of approximately \$41,000 and \$19,000 during the years ended December 31, 2018 and 2017, respectively.

During the period from January 2003 to the present, John H. Schwan, Chairman of the Board, has made loans to the Company which have outstanding balances, for the Company of \$1,597,000 and \$1,507,000 as of December 31, 2018 and 2017, respectively. During 2018 and 2017, interest expense on these outstanding loans was \$93,000 and \$94,000, respectively.

During 2010, Schwan Leasing and Merrick Company, owned by John H. Schwan and Stephen M. Merrick, provided financing for the acquisition and construction of latex balloon production and related equipment (see Note 14).

Items identified as Notes Payable Affiliates in the Company's Consolidated Balance Sheet as of December 31, 2018 and 2017 include loans by shareholders to Flexo Universal totaling \$28,000 and \$41,000, respectively, as well as a loan to CTI Europe totaling \$32,000 and \$32,000, respectively.

**14. Variable Interest Entities (“VIE”) and Transactions**

During 2010, two entities owned by officers and/or principal shareholders of the Company (John H. Schwan and Stephen M. Merrick) provided financing for Flexo Universal, the Company's Mexico subsidiary, for the acquisition and construction of latex balloon production and related equipment. The entities included Venture Leasing L.L.C., (“VLUS”), an Illinois limited liability company which is 100% owned by an entity owned by Mr. Schwan and Mr. Merrick, and Venture Leasing Mexico S. A. de R. L (“VLM”), a Mexico company which is also owned 100% by entities owned by Mr. Schwan and Mr. Merrick. The Company is the primary beneficiary of VLUS & VLM and accordingly

consolidated the result of the entities in its financial statements.

Mr. Schwan and Mr. Merrick, through entities owned by them, arranged for a line of credit in the amount of \$1,000,000 from Barrington Bank in order to loan monies to VLUS as needed. During 2010, VLUS received advances on this line totaling \$700,000. VLUS loaned substantially all of these funds to VLM. VLM utilized the funds to purchase materials, parts, components and services for the acquisition and construction of balloon production and related equipment to be placed at the premises of Flexo Universal. Assembly and construction of this equipment was completed on or about December 31, 2010 and, in January 2011, the equipment was placed in service at Flexo Universal.

The Company has not provided any guarantees related to VLUS or VLM and no creditors of the variable interest entities have recourse to the general credit of the Company as a result of including VLUS & VLM in the consolidated financial statements. The accounts of VLM and VLUS have been consolidated with the accounts of the Company. On May 31, 2016, Flexo Universal purchased the equipment from VLM for 8,700,000 in Mexican Pesos and the lease was terminated.

F-20

---

Table of Contents

Mr. Schwan and Mr. Merrick are partial owners of Clever Container, an Illinois limited liability company engaged in the sale and distribution through a network of independent distributors, of household items including containers and organizing products. Together they own roughly half of Clever Container. The Company acquired a 28.5% interest in Clever Container from third parties in 2016. The Company produces and sells certain container products to Clever Container and also purchases and re-sells products to Clever Container. By reason of the level of ownership of Clever Container by two principal officers and/or shareholders of the Company, the ownership interest of the Company in Clever Container and the transactions among the Company and Clever Container, the determination was made to consolidate the results of Clever Container in the consolidated financial statements of the Company commencing as of October 1, 2013.

During the twelve months ended December 31, 2018 and 2017, Clever Container purchased various products from the Company in the amount of \$858,000 and \$955,000, respectively. As of December 31, 2018 and 2017, the balance of accounts receivable from Clever Container to the Company were \$1,352,000 and \$988,000, respectively.

During November 2018, the Company announced its intent to divest its interest in Clever Container. During February 2019, the Company agreed in principle to sell its 28.5% interest in Clever Container to Messrs. Schwan and Merrick in exchange for their 30% ownership (combined) of CTI Europe. Due to this transaction and an ongoing reduction in involvement between the entities, the Company intends to deconsolidate Clever Container during 2019. As a result of these subsequent events and expected deconsolidation, the Company performed a valuation of its investment with respect to Clever Container. The Company recognized an impairment of equity interest in Clever Container of \$0.2 million in 2018.

The following sets forth the condensed balance sheet of VLM, VLUS and Clever Container for December 31, 2018 and 2017.

	<b>Dec. 31, 2018</b>	<b>Dec. 31, 2017</b>
Current Assets	\$490,000	\$608,000
Property, plant and equipment, net	200,000	231,000
Other noncurrent assets	800,000	740,000
Total assets	\$1,490,000	\$1,579,000
Mortgages and other debt payable	\$2,133,000	\$2,062,000
Total liabilities	\$2,133,000	\$2,062,000

**15. Goodwill**

Under the provisions of U.S. GAAP, goodwill is subject to at least annual assessments for impairment by applying a fair-value based test. U.S. GAAP also requires that an acquired intangible asset should be separately recognized if the benefit of the intangible asset is obtained through contractual or other legal rights, or if the asset can be sold, licensed, rented or exchanged, regardless of the acquirer's intent to do so.

The Company has determined that the fair value of goodwill was not impaired as of December 31, 2018 and 2017.

F-21

---

Table of Contents**16. Commitments***Operating Leases*

In August 2015, the Company's United Kingdom subsidiary entered into a 5-year lease agreement to rent approximately 9,000 square feet of warehouse and office space in Rugby, England for \$6,000 per month.

In November 2016, CTI Europe entered into a lease agreement for 13,000 square feet of office and warehouse space in Heusenstamm, Germany for a term commencing on February 1, 2017 and ending on February 1, 2022 at the rate per month of \$9,000. A prior lease for space in Heusenstamm was terminated on February 1, 2017.

In August 2011, Flexo Universal entered into a 5-year lease to rent 73,000 square feet of warehouse and office space in Guadalajara, Mexico at the cost of \$22,000 per month. The lease was extended to February 28, 2017. Effective March 1, 2017, Flexo Universal entered into a five year lease for these premises at a cost of 493,090 Mexican Pesos per month (approximately \$26,000 per month).

In September 2012, we entered into a lease agreement, expiring on February 28, 2017 to rent approximately 118,000 square feet of warehouse and office space in Lake Zurich, Illinois. Effective March 1, 2017, this lease had been renewed for three years, at a basic rental cost per month of:

<u>Lease period</u>	Amount per month
March 1, 2018 – February 28, 2019	\$40,000
March 1, 2019 – February 28, 2020	\$42,000

All of the Company's lease payments are recognized on a straight-line basis. The net lease expense was approximately \$1.4 million for the years ended December 31, 2018 and 2017, respectively.

The future aggregate minimum net lease payments under existing agreements as of December 31 are as follows:



2019	1,437,000
2020	957,000
2021	815,000
2022	146,000
2023+	75,000
Total	\$3,430,000

F-22

---

Table of Contents*Licenses*

The Company has certain merchandising license agreements that require royalty payments based upon the Company's net sales of the respective products. The agreements call for guaranteed minimum commitments that are determined on a calendar year basis. Future guaranteed commitments due, as computed on a pro rata basis, as of December 31, are as follows:

2019	500,000
Total	\$500,000

**17. Stockholders' Equity***Stock Options*

The Compensation Committee administers the stock-based plans. The exercise price for Incentive Stock Options ("ISO") cannot be less than the fair value of the stock subject to the option on the grant date (110% of such fair value in the case of ISOs granted to a stockholder who owns more than 10% of the Company's Common Stock). The exercise price of a Non-Qualified Stock Options ("NQSO") shall be fixed by the Compensation Committee at whatever price the Committee may determine in good faith. Unless the Committee determines otherwise, options beginning with the 2009 Plan generally had a 4-year term with a 3-year vesting schedule. Unless the Committee provides otherwise, options terminate upon the termination of a participant's employment, except that the participant may exercise an option to the extent it was exercisable on the date of termination and for a period of time after termination. Officers, directors and employees of, and consultants to the Company, or any parent or subsidiary corporation selected by the Committee, are eligible to receive options under the Plan. Subject to certain restrictions, the Committee is authorized to designate the number of shares to be covered by each award, the terms of the award, the date on which and the rates at which options or other awards may be exercised, the method of payment, vesting and other terms.

On June 8, 2018, our shareholders approved the 2018 Stock Incentive Plan ("2018 Plan"). The 2018 Plan authorizes the issuance of up to 300,000 shares of our common stock in the form of equity-based awards. No such shares were issued as of December 31, 2018.

The Company has applied the Black-Scholes model to value stock-based awards. That model incorporates various assumptions in the valuation of stock-based awards relating to the risk-free rate of interest to be applied, the estimated dividend yield and expected volatility of the Company's Common Stock. The risk-free rate of interest is the U.S.

Treasury yield curve for periods within the expected term of the option at the time of grant. The expected volatility is based on historical volatility of the Company's Common Stock.

F-23

---

Table of Contents

The valuation assumptions we have applied to determine the value of stock-based awards were as follows:

Historical stock price volatility: The Company used the weekly closing price to calculate historical annual volatility.

Risk-free interest rate: The Company bases the risk-free interest rate on the rate payable on US treasury securities in effect at the time of the grant, which varied between 2.2% and 2.9%.

Expected life: The expected life of the option represents the period of time options are expected to be outstanding. The Company uses an expected life of 3.75 years.

Dividend yield: The estimate for dividend yield is 0%, as the Company did not issue dividends during 2018 or 2017 and does not expect to do so in the foreseeable future.

Estimated forfeitures: When estimating forfeitures, the Company considers historical terminations as well as anticipated retirements.

The Company, at the discretion of the board, may issue options in excess of the total available, if options related to that stock plan are cancelled. In some cases, not all shares that are available to a stock plan are issued, as the Company is unable to issue options to a previous plan when a new plan is in place.

The Company's pre-tax income for the fiscal year ended December 31, 2018 and 2017 includes approximately \$172,000 and \$21,000, respectively, of compensation costs related to share-based payments. As of December 31, 2018, there is \$193,000 of unrecognized compensation expense related to non-vested stock option grants. We expect approximately \$92,000, \$56,000, and \$32,000 to be recognized during 2019, 2020, and 2021 respectively.

On April 15, 2009, the Board of Directors approved for adoption, and on June 5, 2009, the shareholders of the Company approved the 2009 Stock Incentive Plan ("2009 Plan"). The 2009 Plan authorized the issuance of up to 510,000 shares of stock or options to purchase stock of the Company (including cancelled shares reissued under the plan.) As of December 31, 2017, 399,469 were outstanding, of which 26,788 were vested and 372,681 were not vested. Vesting is determined at time of grant. As of December 31, 2018, 394,469 were outstanding, of which 88,589 were vested and 305,880 were not vested.

On June 8, 2018, our shareholders approved the 2018 Stock Incentive Plan (“2018 Plan”). The 2018 Plan authorizes the issuance of up to 300,000 shares of our common stock in the form of equity-based awards.

No options were exercised during the years ended December 31, 2018 and 2017.

F-24

---

Table of Contents

The following is a summary of the activity in the Company's stock option plans and other options for the years ended December 31, 2018 and 2017, respectively:

	<b>December 31, 2018</b>		<b>December 31, 2017</b>	
	<b>Shares</b>	<b>Weighted Avg. Exercise Price</b>	<b>Shares</b>	<b>Weighted Avg. Exercise Price</b>
Exercisable, beginning of period	103,463	\$ 5.38	83,275	\$ 5.20
Vested	66,801	3.67	37,138	5.70
Exercised	-	-	-	-
Cancelled/Expired	(5,000 )	5.76	(16,950 )	5.17
Exercisable at the end of period	165,264	\$ 4.05	103,463	\$ 5.38

	<b>December 31, 2018</b>		<b>December 31, 2017</b>	
	<b>Shares</b>	<b>Weighted Avg. Exercise Price</b>	<b>Shares</b>	<b>Weighted Avg. Exercise Price</b>
Outstanding, beginning of period	476,144	\$ 3.97	143,094	\$ 5.22
Granted	-	-	350,000	3.52
Exercised	-	-	-	-
Cancelled/Expired	(5,000 )	5.76	(16,950 )	5.17
Outstanding at the end of period	471,144	\$ 3.95	476,144	\$ 3.97

On December 1, 2017, pursuant to his offer of employment with the Company as President, Mr. Jeffrey Hyland was granted 25,000 shares of restricted stock (vesting over four years), 65,000 incentive stock options (vesting over five years) and 260,000 non-qualified options (vesting over five years).

At December 31, 2018, there were 300,000 options available to grant. The above represents instruments broadly referred to as options which include non-qualified stock options, incentive stock options, grants of restricted common stock, and similar instruments.

Subsequent to the reporting period, during January 2019, and as further described in Note 21, the settlement of an arbitration proceeding resulted in the issuance of 20,000 shares of the Company's common stock. An expense for the fair value of these shares was recorded as of December 31, 2018 in the amount of approximately \$67,000.



Table of Contents**18. Earnings Per Share**

Basic earnings per share is computed by dividing net income by the weighted average number of shares of common stock outstanding during each period.

Diluted earnings per share is computed by dividing the net income by the weighted average number of shares of common stock and equivalents (stock options and warrants), unless anti-dilutive, during each period.

**Consolidated Earnings per Share**

	Year Ended December 31,	
	2018	2017
<b>Basic</b>		
Average shares outstanding:		
Weighted average number of shares outstanding during the period	3,578,885	3,568,885
<b>Earnings:</b>		
Net (loss)/income attributable to CTI Industries Corporation	\$(3,585,709)	\$(1,603,103)
Amount for per share Computation	\$(3,585,709)	\$(1,603,103)
Net (loss)/income per share applicable to Common Shares	\$(1.00 )	\$(0.45 )
<b>Diluted</b>		
Average shares outstanding:	3,578,885	3,568,885
Weighted averages shares Outstanding Common stock equivalents (options, warrants)	-	47,359
Weighted average number of shares outstanding during the period	3,578,885	3,616,244
<b>Earnings:</b>		
Net (loss)/income attributable to CTI Industries Corporation	\$3,585,709 )	\$(1,603,103)
Amount for per share computation	\$(3,585,709)	\$(1,603,103)
Net (loss)/ income per share applicable to Common Shares	\$(1.00 )	\$(0.44 )





Table of Contents**19. Product and Geographic Segment Data**

The Company's operations consist of a single business segment which designs, manufactures, and distributes film products. Transfers between geographic areas were primarily at cost plus a standard markup. The Company's subsidiaries have assets consisting primarily of trade accounts receivable, inventory and machinery and equipment. Sales and selected financial information by geographic area for the years ended December 31, 2018 and 2017, respectively, are:

	<b>United States</b>	<b>United Kingdom (UK)</b>	<b>Europe (Excluding Mexico)</b>	<b>Consolidated</b>
Year ended 12/31/18				
Sales to outside customers	\$40,554,000	\$1,438,000	\$4,731,000	\$8,868,000
Total Assets	\$25,354,000	\$879,000	\$3,052,000	\$9,476,000

	<b>United States</b>	<b>United Kingdom (UK)</b>	<b>Europe (Excluding Mexico)</b>	<b>Consolidated</b>
Year ended 12/31/17				
Sales to outside customers	\$41,165,000	\$1,908,000	\$4,142,000	\$9,022,000
Total Assets	\$27,784,000	\$923,000	\$2,989,000	\$8,288,000

The following table provides a breakdown of product net sales from operations in each of the years indicated (in thousands):

<b>Product Category</b>	<b>(000 Omitted)</b>		<b>\$</b>	<b>% of</b>	
	<b>2018</b>	<b>% of Net Sales</b>		<b>2017</b>	<b>% of Net Sales</b>
Foil Balloons	24,962	45 %	29,103	52 %	
Latex Balloons	8,793	16 %	9,400	17 %	

Vacuum Sealing Products	8,820	16	%	7,866	14	%
Film Products	2,006	4	%	2,602	4	%
Other Products	11,010	19	%	7,266	13	%
<b>Total</b>	<b>55,591</b>	<b>100.0</b>	<b>%</b>	<b>56,237</b>	<b>100.0</b>	<b>%</b>

## 20. Contingencies

In the ordinary conduct of our business, we are from time to time subject to lawsuits, investigations and claims, including environmental claims and employee-related matters. Although we cannot predict with certainty the ultimate resolution of lawsuits, investigations and claims asserted against us, including civil penalties or other enforcement actions, we do not believe that any currently pending legal proceeding or proceedings to which we are a party will have a material adverse effect on our business, financial condition or results of operations.

Table of Contents**21. Legal Proceedings**

The Company may be party to certain lawsuits or claims arising in the normal course of business. The ultimate outcome of these matters is unknown but, in the opinion of management, we do not believe any of these proceedings will have, individually or in the aggregate, a material adverse effect upon our financial condition, cash flows or future results of operation.

In July, 2017, God's Little Gift, Inc. (d\b\l)a Helium and Balloons Across America and Gary Page ("Claimants") filed an action against the Company based on disputed compensation amounts over several years. This action was resolved by mutual agreement between the parties during January 2019. Mr. Page received 20,000 shares of CTI common stock, \$5,000 in cash, and a minimum payout in his monthly royalty calculation of \$7,667 beginning March 1, 2019 and ending August 1, 2021. The Company accrued the \$0.3 million in committed costs under this settlement in its December 31, 2018 financial statements.

**Schedule II – Valuation and Qualifying Accounts:**

The following is a summary of the allowance for doubtful accounts related to accounts receivable for the years ended December 31:

	2018	2017
Balance at beginning of year	\$ 114,000	\$ 137,000
Charged to expenses	4,000	6,000
Uncollectible accounts written off	(33,000 )	(29,000 )
Balance at end of year	\$ 85,000	\$ 114,000

The following is a summary of the allowance for excess inventory for the years ended December 31:

	2018	2017
Balance at beginning of year	\$ 500,000	\$ 794,000

Charged to expenses	-	-
Excess inventory written off	(46,000 )	(294,000)
Balance at end of year	\$454,000	\$500,000

F-28

---

Table of Contents

The following is a summary of property and equipment and the related accounts of accumulated depreciation for the years ended December 31:

	2018	2017
<b>Cost Basis</b>		
Balance at beginning of year	\$31,443,000	\$38,250,000
Additions	492,000	813,697
Disposals		(7,620,697 )
Balance at end of year	\$31,935,000	\$31,443,000
<b>Accumulated depreciation</b>		
Balance at beginning of year	\$26,879,000	\$32,938,000
Depreciation	1,241,000	1,568,697
Disposals		(7,620,697 )
Balance at end of year	\$28,120,000	\$26,886,000

The following is a summary of the valuation allowance for income taxes for the years ended December 31:

<b>Deferred Tax Asset Valuation Allowance</b>	2018	2017
Beginning Balance	631,706	45,000
Additions charged (credited) to expense	1,777,768	586,706
Balance at end of year	2,409,474	631,706

**EXHIBIT INDEX**

Exhibit  
Document  
Number

Edgar Filing: CTI INDUSTRIES CORP - Form 10-K

- 3.1 Restated Articles of Incorporation (Incorporated by reference to Exhibit A to Registrant's Schedule 14A Definitive Proxy Statement filed April 29, 2015).
- 3.2 Amended and Restated By-Laws of CTI Industries Corporation (Incorporated by reference to Exhibit 3.2, contained in Registrant's Form 8-K filed on March 17, 2017).
- 4.1 Form of CTI Industries Corporation's common stock certificate (Incorporated by reference to Exhibit 4.1 contained in Registrant's Report on Form 10-K dated March 31, 2017).
- 10.1 CTI Industries Corporation 2009 Stock Incentive Plan (Incorporated by reference to Schedule A contained in Registrant's Schedule 14A Definitive Proxy Statement, as filed with the Commission on April 30, 2009).

F-29

---

Table of Contents

- 10.2 CTI Industries Corporation 2018 Stock Incentive Plan (Incorporated by Reference to Schedule A contained in Registrant's 14A Definitive Proxy Statement, as filed with the Commission on April 30, 2018)
- 10.3 Lease Agreement between Schultz Bros. Co. and the Company dated September 19, 2012 (Incorporated by reference to Exhibit 10.8 contained in Registrant's Report on Form 10-Q dated November 14, 2012).
- 10.4 Stock Purchase Warrant to Purchase Common Stock of CTI Industries Corporation (Incorporated by reference to Exhibit 10.5 contained in Registrant's Report on Form 10-Q dated August 22, 2016).
- 10.5 Registration Rights Agreement between [Purchaser] and the Company (Incorporated by reference to Exhibit 10.6 contained in Registrant's Report on Form 10-Q dated August 22, 2016).
- 10.6 Promissory Note between CTI Industries and Stephen M. Merrick dated September 30, 2016 (Incorporated by reference to Exhibit 10.1 contained in Registrant's Report on Form 10-Q dated November 14, 2016).
- 10.7 Promissory Note between CTI Industries and John H. Schwan dated September 30, 2016 (Incorporated by reference to Exhibit 10.2 contained in Registrant's Report on Form 10-Q dated November 14, 2016).
- 10.8 Employment Agreement between Jeffrey S. Hyland and the Company dated December 1, 2017 (Incorporated by reference to Exhibit 10.38 contained in Registrant's Report on Form 10-K filed on April 2, 2018).
- 10.9 Revolving Credit, Term Loan, and Security Agreement dated December 14, 2017 (Incorporated by reference to Exhibit 10.1, contained in Registrant's Form 8-K filed on December 19, 2017).
- 10.10 Revolving Credit Note dated December 14, 2017 (Incorporated by reference to Exhibit 10.2, contained in Registrant's Form 8-K filed on December 19, 2017).
- 10.11 Term Note dated December 14, 2017 (Incorporated by reference to Exhibit 10.3, contained in Registrant's Form 8-K filed on December 19, 2017).
- 10.12 Promissory Note dated December 14, 2017 (Incorporated by reference to Exhibit 10.4, contained in Registrant's Form 8-K filed on December 19, 2017).
- 10.13 Real Property Mortgage dated December 14, 2017 (Incorporated by reference to Exhibit 10.5, contained in Registrant's Form 8-K filed on December 19, 2017).
- 10.14 Subordination Agreement dated December 14, 2017 (Incorporated by reference to Exhibit 10.6, contained in Registrant's Form 8-K filed on December 19, 2017).



Table of Contents

- 10.15 Waiver and Amendment No. 1 to Revolving Credit, Term Loan and Security Agreement dated June 12, 2018 (Incorporated by reference to Exhibit 10.1, contained in Registrant's Form 8-K filed on June 12, 2018)
- 10.16 Consent and Amendment No. 2 to Revolving Credit, Term Loan and Security Agreement dated October 8, 2018 (Incorporated by reference to Exhibit 10.1, contained in Registrant's form 8-K filed on October 12, 2018)
- 10.17 Subscription Agreement among Registrant and John H. Schwan dated December 21, 2018 (Incorporated by reference to Exhibit 10.1, contained in Registrant's form 8-K filed on January 17, 2019)
- 10.18 Settlement Agreement and Release dated January 21, 2019 (filed herewith as Exhibit 10.19)
- 10.19 Amendment No.1 to Agreement among CTI, GLG, Page and H One dated January 21, 2019 (filed herewith as Exhibit 10.19)  
Amendment No. 3 and Forbearance Agreement to Revolving Credit, Term Loan and Security Agreement dated March 4, 2019 (Incorporated by reference to Exhibit 10.1, contained in Registrant's form 8-K filed on March 8, 2019)
- 14 Code of Ethics (Incorporated by reference to Exhibit contained in the Registrant's Form 10-K/A Amendment No. 2, as filed with the Commission on October 13, 2004).

F-31

---

Table of Contents

21	Subsidiaries (description incorporated in Form 10-K under Item No. 1).
23.1	Consent of Independent Registered Public Accounting Firm, Plante & Moran, PLLC.
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and rule 15d-14(a) of the Securities Exchange Act, as amended (filed herewith).
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and rule 15d-14(a) of the Securities Exchange Act, as amended (filed herewith).
32	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).
99	Audited financial statements of the Company's subsidiary, Flexo Universal, S. de R.L. de C.V. for the year ended December 31, 2018.
101	Interactive Data Files, including the following materials from the Company's Annual Report on Form 10-K for the year ended December 31, 2018, formatted in XBRL: (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Operations, (iii) the Consolidated Statements of Cash Flows, and (iv) the Notes to Consolidated Financial Statements.