Hallwood Group Inc
Form 10-K
March 31, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(MARK ONE)

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

For the fiscal year ended December 31, 2013

or

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

for the transition period from __________ to __________

Commission file number: 1-8303

The Hallwood Group Incorporated

(Exact name of registrant as specified in its charter)

Delaware	**51-0261339**
(State or Other Jurisdiction of	**(I.R.S. Employer**
Incorporation or Organization)	**Identification No.)**
3710 Rawlins, Suite 1500, Dallas, Texas	**75219**
(Address of Principal Executive Offices)	**(Zip Code)**

Registrant s telephone number, including area code: 214-528-5588

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

Title of each class	**Name of each exchange on which registered**
Common Stock, par value $0.10 per share	**NYSE MKT**

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

None

(Title of Class)

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

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

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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark if the disclosure of the delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405) 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. x

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

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

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

As of June 28, 2013, which is the last business day of the registrant s most recently-completed second fiscal quarter, the aggregate market value of voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold on the NYSE MKT, was $5,009,000.

As of the close of business on March 25, 2014, there were 1,525,166 shares of common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

The information called for by Part III of this Annual Report on Form 10-K is incorporated herein by reference to the registrant s definitive Proxy Statement for the 2014 Annual Meeting of Stockholders.

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THE HALLWOOD GROUP INCORPORATED

FORM 10-K

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Special Note Regarding Forward-Looking Statements

This Annual Report on Form 10-K (this Form 10-K), including but not limited to the section of this annual report on Form 10-K entitled Management s Discussion and Analysis of Financial Condition and Results of Operations, information concerning the Company s business prospects or future financial performance, anticipated revenues, expenses, profitability or other financial items, including the outcome of pending litigation, and its strategies, plans and objectives, together with other statements that are not historical facts, includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). Forward-looking statements generally can be identified by the use of forward-looking terminology, such as may, will, would, expect, intend, could, estim should, anticipate , doubt or believe. The Company intends that all forward-looking statements be subject to the safe harbors created by these laws. All statements other than statements of historical information provided herein are forward-looking and may contain information about financial results, economic conditions, trends, and known uncertainties. All forward-looking statements are based on current expectations regarding important risk factors. Many of these risks and uncertainties are beyond the Company s ability to control, and, in many cases, the Company cannot predict all of the risks and uncertainties that could cause actual results to differ materially from those expressed in the forward-looking statements. Actual results could differ materially from those expressed in the forward-looking statements, and readers should not regard those statements as a representation by the Company or any other person that the results expressed in the statements will be achieved. Important risk factors that could cause results or events to differ from current expectations are described under the section of this annual report on Form 10-K entitled Risk Factors and elsewhere in this annual report on Form 10-K. These factors are not intended to be an all-encompassing list of risks and uncertainties that may affect the operations, performance, development and results of the Company s business. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Company undertakes no obligation to release publicly the results of any revisions to these forward-looking statements which may be made to reflect events or circumstances after the date hereof, including without limitation, changes in its business strategy or planned capital expenditures, growth plans, or to reflect the occurrence of unanticipated events, although other risks and uncertainties may be described, from time to time, in the Company s periodic reports and filings with the Securities and Exchange Commission (the SEC).

PART I

Item 1. Business

The Hallwood Group Incorporated (the Company) (NYSE MKT: HWG) is a corporation incorporated in Delaware in 1981 and it operates as a holding company. The Company operates its principal business in the textile products industry through its wholly owned subsidiary, Brookwood Companies Incorporated (Brookwood). Information contained herein includes references to the Company and its subsidiaries (collectively, the Hallwood Group).

Hallwood Financial Proposal and Merger Agreement On November 6, 2012, the Company received a proposal (the HFL Proposal) from Hallwood Financial Limited (Parent or Hallwood Financial) to acquire all of the outstanding shares of the Company s common stock that Parent does not beneficially own at a cash purchase price of $10.00 per share. Parent is controlled by Anthony J. Gumbiner, Chairman and Chief Executive Officer of the Company and Parent currently owns 1,001,575, or 65.7%, of the issued and outstanding shares of common stock, par value $0.10 per share, of the Company (such outstanding shares, collectively, the Company Common Stock, and, each, a Share).

In November 2012, the board of directors of the Company (the Board) formed a special committee (the Special Committee), consisting of three independent directors of the Company, to evaluate the Merger (as defined below) and other alternatives available to the Company.

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On June 4, 2013, the Company announced that the Company, Parent, and HFL Merger Corporation, a Delaware corporation and a wholly owned subsidiary of the Parent (Merger Sub), entered into an Agreement and Plan of Merger (as amended by the Amendment to Agreement and Plan of Merger, dated as of July 11, 2013, and the Second Amendment to Agreement and Plan of Merger, dated as of February 7, 2014, the Merger Agreement). The Merger Agreement provides that, upon the terms and subject to the conditions set forth in the Merger Agreement, Merger Sub will merge with and into the Company (the Merger), with the Company continuing as the surviving corporation and a wholly owned subsidiary of Parent. The Special Committee unanimously determined that the transactions contemplated by the Merger Agreement (as in effect on such date), including the Merger, are advisable and in the best interests of the Company and its stockholders (other than the persons and entities associated with Mr. Gumbiner), and unanimously recommended that the Board approve and declare advisable the Merger Agreement and the transactions contemplated thereby, including the Merger, and that the Company s stockholders vote for the adoption of the Merger Agreement (as in effect on such date). Based in part on that recommendation, the Board (other than Mr. Gumbiner, who did not participate due to his interest in the Merger) unanimously (i) determined that the transactions contemplated by the Merger Agreement, including the Merger, are advisable and in the best interests of the Company and its stockholders (other than the persons and entities associated with Mr. Gumbiner), (ii) approved and declared advisable the execution, delivery and performance of the Merger Agreement and the consummation of the transactions contemplated thereby, including the Merger and (iii) resolved to recommend that the Company s stockholders vote for the adoption of the Merger Agreement. Accordingly, the Board (without Mr. Gumbiner s participation) unanimously recommended that the stockholders of the Company adopt the Merger Agreement.

On August 23, 2013, Gary L. Sample (Plaintiff) filed a purported class and derivative action in the Court of Chancery of the State of Delaware (the Delaware Court) against the parties to the Merger Agreement and certain directors and officers of the Company (collectively, the Defendants), asserting, among other things, that the original Merger Consideration (as defined below) was unfair and did not reflect the true value of the Company and all of its assets (the Sample Litigation).

On February 7, 2014, Plaintiff and the Defendants (together, the Parties) entered into a Stipulation of Settlement (the Stipulation), by and through their respective attorneys, whereby the Parties agreed that, in order to resolve the Sample Litigation, the parties to the Merger Agreement would, among other actions, amend the Merger Agreement to increase the Merger Consideration by $3.00 per share, from $10.00 per Share to $13.00 per Share, less any incentive fee and attorneys fees awarded by the Delaware Court to Plaintiff and Plaintiff s counsel in accordance with the Stipulation (the Increased Merger Consideration). The Defendants specifically deny that they have engaged in any wrongdoing, deny that they committed any violation of law, deny that they breached any fiduciary duties, and deny liability of any kind to Plaintiff, the Company, or its stockholders. The Increased Merger Consideration will be paid if the Merger is consummated pursuant to the terms of the Merger Agreement as amended by the Second Amendment to the Merger Agreement, which was entered into by the Company, Parent, and Merger Sub as of February 7, 2014 (the Second Amendment). The Delaware Court approved the Stipulation on March 28, 2014.

Pursuant to the Merger Agreement, Merger Sub will merge with and into the Company, with the Company continuing as the surviving corporation and a wholly owned subsidiary of Parent, and each share of Common Stock outstanding immediately prior to the effective time of the Merger (other than certain excluded and dissenting shares of Common Stock) will be cancelled and converted into the right to receive $12.39 in cash, without interest (the Merger Consideration) based on the settlement of the Sample Litigation. The Sample Litigation is more fully described in Item 3 of this annual report on Form 10-K, Legal Proceedings. The following excluded and dissenting shares of Common Stock will not be entitled to the Merger Consideration: (i) shares held by Parent, Merger Sub, the Company or any wholly owned subsidiary of the Company or held in the Company s treasury and (ii) shares outstanding immediately prior to the effective time of the Merger held by a stockholder who has neither voted in favor of the Merger nor consented thereto in writing and who has demanded properly in writing appraisal for such shares and otherwise properly perfected and not withdrawn or lost the right to an appraisal of such dissenting shares pursuant to Section 262 of the General Corporation Law of the State of Delaware.

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Consummation of the Merger is subject to certain other customary conditions, including, among others, (i) absence of any order or injunction prohibiting the consummation of the Merger, (ii) subject to certain exceptions, the accuracy of representations and warranties with respect to the business of the Company, (iii) each of the Company and Parent having performed their respective obligations pursuant to the Merger Agreement and (iv) the absence of a Company Material Adverse Effect, which is defined in the Merger Agreement to include the occurrence of an Event of Default under that certain Loan Agreement, dated as of March 30, 2012, among Branch Banking and Trust Company, Brookwood Companies Incorporated, the Company and the other signatories thereto, filed with the SEC as Exhibit 10.20 to the Company s Annual Report on Form 10-K for the year ended December 31, 2011.

The Company s stockholders will be asked to consider and vote on a proposal to adopt the Merger Agreement at a special meeting of stockholders. In connection therewith, the Company will file with the SEC and furnish to the Company s stockholders a proxy statement and other relevant documents. Before making any voting decision, the Company s stockholders are urged to read the proxy statement in its entirety when it becomes available and any other documents to be filed with the SEC in connection with the proposed Merger or incorporated by reference into the proxy statement because those documents will contain important information about the proposed Merger and the parties to the Merger. The Company s stockholders will be able to obtain a free copy of documents filed with the SEC at the SEC s website at http://www.sec.gov. In addition, the Company s stockholders may obtain a free copy of the Company s filings with the SEC from the Company s website at http://www.hallwood.com/hwg/SEC.php or by directing a request to: The Hallwood Group Incorporated, 3710 Rawlins, Suite 1500, Dallas, TX 75219; Attention: Investor Relations; Phone: (214) 528-5588 or (800) 225-0135.

The foregoing information only describes certain terms of the Merger Agreement, as amended, and is not a complete description of all of the parties rights and obligations under the Merger Agreement, as amended. For the complete terms, please read: (a) the Merger Agreement attached as Exhibit 2.1 to the Company s Current Report on Form 8-K filed with the SEC on June 5, 2013; (b) the Amendment to Agreement and Plan of Merger, dated as of July 11, 2013, included as Exhibit 2.1 to the Company s Current Report on Form 8-K filed with the SEC on July 12, 2013; and (c) the Second Amendment to Agreement and Plan of Merger, dated as of February 7, 2014, included as Exhibit 2.1 to the Company s Current Report on Form 8-K filed with the SEC on February 10, 2014.

The Company s shares trade on the NYSE MKT stock exchange under the symbol of HWG and closed on November 5, 2012 (the day prior to the receipt of the HFL Proposal) at $6.00 per share. The Company s shares closed on March 25, 2014 at $12.20 per share.

Going Concern As further discussed under Item 1A, Risk Factors of this annual report on Form 10-K, (i) as a holding company, the Company is dependent upon Brookwood for cash, (ii) the Company does not currently earn sufficient cash through its operations, directly or through Brookwood, to fund its ongoing operating costs or obligations, including the HFL Loan (as hereinafter defined in Item 1A Risk Factors), and (iii) Brookwood s ability to pay the Company a dividend or other advance is dependent upon circumstances that are outside of the Company s control. The Company can give no assurance that Brookwood will have the ability to satisfy the Company s cash flow needs, or that the Company would be able to obtain other sources of funding in such a circumstance, and therefore there is substantial doubt as to the Company s ability to continue as a going concern.

The Company s audited consolidated financial statements for the fiscal year ended December 31, 2013, as included in this annual report on Form 10-K, contains an audit opinion from its independent public accounting firm which includes explanatory language related to going concern resulting from the uncertainty of the payment of dividends from its subsidiary to fund the Company s ongoing operations and obligations.

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As a holding company, the Company is dependent on Brookwood to receive the cash necessary to fund its ongoing operations and its obligations. Brookwood paid $3,900,000 of dividends during 2013 to the Company. At December 31, 2013 and December 31, 2012, the Company had approximately $972,000 and $145,000, respectively, of cash and cash equivalents.

If for any reason Brookwood is unable to pay a cash dividend or other advance to the Company, the Company would be required to seek alternative sources of funding. The Company has not yet determined what, if any, sources of funding would be available to it (other than the HFL Loan, which was amended on March 26, 2014 to provide up to $3,000,000 of liquidity in 2014; for more information see Item 1A Risk Factors), but it will consider such alternatives as an additional or new facility or term loan and potential sales of assets or additional securities. No assurance can be given that any such additional sources of funding will be available to the Company.

Additionally, any payment of a dividend or advance by Brookwood to the Company is dependent on a number of other factors including compliance with the loan covenants in Brookwood s Amended and Restated Credit Facility with Branch Banking & Trust Company, the approval of Brookwood s board of directors, Brookwood s ability to meet the requirements of the Delaware corporate laws for payment of dividends, and compliance with other applicable laws and requirements. As a result, no assurance can be given that these amounts will be available when needed.

Any failure to receive from Brookwood cash required by the Company could have a material adverse effect on the Company s financial position, results of operations and cash flows and could substantially impair the Company s ability to continue as a going concern. The consolidated financial statements have been prepared assuming the Company will continue as a going concern and do not include any adjustments that might result should the Company be unable to continue as a going concern.

See below in the section entitled *Brookwood s Revolving Credit Facility* , for information describing Brookwood s credit facility that was recently amended and restated to extend its maturity date to March 30, 2016.

Textile Products. Textile products operations are conducted through Brookwood. Brookwood is an integrated textile firm that develops and produces innovative fabrics and related products through specialized finishing, treating and coating processes.

Organization. Brookwood principally operates as a converter, finisher and laminator in the textile industry, and it processes fabrics at its plants, located in Rhode Island and Connecticut, or by contracting with independent finishers. Brookwood is one of the largest coaters of woven nylons in the United States. Brookwood is known for its extensive, in-house expertise in high-tech fabric development and is a major supplier of specialty fabric to U.S. military contractors. Brookwood produces fabrics that meet standards and specifications set by both government and private industry, which are used by military, consumer and industrial customers. Brookwood has two principal subsidiaries as of December 31, 2013:

Kenyon Industries, Inc. (Kenyon). Kenyon, located in Rhode Island, uses the latest technologies and processes in dyeing, finishing, coating and printing of woven synthetic products. Kenyon provides quality finishing services for fabrics used in a variety of markets, such as military, luggage and knapsacks, flag and banner, apparel, industrial and sailcloth.

Brookwood Laminating, Inc. (Brookwood Laminating). Brookwood Laminating, located in Connecticut, uses the latest in processing technology to provide quality laminating services for fabrics used in military clothing and equipment, sailcloth, medical equipment, industrial applications and consumer apparel. Up to five layers of textile materials can be processed using both wet and dry lamination techniques.

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Raw Materials and Suppliers. The principal raw materials used by Brookwood include various untreated woven nylons, other fabrics, films, dyes and chemical compounds acquired primarily from U.S. suppliers.

Brookwood generally maintains relationships with a limited number of suppliers; however, Brookwood believes that these raw materials are available from alternative suppliers if a supplier cannot meet Brookwood s requirements. Some of Brookwood s significant suppliers include Glen Raven, Highland, Precision Fabrics Group, Inc., Schneider Mills, Inc., and Synthetic Resources.

Sales and Distribution. Brookwood s products are sold through its internal sales force in New York, Connecticut and California and a small network of independent sales representatives. Substantially all products are sold to U.S. organizations, including various customers holding or participating in military contracts.

Brookwood relies on military sales for a significant portion of its annual sales revenue. Military sales were $69,419,000, $68,091,000 and $73,906,000 in 2013, 2012 and 2011, respectively, which represented 53.7%, 52.2% and 53.0% of Brookwood s sales. Generally, military sales represent sales of a product to a customer (prime and sub-prime contractors) that will be incorporated into an end product that will be used to fulfill a U.S. or international military contract. Additionally, sales to one Brookwood customer, Tennier Industries, Inc. (Tennier), accounted for more than 10% of Brookwood s sales in 2013, 2012 and 2011. Sales to Tennier, which are included in military sales, represented 19.4%, 16.3% and 10.0% of Brookwood s sales in 2013, 2012 and 2011, respectively. While Brookwood has enjoyed substantial revenues from its military business, and while Brookwood s relationship with Tennier is ongoing, there is no assurance that such revenues from either source will continue. For further discussion of the risks associated with Brookwood s dependence on this customer and military sales, see Item 1A of this annual report on Form 10-K, Risk Factors .

Competition. The textile market remains highly competitive. Competition is principally based on product development, design, price, quality and service. Brookwood s ability to compete is enhanced by its in-house expertise and vertical integration of its product development, converting, finishing and laminating process.

Brookwood s competitive position varies by product line. There are several major domestic competitors in the synthetic fabrics business, none of which dominates the market. Brookwood believes, however, that it has a strong competitive position. In addition, Brookwood believes that it is one of a few finishers successful in printing camouflage on nylon for sale to apparel suppliers of the U.S. government. Additional competitive strengths of Brookwood include: knowledge of its customers business needs; its ability to design and produce special fabrics such as textured blends; waterproof breathable fabrics; state of the art fabric finishing equipment at its facilities; and substantial vertical integration.

Seasonality and Backlog. The textile industry historically experiences cyclical swings and backlog can be short term in nature. Brookwood has partially offset the effect of those cyclical swings by diversifying its product lines and business base. The backlog is subject to market conditions and the timing of contracts granted to its prime government contractor customers. Management believes that Brookwood maintains a level of inventory adequate to leverage its sales requirements.

Patents and Trademarks. Brookwood has and continues to obtain various patents and trademarks. Brookwood s products are sold around the world under brand-name, logo and certain trademarks. Trademark protection continues in some countries for as long as the mark is used and, in other countries, for as long as it is registered. Registrations are generally for fixed, but renewable, terms. Brookwood owns or licenses a number of U.S. and foreign utility and design patents. The utility patents involve technical fabrics as well as uses for the fabrics, formulations applied to the fabrics, and product manufacturing processes for making them. The design patents cover various camouflage designs. Patents for individual products and processes extend for varying periods according to the date of patent filing or grant and the legal term of patents in the various countries where patent protection is obtained. The actual protection afforded by a patent, which can vary from country to country, depends upon the type of patent, the scope of its coverage and the availability of legal remedies in the country.

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Brookwood has ongoing programs of research and development in all of its divisions adequate to maintain the exploration, development and production of innovative products and technologies. Research and development expenses were approximately $621,000 in 2013 and $769,000 in 2012.

Government Regulations. From time to time, the military limits orders for existing products and adopts revised specifications for new products to replace the products for which Brookwood s customers have been suppliers. The U.S. government released orders in recent years that include Brookwood s products, which resulted in significant military sales. Changes in specifications, procurement entity budgets, or orders present a potential opportunity for additional sales; however, it is a continuing challenge to adjust to changing specifications, budgetary and production requirements. Brookwood has regularly conducted research and development on various processes and products intended to comply with the revised specifications and it participates in the bidding process for new military products. However, to the extent Brookwood s products are not included in future purchases by the U.S. government for any reason, Brookwood s sales could be adversely affected. A provision of U.S. federal law, known as the Berry Amendment, generally requires the Department of Defense to give preference in procurement to domestically produced products, including textiles. Brookwood s sales of products to the U.S. military market are highly dependent upon the continuing application and enforcement of the Berry Amendment by the U.S. government. In addition, the U.S. government is releasing contracts for shorter periods than in the past. We acknowledge the unpredictability in revenues and margins due to military sales and are unable at this time to predict future sales trends.

Additionally, Kenyon and Brookwood Laminating are subject to a broad range of federal, state and local laws and regulations relating to the pollution and protection of the environment. Among the many environmental requirements applicable to Kenyon and Brookwood Laminating are laws relating to air emissions, ozone depletion, wastewater discharges and the handling, disposal and release of solid and hazardous substances and wastes, including but not limited to such laws as the Comprehensive Environmental Response Compensation and Liability Act (CERCLA), which may impose liability retroactively and without fault for releases or threatened releases of hazardous substances at on-site or off-site locations Although, based on continuing internal review and advice from independent consultants, Kenyon and Brookwood Laminating believe that they are currently in substantial compliance with applicable environmental requirements, there is financial and other risk associated with the applicability of these environmental regulations. Brookwood and its subsidiaries incurred capital expenditures to comply with environmental regulations of approximately $421,000, $572,000, and $136,000 in the years ended December 31, 2013, 2012, and 2011, respectively. For a discussion of the risks associated with compliance with government regulators and environmental laws, see Item 1A of this annual report on Form 10-K, Risk Factors .

Brookwood s business and operations are also subject to various international trade agreements and regulations such as the North American Free Trade Agreement (NAFTA) and the Central American Free Trade Agreement (CAFTA), and the activities and regulations of the World Trade Organization (WTO). The elimination of duties and/or quotas or other trade restrictions with respect to certain countries could adversely affect Brookwood as a result of increased competition from textile manufacturers in such countries. The U.S. government is engaged in discussions with a number of countries or trading blocs with the intent of further liberalizing trade. Authority to negotiate new fast track agreements has been granted by Congress, making new agreements in this field more likely.

Accordingly, Brookwood believes it must fully utilize other competitive strategies to replace sales lost to importers. One strategy is to identify new market niches. In addition to its existing products and proprietary technologies, Brookwood has developed advanced breathable, waterproof laminate and other materials, which have been well received by its customers. Continued development of these fabrics for military, industrial and consumer application is a key element of Brookwood s business plan.

Brookwood s Revolving Credit Facility. On March 30, 2012, Brookwood and its subsidiaries entered into a loan agreement by and among Brookwood, its subsidiaries and Branch Banking and Trust Company (BB&T), as subsequently amended (the Revolving Credit Facility).

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The Revolving Credit Facility provided for borrowings of up to $25,000,000 and is secured by a first lien on substantially all of the assets of Brookwood. The Revolving Credit Facility had a maturity date of March 30, 2014, however it was recently amended and restated as described below, extending the maturing date to March 30, 2016.

The interest rate on the Revolving Credit Facility was 1.165% at December 31, 2013.

Loan Covenants of the Revolving Credit Facility. The Revolving Credit Facility, as amended, required Brookwood to satisfy certain financial covenants on the last day of each fiscal quarter. As of December 31, 2013 and 2012, and for each of the quarterly periods during 2013 and 2012, Brookwood was in compliance with loan covenants of the Revolving Credit Facility.

During the year ended December 31, 2013, Brookwood made net repayments of its borrowings under the Revolving Credit Facility and the outstanding balance was $1,175,000. During the year ended December 31, 2012, Brookwood had net proceeds under the Revolving Credit Facility and the outstanding balance was $5,330,000 at December 31, 2012.

March 2014 amendment to Revolving Credit Facility. On March 28, 2014, Brookwood and its subsidiaries executed an amended and restated credit agreement with BB&T (the Amended and Restated Credit Facility). The Amended and Restated Credit Facility, which matures on March 30, 2016, allows for borrowings based generally on a percentage of eligible receivables with maximum borrowings of $25 million. Interest rates are based on LIBOR plus a margin of between 1.50% and 2.50% based upon the fixed charge coverage ratio, as defined in the Amended and Restated Credit Facility. The Amended and Restated Credit Facility contains a minimum fixed charge coverage ratio covenant and a minimum excess availability covenant, each as defined in the Amended and Restated Credit Facility. The minimum fixed charge coverage ratio is 1.10 to 1.00 and will be measured quarterly beginning with the quarter ended September 30, 2014. The minimum excess availability covenant is measured monthly. In 2014, dividends and other distributions to Hallwood are limited to $750,000 payable after September 30, 2014. In subsequent periods, Brookwood may make dividends and distributions to Hallwood as long as Brookwood is in compliance with both the minimum fixed charge coverage ratio and minimum excess availability covenants. While borrowings under the Amended and Restated Credit Facility are likely to be limited to amounts less than $25 million, management believes that it will provide adequate liquidity for Brookwood through at least December 31, 2014. Should Brookwood, at its option, terminate its factoring relationship with BB&T, the Amended and Restated Credit Facility would also terminate. Brookwood management at this time has no intention of terminating its factoring relationship with BB&T during the term of the Amended and Restated Credit Facility. As of March 28, 2014, subject to the provisions of the Amended and Restated Credit Facility and current borrowings of approximately $4 million, Brookwood had unused borrowing availability of approximately $4 million under this credit facility.

The terms of the Amended and Restated Credit Facility provide that the facility may be used for refinancing existing indebtedness, providing for working capital and financing ongoing operations and capital expenditures.

The Amended and Restated Credit Facility contains customary representations, warranties and affirmative covenants on behalf of Brookwood and also contains negative covenants which, among other things, prohibit Brookwood from any of the following (without obtaining prior BB&T written consent and with certain exceptions): (i) permitting liens (other than customary liens) to exist on any of its properties; (ii) incurring other debt other than accounts payable to trade creditors incurred in the ordinary course of business and factors; (iii) making capital expenditures in excess of $5,000,000 in any year; (iv) purchasing substantially all of the assets of another entity; (v) entering into new leases except operating leases for machinery and equipment that do not in the aggregate require payments in excess of $250,000 in any year and real estate leases in the ordinary course of business; (vi) paying dividends, or acquiring any of its stock, other than as described above in *March 2014 amendment to Revolving Credit Facility*; (vii) making loans or advances to, or guaranties for the benefit of, any person; and (viii) disposing of its assets or properties except in the ordinary course of its business.

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Payments of Dividends. Brookwood paid to the Company dividends of $1,000,000 in February 2012 and $4,000,000 in each of the years ended December 31, 2011 and 2010. In May 2012, following the Company s request for additional dividends, Brookwood requested BB&T to approve two dividends for a total amount of $9,000,000 (including the previously mentioned $8,000,000 dividend that the Company used in part to satisfy the Judgment in the Adversary Proceeding). BB&T consented to the dividends, which were paid to the Company in May 2012. Additionally, Brookwood paid dividends during 2012 to the Company of $1,000,000 and $350,000 in August and December, respectively. Brookwood paid $3,900,000 of dividends during 2013 to the Company.

In addition to the limitations described above in *March 2014 amendment to Revolving Credit Facility*, any future payments or advances would also be contingent upon the approval of Brookwood s board of directors and Brookwood s ability to meet the requirements of the Delaware corporate laws for the payment of dividends and compliance with other applicable laws and requirements.

For the three years ended December 31, 2013, textile products operations accounted for all of Hallwood Group s operating revenues. For details regarding revenue, profit and total assets, see Note 16 to the Company s consolidated financial statements.

Energy. Prior to October 29, 2009, the Company held an investment in Hallwood Energy, L.P. (Hallwood Energy) and Hallwood Energy Management, LLC, its general partner (HEM). Hallwood Energy was a privately held independent oil and gas limited partnership that operated as an upstream energy company engaged in the acquisition, development, exploration, production, and sale of hydrocarbons, with a primary focus on natural gas assets. The Company accounted for the investment in Hallwood Energy using the equity method of accounting.

Bankruptcy Reorganization by Hallwood Energy. In March 2009, Hallwood Energy, HEM and Hallwood Energy s subsidiaries filed petitions for relief under Chapter 11 of the United States Bankruptcy Code. The cases were adjudicated in the United States Bankruptcy Court for the Northern District of Texas, Dallas Division, in *In re Hallwood Energy, L.P., et al Case No. 09-31253*. The Company was only an investor in and creditor of Hallwood Energy. The bankruptcy filing did not include the Company or Brookwood. In October 2009, the Bankruptcy Court confirmed a plan of reorganization of the debtors.

Litigation. As further discussed in Item 3. of this annual report on Form 10-K, in connection with Hallwood Energy s bankruptcy proceeding, Hallwood Energy and other parties filed a number of lawsuits against the Company, its directors and various other parties. One of the lawsuits involved an acquisition and farmout agreement entered into between Hallwood Energy and FEI Shale, L.P., a subsidiary of Talisman Energy, Inc. in June 2008 and a related equity support agreement executed by the Company (the Adversary Proceeding). In July 2011, the court in the Adversary Proceeding issued Proposed Findings (as that term is defined in Item 3 of this annual report on Form 10-K, Legal Proceedings) setting forth damages totaling approximately $18,700,000, plus prejudgment and postjudgment interest. In April 2012, the United States District Court entered a final judgment (the Judgment) substantially adopting the Proposed Findings. The Company satisfied the Judgment of $21,721,000, including prejudgment and postjudgment interest in May 2012. The Adversary Proceeding was closed by the Bankruptcy Court on November 22, 2013.

Segment and Related Information. For details regarding revenue, profit (loss) and total assets, see Note 16 to the Company s consolidated financial statements.

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Number of Employees

The Company and its wholly owned Brookwood subsidiary had 439, 441, and 458 full time employees as of February 28, 2014, 2013, and 2012, respectively, comprised as follows:

	February 28,		
	2014	2013	2012
Company	7	7	7
Brookwood	432	434	451
Total	439	441	458

In March 2013, Kenyon entered into an agreement for a new three-year collective bargaining agreement with Local 1321T of the New England Joint Board of UNITE HERE! union, representing approximately 230 employees at its Rhode Island plant facility, effective from March 1, 2013 through February 28, 2016.

Available Information

The Company s Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to reports filed pursuant to Sections 13(a) and 15(d) of the Exchange Act are available on the Company s website at www.hallwood.com, as soon as reasonably practicable after such reports are electronically filed with the SEC. Additionally, the Company s Code of Business Conduct and Ethics, Whistle Blower Policy and Audit Committee Charter may be accessed through the website. Any stockholder may request a printed copy of these documents by contacting Mr. Richard Kelley, the Company s Vice President, Chief Financial Officer and Secretary, at (800) 225-0135. The Company s website and the information contained therein or connected thereto shall not be deemed to be incorporated into this annual report on Form 10-K.

Executive Officers of the Company

In addition to Mr. Gumbiner, age 69, who serves as Director, Chairman and Chief Executive Officer of the Company (see Item 10), the following individuals also serve as executive officers:

William L. Guzzetti, age 70, has served as President and Chief Operating Officer of the Company since March 2005 and as Executive Vice President from October 1989 to March 2005. He also served as President, Chief Operating Officer and a Director of the general partner of Hallwood Energy and each of the former energy affiliates from their inception until June 2009. Mr. Guzzetti had served as President, Chief Operating Officer and a Director of Hallwood Energy Corporation, formerly based in Denver, Colorado and sold in May 2001, from December 1998 until May 2001 and of its predecessors since 1985. From 1990 until its sale in 2004, Mr. Guzzetti served as President, Chief Operating Officer and a Director of Hallwood Realty, LLC (Hallwood Realty) and Hallwood Commercial Real Estate, LLC, respectively. He had served as the President and a director of Hallwood Energy Corporation, formerly based in Cleburne, Texas and sold in December 2004, from December 2002 until December 2004. He is a member of the Florida Bar and the State Bar of Texas.

Richard Kelley, age 53, assumed the positions of Vice President, Chief Financial Officer and Secretary of the Company, in December 2008. Mr. Kelley has been with the Company, or one of the Company s affiliates, since 1985. Prior to his appointment, Mr. Kelley served as the Company s Director of Human Resources since July 2004. He served as the Manager of Financial & SEC Reporting for Hallwood Realty from May 1990 to July 2004. Mr. Kelley served as the Financial Reporting Accountant from June 1985 to March 1987 and as the Manager of Financial & SEC Reporting from March 1987 to May 1990 for Hallwood Energy Corporation.

Amber M. Brookman, age 71, has served as President, Chief Executive Officer and a Director of Brookwood since 1989.

For more information, see Item 10 of this annual report on Form 10-K.

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Item 1A. Risk Factors

Investors should carefully review and consider the risks described below and the forward-looking statements contained in this annual report on Form 10-K before evaluating the Company s business or making an investment decision. The Company s business, financial condition or results of operations could be materially adversely affected by these risks. The trading price of the Company s common stock could decline due to any of these risks, and investors may lose all or part of their investment. Investors should also refer to the other information included or incorporated by reference in this annual report on Form 10-K, including the financial statements and related notes thereto. These risks and uncertainties could cause actual results and events to differ materially from those anticipated. Additional risks that the Company does not presently consider material, or of which it is not currently aware, may also have an adverse impact on the business. Also see the section of this annual report on Form 10-K entitled Special Note Regarding Forward-Looking Statements on Page 3.

Risks related to the Company

There is substantial doubt about the Company s ability to continue as a going concern.

As discussed in depth throughout this annual report on Form 10-K, (i) as a holding company, the Company is dependent upon Brookwood for cash, (ii) the Company does not currently have sufficient cash, either directly or through Brookwood, to pay its operating costs at the holding company level or the HFL Loan (described below), and (iii) Brookwood s ability to pay the Company a dividend or other advance is dependent upon circumstances that are outside of the Company s control. The Company can give no assurance that Brookwood will have the ability to satisfy the Company s cash flow needs, or that the Company would be able to obtain other sources of funding if needed, and therefore there is substantial doubt as to the Company s ability to continue as a going concern.

Any failure by Brookwood to pay dividends or tax sharing payments to the Company could have a material adverse effect on the Company s financial position, results of operations and cash flows.

As a holding company, the Company is dependent on Brookwood to receive the cash necessary to fund its ongoing operations and its obligations, including the HFL Loan. At December 31, 2013, the Company had approximately $972,000 of cash and cash equivalents, including a $1,000,000 dividend from Brookwood received in December 2013. As of December 31, 2013, the outstanding balance of the HFL Loan was $5,411,000. Any failure to receive from Brookwood cash required by the Company could have a material adverse effect on the Company s financial position, results of operations and cash flows and could substantially impair the Company s ability to continue as a going concern.

Brookwood s ability to pay dividends and tax sharing payments or make advances to the Company is contingent upon Brookwood s compliance with loan covenants and other factors, many of which are beyond the Company s control.

Brookwood s ability to pay dividends and tax sharing payments or make advances to the Company are contingent upon Brookwood s compliance with its loan covenants and is limited by the Amended and Restated Credit Facility with BB&T. This limitation could adversely affect the Company if these payments were restricted and such a restriction could substantially impair the Company s ability to continue as a going concern.

On March 28, 2014 Brookwood executed an Amended and Restated Credit Agreement, as defined and discussed below. Although Brookwood expects to have sufficient borrowing capacity in 2014, dividends and other distributions to Hallwood in 2014 are limited to $750,000 payable after September 30, 2014. In subsequent periods, Brookwood may make dividends and distributions to Hallwood as long as Brookwood is in compliance with both the minimum fixed charge coverage ratio and minimum excess availability covenants.

In addition to the limitations described in the Amended and Restated Credit Facility, any future payments or advances would also be contingent upon the approval of Brookwood s board of directors and Brookwood s ability to meet the requirements of the Delaware corporate laws for the payment of dividends and compliance with other applicable laws and requirements.

The voting power in the Company is substantially controlled by one significant stockholder, who has the ability to substantially influence the Company, and the interests of this stockholder may conflict with or differ from those of other stockholders.

Hallwood Financial, a corporation controlled by the Company s Chairman and Chief Executive Officer, Mr. Anthony J. Gumbiner, and members of his family, is its largest shareholder, with ownership representing approximately 65.7% of the Company s outstanding common stock as of March 25, 2014. Consequently, Mr. Gumbiner, through Hallwood Financial, is in a position to significantly influence any matters that are brought to a vote of the shareholders, including, but not limited to, the election of members of the Board and any action requiring the approval of shareholders, including any amendments to its governing documents, mergers or sales of all or substantially all of the Company s assets. This concentration of ownership also may delay, defer or even prevent a change in control of the Company and make some transactions more difficult or impossible without the support of Hallwood Financial. These transactions might include proxy contests, tender offers, mergers or other purchases of common stock that could give stockholders the opportunity to realize a premium over the then-prevailing market price for shares of the Company s common stock.

The Judgment in particular, and litigation in general, have been expensive and have added substantial debt to the Company, which the Company may not be able to repay without new funding, if available.

As further discussed in Item 3 of this annual report on Form 10-K, Legal Proceedings , in connection with Hallwood Energy s bankruptcy proceeding, Hallwood Energy and other parties filed a number of lawsuits against the Company, its directors and various other parties. In July 2011, the court in the Adversary Proceeding issued Proposed Findings (as that term is defined in Item 3 of this annual report on Form 10-K) setting forth damages totaling approximately $18,700,000, plus prejudgment and postjudgment interest. In April 2012, the United States District Court substantially adopted the Proposed Findings. The Company satisfied the Judgment of $21,721,000, including prejudgment and postjudgment interest, in May 2012. The Adversary Proceeding was closed by the Bankruptcy Court on November 22, 2013.

In May 2012, to fund in part the payment of the Judgment, the Company obtained the $10,000,000 HFL Loan from Hallwood Family (BVI) L.P., a limited partnership associated with Mr. Anthony J. Gumbiner, the Company s chairman, Chief Executive Officer and principal stockholder (the HFL Loan). The HFL Loan is secured by a subordinated pledge of all of the stock of Brookwood and by the Company s interest in the anticipated refunds of federal income taxes, which were approximately $4,570,000 that the Company received in 2013. In connection with the HFL Loan, a Pledge and Security Agreement and a Subordination and Intercreditor Agreement (Intercreditor Agreement) were entered into and effective May 9, 2012. The Intercreditor Agreement, among other things, subordinates any security interest or lien that Hallwood Family (BVI) L.P. may have in certain assets of the Company, including the stock of Brookwood, to BB&T. The HFL Loan bears interest at the rate of 6% per year, payable on a quarterly basis. The Company may prepay the HFL Loan at any time without penalty. The documents reflecting the HFL Loan contain representations, warranties and covenants that are typical for loans of this type. The outstanding balance on the HFL Loan was $8,747,000 at December 31, 2012.

On March 11, 2013, the promissory note associated with the HFL Loan was amended to primarily (i) extend the maturity date of the HFL Loan by two years until June 30, 2015 and (ii) provide for an additional advance of $300,000 under the promissory note, resulting in a then outstanding balance of $9,047,000.

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On May 13, 2013, the promissory note associated with the HFL Loan was amended, pursuant to a Second Amendment to Promissory Note, to convert it to a revolving credit facility, under certain conditions until December 31, 2013, to provide additional liquidity to the Company. The Company was advanced $405,000 under the HFL Loan s revolving credit facility in May 2013.

In late May 2013, the Company received a net refund of approximately $4,300,000 from the IRS of 2010 federal taxes. The proceeds of these funds were used to pay $4,000,000 towards principal and interest outstanding on the HFL Loan, with the balance retained for the Company s expenses and cash needs. As of December 31, 2013, the outstanding balance of the HFL Loan was $5,411,000.

On March 26, 2014, the promissory note associated with the HFL Loan was amended, pursuant to a Third Amendment to Promissory Note, to extend the revolving credit facility under certain conditions until December 31, 2014 to provide up to $3,000,000 in funding for general and administrative expenses of the Company. Hallwood Family (BVI) L.P. will not have any obligation to advance any additional amounts to the Company on or after December 31, 2014.

If for any reason Brookwood is unable to pay cash dividends or other advances to the Company, the Company would be required to seek alternative sources of funding. The Company has not yet determined what, if any, sources would be available to it (other than the HFL Loan, which was amended on March 26, 2014 to provide up to $3,000,000 of liquidity in 2014), but may consider such alternatives as an additional or new facility or term loan and potential sales of assets or additional securities. No assurance can be given that any such additional sources of funding will be available to the Company, which could result in the Company not being able to continue as a going concern. The consolidated financial statements have been prepared assuming the Company will continue as a going concern and do not include any adjustments that might result should the Company be unable to continue as a going concern.

The Company s success is dependent upon retaining key management personnel whose continued service is not guaranteed.

The Company is dependent upon its executive officers for strategic business direction and specialized industry experience. While the Company believes that it could find replacements for these key personnel, loss of their services could adversely affect the Company s operations.

Risks related to the Company s Textile Products Business

Brookwood relies on sales of its military products for a substantial portion of its revenue and weakness in sales of these products can lead to a significant reduction in profitability.

Military sales were $69,419,000, $68,091,000 and $73,906,000 in 2013, 2012 and 2011, respectively, which represented 53.7%, 52.2% and 53.0% of Brookwood s sales. These sales amounts were 2.0% higher in 2013 and 7.9% lower in 2012 from the respective previous years. Generally, military sales represent sales of a product to a customer (prime and sub-prime contractors) that will be incorporated into an end product that will be used to fulfill a U.S. or international military contract. While Brookwood has enjoyed substantial revenues from its military business, sales of, and orders for, such products have been volatile and difficult to predict. In fact, orders have been weak in the fourth quarter of 2013 and the first quarter of 2014 through the date of this annual report on Form 10-K resulting in weak military revenues in the first quarter of 2014. We believe that such reduction of sales and orders is due at least in part to a reduction of deployed troops and continued debate in congress and the administration regarding federal spending. If such conditions persist, orders from the military, including orders for Brookwood s products, may experience further decline which could have a material adverse effect on Brookwood s operating results and financial condition.

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Brookwood depends on a few key customers for a significant portion of its annual sales revenue, and loss of one or more of these key customers could result in a significant loss of revenues.

Sales to Tennier, a significant customer, accounted for more than 10% of Brookwood s sales in 2013, 2012 and 2011. Brookwood s relationship with Tennier is ongoing. Sales to Tennier, which are included in military sales, were $25,071,000, $21,282,000 and $13,916,000 in 2013, 2012 and 2011, respectively, which represented 19.4%, 16.3% and 10.0% of Brookwood s sales.

Brookwood continues to identify new market niches. In addition to its existing products and proprietary technologies, Brookwood has developed advanced breathable, waterproof laminate and other materials, which have been well received by its customers. Continued development of these fabrics for military, industrial and consumer applications is a key element of Brookwood s business plan. The ongoing success of Brookwood is contingent on its ability to maintain its level of military business or expand its sales of its consumer and industrial product lines. While volatile, the significant opportunities for the military product line necessitate that it be a key focus of Brookwood s sales and marketing efforts; however, during this time of relative weakness of sales and orders of military products, Brookwood is aggressively seeking new customers and opportunities for our consumer and industrial product lines. There can be no assurance that the positive results of the past can be sustained or that competitors will not aggressively seek to replace products developed by Brookwood.

Changes in military procurement practices or regulations could adversely affect Brookwood s business.

From time to time, the military limits orders for existing products and adopts revised specifications for new products to replace the products for which Brookwood s customers have been suppliers. Adjusting to changing specifications, procurement entity budgets, or orders is a continuing challenge. To the extent Brookwood s products are not included in future purchases by the U.S. government for any reason, Brookwood s sales could be adversely affected. A provision of U.S. federal law, known as the Berry Amendment, generally requires the U.S. Department of Defense to give preference in procurement to domestically produced products, including textiles. Brookwood s sales of products to the U.S. military market are highly dependent upon the continuing application and enforcement of the Berry Amendment by the U.S. government. Brookwood s management acknowledges the unpredictability in revenues and margins due to military sales and is unable at this time to predict future sales trends.

Brookwood depends upon a limited number of third-party suppliers for raw materials, and the loss of certain suppliers could adversely affect Brookwood s business.

As discussed in Item 1 of this annual report on Form 10-K, Brookwood purchases a significant amount of the fabric and other materials it processes and sells from a small number of suppliers, some of which compete with Brookwood, targeting specific military specifications. The loss of certain of Brookwood s suppliers could adversely affect Brookwood s business unless or until alternative supply arrangements were secured. In addition, if Brookwood were able to secure alternative arrangements, there can be no assurance that such arrangements would include terms as favorable to Brookwood as those contained in Brookwood s current supply arrangements.

Brookwood s factoring agreements expose it to credit risks, which could result in an adverse effect on Brookwood s business, operating results and financial condition.

Brookwood maintains factoring agreements with several factors, which provide that receivables resulting from credit sales to customers, excluding the U.S. government, may be assigned for collection to the factor, subject to a commission and the factor s prior approval. While factoring credit sales helps to mitigate credit risk related to specific customers, the factoring agreements expose Brookwood to credit risk of the factors if any of them fail to meet their respective obligations. Brookwood seeks to manage this risk by conducting business with a number of reputable factors and monitoring the factors performance under their agreements, but there is no guarantee that such factors will have the ability to fulfill their obligations to Brookwood in a timely manner, which failure could have a material adverse effect on the Company.

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Brookwood s ability to comply with its Amended and Restated Credit Facility is subject to future performance and other factors.

On March 28, 2014, Brookwood and its subsidiaries executed an amended and restated credit agreement with BB&T (the Amended and Restated Credit Facility). The Amended and Restated Credit Facility, which matures on March 30, 2016, allows for borrowings based generally on a percentage of eligible receivables with maximum borrowings of $25 million. Interest rates are based on LIBOR plus a margin of between 1.50% and 2.50% based upon the fixed charge coverage ratio, as defined in the Amended and Restated Credit Facility. The Amended and Restated Credit Facility contains a minimum fixed charge coverage ratio covenant and a minimum excess availability covenant, each as defined in the Amended and Restated Credit Facility. The minimum fixed charge coverage ratio is 1.10 to 1.00 and will be measured quarterly beginning with the quarter ended September 30, 2014. The minimum excess availability covenant is measured monthly. In 2014, dividends and other distributions to Hallwood are limited to $750,000 payable after September 30, 2014. In subsequent periods, Brookwood may make dividends and distributions to Hallwood as long as Brookwood is in compliance with both the minimum fixed charge coverage ratio and minimum excess availability covenants. While borrowings under the Amended and Restated Credit Facility are likely to be limited to amounts less than $25 million, management believes that it will provide adequate liquidity for Brookwood through at least December 31, 2014. Should Brookwood, at its option, terminate its factoring relationship with BB&T, the Amended and Restated Credit Facility would also terminate. Brookwood management at this time has no intention of terminating its factoring relationship with BB&T during the term of the Amended and Restated Credit Facility. As of March 28, 2014, subject to the provisions of the Amended and Restated Credit Facility and current borrowings of approximately $4 million, Brookwood had unused borrowing availability of approximately $4 million under this credit facility.

The strength of Brookwood s competitors may impact its ability to maintain and grow sales, which could decrease revenues.

The cyclical nature of the textile and apparel industries, characterized by rapid shifts in military procurement, fashion and consumer demand and competitive pressures, results in volatility in both price and demand. The demand for any particular product varies from time to time based largely upon changes in military specifications, consumer and industrial preferences, and general economic conditions affecting the textile and apparel industries, such as consumer expenditures for non-durable goods. The textile and apparel industries are also cyclical because the supply of particular products changes as competitors enter or leave the market.

Brookwood sells primarily to domestic manufacturers, some of which operate offshore sewing operations. Some of Brookwood s customers have moved their business offshore. Brookwood has responded by shipping fabric Asia to Asia and also by supplying finished products directly to manufacturers. Brookwood competes with numerous domestic and foreign fabric manufacturers, including companies larger in size and having greater financial resources than Brookwood. The principal competitive factors in the woven fabrics markets are price, service, delivery time, quality and flexibility, with the relative importance of each factor depending upon the needs of particular customers and the specific product offering.

There are an increasing number of competitors entering the military market. These competitors vary and include converters from other market segments, as well as major mills, some of which are Brookwood suppliers, who are selectively targeting specific military specifications. As these companies enter the military market, the competitive pressures may result in further price and demand volatility, which could decrease Company revenues.

Brookwood is subject to many environmental regulations that may result in significant costs or liabilities or cause interruptions in its operations.

Kenyon and Brookwood Laminating are subject to a broad range of federal, state and local laws and regulations relating to the pollution and protection of the environment. Among the many environmental requirements applicable to Kenyon and Brookwood Laminating are laws relating to air emissions, ozone

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depletion, wastewater discharges and the handling, disposal and release of solid and hazardous substances and wastes. Kenyon and Brookwood Laminating are also subject to such laws as CERCLA, which may impose liability retroactively and without fault for releases or threatened releases of hazardous substances at on-site or off-site locations. Actions by federal, state and local governments concerning environmental matters could result in laws or regulations that could increase the cost of producing the products manufactured by Kenyon and Brookwood Laminating or otherwise adversely affect demand for their products. Widespread adoption of any prohibitions or restrictions could adversely affect the ability to produce products and the cost of such products, and thus have a material adverse effect upon Kenyon, Brookwood Laminating, Brookwood, and the Company.

Some risk of environmental liability is inherent in the nature of Brookwood s business. There can be no assurance that material environmental liabilities will not arise. It is also possible that future developments in environmental regulation could lead to significant environmental compliance or cleanup costs.

Brookwood s business could lose a significant competitive advantage if it fails to adequately protect its intellectual property rights.

Brookwood considers its patents and trademarks, in the aggregate, to be important to its business and seeks to protect this proprietary know-how in part through U. S. patent and trademark registrations. No assurance can be given, however, that such protection will give Brookwood any material competitive advantage. In addition, Brookwood maintains certain trade secrets for which, in order to maintain the confidentiality of such trade secrets, it has not sought patent or trademark protection. As a result, such trade secrets could be infringed upon and such infringement could have a material adverse effect on its business, results of operations, financial condition or competitive position.

Changes in international trade regulations could adversely affect Brookwood s competitive position and have a material adverse effect on its business, results of operations or financial condition.

Imports of foreign-made textile and apparel products are a significant source of competition for most sectors of the domestic textile industry. Changes in international trade regulation, including future trade agreements, could provide Brookwood s competitors an advantage, increase Brookwood s costs, limit the countries from which it can purchase raw materials and set quotas on products that may be imported from a particular country, any of which could have a material adverse effect on Brookwood s business, results of operations or financial condition.

Brookwood s success is dependent upon retaining key management personnel whose continued service is not guaranteed.

Brookwood is dependent upon its executive officers for strategic business direction and specialized industry experience. While the Company believes that it could find replacements for these key personnel, the loss of their services could adversely affect Brookwood s operations.

Risks Related to the Merger

The Merger is subject to various closing conditions described in Item 1 of this annual report on Form 10-K and other uncertainties, and there can be no assurances as to whether or when it may be completed. We cannot predict with certainty whether or when any of the required closing conditions will be satisfied or if other uncertainties may arise, as some of the conditions to close the Merger are outside of our control. In addition, third parties, such as regulators and lenders, could impose requirements or obligations as conditions for their approvals which could delay or increase the cost of the Merger and otherwise negatively impact our performance and financial condition. Despite our best efforts, we may not be able to satisfy or receive in a timely fashion the various closing conditions and obtain the necessary approvals, and such failure or delay in completing the Merger may cause uncertainty or other negative consequences that may materially and adversely affect our performance, financial condition, results of operations, and price per share of our common stock.

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Failure to complete the Merger could materially impact our business, financial condition, results of operations, stock price, and cash flows. There is no assurance that the Merger will consummated at all, or that any event, change or other circumstances will not occur that could give rise to the termination of the Merger Agreement. If the Merger is not consummated for any reason, we will be subject to several risks, including without limitation, (i) the price of our common stock may decline if the Merger does not occur; (ii) we will remain liable for significant transaction costs that would be payable even if the Merger is not consummated; and (iii) we will not have enough cash to meet the needs of the Company as a going concern. For these and other reasons, failure to consummate the Merger would adversely impact our business, financial condition, results of operations, stock price, and cash flows.

Our executive officers and directors may have interests that are different from, or in addition to, those of our stockholders generally. For example, our shareholders should be aware that Mr. Gumbiner has interests in the Merger that are different to those of our stockholders. Further, certain executives may receive severance and other payments in the event of the Merger or if their employment is terminated following consummation of the Merger. The interests of our directors and executive officers in the proposed Merger will be described in more detail in the definitive proxy statement regarding the proposed Merger that we will file with the SEC.

Item 1B. Unresolved Staff Comments

Not applicable.

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Item 2. Properties

Real Properties

The general character, location and nature of the significant real properties owned by the Company and its subsidiaries and the encumbrances against such properties are described below.

Cost of real estate owned by property type, segment and location as of December 31, 2013 (in thousands):

Property Type	Segment	Location	Cost
Dyeing and finishing plant (Kenyon)	Textile	Rhode Island	$ 9,287
Production facility (Plainfield)	Textile	Connecticut	5,537
Total			$ 14,824

The Kenyon dyeing and finishing plant is a multi-shift facility well-suited for that particular business. The development of new products and varying levels of utilization require the plant to be regularly upgraded. The Brookwood capital stock is pledged as collateral under its Amended and Restated Credit Facility and the plant is encumbered by a negative pledge under this facility. In addition, the Amended and Restated Credit Facility also contains a covenant to reasonably maintain property and equipment.

Brookwood Laminating has occupied its Plainfield facility since 2006 and purchased this facility in May 2010 pursuant to a lease purchase option. Brookwood Laminating has updated and customized the facility with building improvements and equipment to develop new products and enhance production efficiencies. Similar to the Kenyon plant, the Brookwood capital stock is pledged under the Amended and Restated Credit Facility and the plant is encumbered by a negative pledge.

Additionally, the HFL Loan is secured by a subordinated pledge of all the stock of Brookwood. For further discussion of the Revolving Credit Facility and the HFL Loan, see Item 7 of this annual report on Form 10-K, Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources.

Leased Facilities

The Company has a lease obligation for office space in Dallas, Texas, which expires in November 2015 and included a one-time option for the Company to terminate the lease in November 2012. Since January 2005, the Company has shared its Dallas office space with Hallwood Investments Limited (HIL), an entity associated with Mr. Gumbiner, the Company s Chairman, Chief Executive Officer and principal stockholder, and certain of HIL s affiliates. In addition, from August 2005 u