NAPCO SECURITY SYSTEMS INC
Form 10-K
September 30, 2008

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 June 30, 2008

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 0-10004

NAPCO SECURITY SYSTEMS, INC.
(Exact name of Registrant as specified in its charter)

Delaware	11-2277818
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer I.D. Number)
333 Bayview Avenue, Amityville, New York	11701
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (631) 842-9400

Securities registered pursuant to Section 12(b) of the Act: Common Stock, par value $.01 per share
(Title of Each Class)

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 [X]

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the 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 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 or a smaller reporting company. See

definition 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 [X] Non-accelerated filer [_] Smaller reporting company [_]

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

As of December 31, 2007, the aggregate market value of the common stock of Registrant held by non-affiliates based upon the last sale price of the stock on such date was $81,898,250.

As of September 29, 2008, 19,095,713 shares of common stock of Registrant were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Part III incorporates information by reference from the Registrant's definitive proxy statement to be filed with the Securities and Exchange Commission in connection with the solicitation of proxies for the Registrant's 2008 Annual Meeting of Stockholders.

PART I

ITEM 1: BUSINESS.

NAPCO Security Systems, Inc. ("NAPCO" or the "Company") was incorporated in December 1971 in the State of Delaware. Its executive offices are located at 333 Bayview Ave, Amityville NY 11701. Its telephone number is (631) 842-9400.

The Company is a diversified manufacturer of security products, encompassing intrusion and fire alarms, building access control systems and electronic locking devices. These products are used for commercial, residential, institutional, industrial and governmental applications, and are sold worldwide principally to independent distributors, dealers and installers of security equipment. On August 18, 2008, the Company acquired substantially all of the assets and business of G. Marks Hardware, Inc. ("Marks") for $25 million, the repayment of $1 million of bank debt and the assumption of certain current liabilities. The Marks business involves the manufacturing and distribution of door-locking devices.

Website Access to Company Reports

Copies of our filings under the Securities Exchange Act of 1934 (including annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to these reports) are available free of charge on our website (www.napcosecurity.com) on the same day they are electronically filed with the Securities and Exchange Commission.

Products

Access Control Systems. Access control systems consist of one or more of the following: various types of identification readers (e.g. card readers, hand scanners, etc.), a control panel, a PC-based computer and electronically activated door-locking devices. When an identification card or other identifying information is entered into the reader, the information is transmitted to the control panel/PC which then validates the data and determines whether to grant

access or not by electronically deactivating the door locking device. An electronic log is kept which records various types of data regarding access activity.

The Company designs, engineers, manufactures and markets the software and control panels discussed above. It also buys and resells various identification readers, PC-based computers and various peripheral equipment for access control systems.

Alarm Systems. Alarm systems usually consist of various detectors, a control panel, a digital keypad and signaling equipment. When a break-in occurs, an intrusion detector senses the intrusion and activates a control panel via hard-wired or wireless transmission that sets off the signaling equipment and, in most cases, causes a bell or siren to sound. Communication equipment such as a digital communicator may be used to transmit the alarm signal to a central station or another person selected by a customer.

The Company manufactures and markets the following products for alarm systems:

Automatic Communicators. When a control panel is activated by a signal from an intrusion detector, it activates a communicator that can automatically dial one or more pre-designated telephone numbers. If programmed to do so, a digital communicator dials the telephone number of a central monitoring station and communicates in computer language to a digital communicator receiver, which prints out an alarm message.

Control Panels. A control panel is the "brain" of an alarm system. When activated by any one of the various types of intrusion detectors, it can activate an audible alarm and/or various types of communication devices. For marketing purposes, the Company refers to its control panels by the trade name, generally "Gemini(TM)" and "Magnum Alert(TM)" followed by a numerical designation.

Combination Control Panels/Digital Communicators and Digital Keypad Systems. A combination control panel, digital communicator and a digital keypad (a plate with push button numbers as on a telephone, which eliminates the need for mechanical keys) has continued to grow rapidly in terms of dealer and consumer preference. Benefits of the combination format include the cost efficiency resulting from a single microcomputer function, as well as the reliability and ease of installation gained from the simplicity and sophistication of micro-computer technology.

Door Security Devices. The Company manufactures a variety of exit alarm locks including simple dead bolt locks, door alarms and microprocessor-based electronic door locks with push button and card reader operation.

Fire Alarm Control Panel. Multi-zone fire alarm control panels, which accommodate an optional digital communicator for reporting to a central station, are also manufactured by the Company.

Area Detectors. The Company's area detectors are both passive infrared heat detectors and combination microwave/passive infrared detectors that are linked to alarm control panels. Passive infrared heat detectors respond to the change in heat patterns caused by an intruder moving within a protected area. Combination units respond to both changes in heat patterns and changes in microwave patterns occurring at the same time.

Peripheral Equipment

The Company also markets peripheral and related equipment manufactured by other companies. Revenues from peripheral equipment have not been significant.

Research and Development

The Company's business involves a high technology element. During the fiscal years ended June 30, 2008, 2007, and 2006, the Company expended approximately $5,500,000, $5,319,000, and $5,109,000, respectively, on Company-sponsored research and development activities conducted by its engineering department to develop and improve the Products. The Company intends to continue to conduct a significant portion of its future research and development activities internally.

Employees

As of June 30, 2008, the Company had approximately 817 full-time employees.

Marketing

The Company's staff of 46 sales and marketing support employees located at the Company's Amityville, United Kingdom and Dubai offices sells and markets the Products primarily to independent distributors and wholesalers of security alarm and security hardware equipment. Management estimates that these channels of distribution represented approximately 63% and 65% of the Company's total sales for the fiscal years ended June 30, 2008 and 2007, respectively. The remaining revenues are primarily from alarm installers and governmental institutions. The Company's sales representatives periodically contact existing and potential customers to introduce new products and create demand for those as well as other Company Products. These sales representatives, together with the Company's technical personnel, provide training and other services to wholesalers and distributors so that they can better service the needs of their customers. In addition to direct sales efforts, the Company advertises in technical trade publications and participates in trade shows in major United States and European cities. Some of the Company's products are marketed under the "private label" of certain customers.

In the ordinary course of the Company's business the Company grants extended payment terms to certain customers. Those customers have materially complied with the extended payment terms. For further discussion on Accounts Receivable and Concentration of Credit Risk see disclosures included in Item 7.

Competition

The security alarm products industry is highly competitive. The Company's primary competitors are comprised of approximately 20 other companies that manufacture and market security equipment to distributors, dealers, central stations and original equipment manufacturers. The Company believes that no one of these competitors is dominant in the industry. Certain of these companies have substantially greater financial and other resources than the Company.

The Company competes primarily on the basis of the features, quality, reliability and pricing of, and the incorporation of the latest innovative and technological advances into, its Products. The Company also competes by offering technical support services to its customers. In addition, the Company competes on the basis of its expertise, its proven products, its reputation and its ability to provide Products to customers on a timely basis. The inability of the Company to compete with respect to any one or more of the aforementioned factors could have an adverse impact on the Company's business. Relatively low-priced

"do-it-yourself" alarm system products have become available in recent years and are available to the public at retail stores. The principal components in the Company's products are integrated circuits, printed circuit boards, microprocessors, sheet metal, plastic resin, machined and cast metal components. The Company believes that these products compete with the Company only to a limited extent because they appeal primarily to the "do-it-yourself" segment of the market. Purchasers of such systems do not receive professional consultation, installation, service or the sophistication that the Company's Products provide.

Seasonality

The Company's fiscal year begins on July 1 and ends on June 30. Historically, the end users of Napco's products want to install its products prior to the summer; therefore sales of its products peak in the period April 1 through June 30, the Company's fiscal fourth quarter, and are reduced in the period July 1 through September 30, the Company's fiscal first quarter. To a lesser degree, sales in Europe are also adversely impacted in the Company's first fiscal quarter because of European vacation patterns, i.e., many distributors and installers are closed for the month of August. In addition, demand is affected by the housing and construction markets.

Raw Materials

The Company prepares specifications for component parts used in the Products and purchases the components from outside sources or fabricates the components itself. These components, if standard, are generally readily available; if specially designed for the Company, there is usually more than one alternative source of supply available to the Company on a competitive basis. The Company generally maintains inventories of all critical components. The Company for the most part is not dependent on any one source for its raw materials.

Sales Backlog

In general, orders for the Products are processed by the Company from inventory. A sales backlog of approximately $1,750,000 and $965,000 existed as of June 30, 2008 and 2007, respectively.

Government Regulation

The Company's telephone dialers, microwave transmitting devices utilized in its motion detectors and any new communication equipment that may be introduced from time to time by the Company must comply with standards promulgated by the Federal Communications Commission ("FCC") in the United States and similar agencies in other countries where the Company offers such products, specifying permitted frequency bands of operation, permitted power output and periods of operation, as well as compatibility with telephone lines. Each new Product that is subject to such regulation must be tested for compliance with FCC standards or the standards of such similar governmental agencies. Test reports are submitted to the FCC or such similar agencies for approval. Cost of compliance with these regulations has not been material.

Patents and Trademarks

The Company has been granted several patents and trademarks relating to the Products. While the Company obtains patents and trademarks as it deems appropriate, the Company does not believe that its current or future success is dependent on its patents or trademarks.

Foreign Sales

The revenues and identifiable assets attributable to the Company's domestic and foreign operations for its last three fiscal years, are summarized in the

following table:

Financial Information Relating to Domestic and Foreign Operations

	2008	2007
		(in thousands)
Sales to external customers(1):		
Domestic	$56,122	$56,810
Foreign	12,245	9,392
Total Net Sales	$68,367	$66,202
Identifiable assets:		
United States	$50,056	$47,636
Dominican Republic (2)	19,841	21,246
Other foreign countries	6,826	7,903
Total Identifiable Assets	$76,723	$76,785

(1) All of the Company's sales originate in the United States and are shipped primarily from the Company's facilities in the United States and United Kingdom. There were no sales into any one foreign country in excess of 10% of total Net Sales.

(2) Consists primarily of inventories ($14,754,000) and fixed assets ($4,970,000) located at the Company's principal manufacturing facility in the Dominican Republic.

ITEM 1A: RISK FACTORS.

The risks described below are among those that could materially and adversely affect the Company's business, financial condition or results of operations. These risks could cause actual results to differ materially from historical experience and from results predicted by any forward-looking statements related to conditions or events that may occur in the future.

Our Business Could Be Materially Adversely Affected as a Result of General Economic and Market Conditions

We are subject to the effects of general economic and market conditions. If these conditions deteriorate, our business, results of operations or financial condition could be materially adversely affected.

Our Business Could Be Materially Adversely Affected as a Result of Housing Market Conditions

We are subject to the effects of housing market conditions. If these conditions deteriorate, resulting in the decline in new housing starts, existing home sales or existing home renovations, our business, results of operations or financial

condition could be materially adversely affected, particularly in our intrusion product lines.

Our Business Could Be Materially Adversely Affected as a Result of Lessening Demand in the Security Market

Our revenue and profitability depend on the overall demand for our products. Delays or reductions in spending, domestically or internationally, for electronic security systems could materially adversely affect demand for our products, which could result in decreased revenues or earnings.

The Markets We Serve Are Highly Competitive and We May Be Unable to Compete Effectively

We compete with approximately 20 other companies that manufacture and market security equipment to distributors, dealers, control stations and original equipment manufacturers. Some of these companies may have substantially greater financial and other resources, than the Company. The Company competes primarily on the basis of the features, quality, reliability and pricing of, and the incorporation of the latest innovative and technological advances into, its products. The Company also competes by offering technical support services to its customers. In addition, the Company competes on the basis of its expertise, its proven products, its reputation and its ability to provide products to customers on a timely basis. The inability of the Company to compete with respect to any one or more of the aforementioned factors could have an adverse impact on the Company's business.

Our Business Could be Materially Adversely Affected as a result of Offering Extended Payment Terms to Customers

We regularly grant credit terms beyond 30 days to our customers. These terms are offered in an effort to keep a full line of our products in-stock at our customers locations. The longer terms that are granted, the more risk is inherent in collection of those receivables. We believe that our Bad Debt reserves are adequate to account for this inherent risk.

Competitors May Develop New Technologies or Products in Advance of Us

Our business may be materially adversely affected by the announcement or introduction of new products and services by our competitors, and the implementation of effective marketing or sales strategies by our competitors. There can be no assurance that competitors will not develop products that are superior to the Company's products. Further, there can be no assurance that the Company will not experience additional price competition, and that such competition may not adversely affect the Company's position and results of operations.

The Company's Products are Subject to Technological Changes from Time to Time, Which may Result in Increased Research and Developments Expenditures to Attract or Retain Customers

The industry in which the Company operates is characterized by constantly improved products. Future success will depend, in part, on our ability to continue to develop and market products and product enhancements cost-effectively, which will require continued expenditures for product engineering, sales and marketing. The Company's research and development expenditures, which were $5,500,000 and $5,319,000 for 2008 and 2007, respectively, are principally targeted at enhancing existing products, and to a lesser extent at developing new ones. If the Company cannot modify its products to meet its customers' changing needs, we may lose sales.

We Rely On Distributors To Sell Our Products And Any Adverse Change In Our Relationship With Our Distributors Could Result In A Loss Of Revenue And Harm Our Business.

We distribute our products primarily through independent distributors and wholesalers of security alarm and security hardware equipment. Our distributors and wholesalers also sell our competitors' products, and if they favor our competitors' products for any reason, they may fail to market our products as effectively or to devote resources necessary to provide effective sales, which would cause our results to suffer. In addition, the financial health of these distributors and wholesalers and our continuing relationships with them are important to our success. Some of these distributors and wholesalers may be unable to withstand adverse changes in business conditions. Our business could be seriously harmed if the financial condition of some of these distributors and wholesalers substantially weakens.

Members of Management and Certain Directors Beneficially Own a Substantial Portion of the Company's Common Stock and May Be in a Position to Determine the Outcome of Corporate Elections

Richard L. Soloway, our Chief Executive Officer, members of management and the Board of Directors beneficially own 31.4% of the currently outstanding shares of Common Stock. By virtue of such ownership and their positions with Napco, they may have the practical ability to determine the election of all directors and control the outcome of substantially all matters submitted to Napco's stockholders.

In addition, Napco has a staggered Board of Directors. Such concentration of ownership and the staggered Board could have the effect of making it more difficult for a third party to acquire, or discourage a third party from seeking to acquire, control of Napco.

We Are Dependent Upon the Efforts of Richard L. Soloway, Our Chief Executive Officer

The success of the Company is largely dependent on the efforts of Richard L. Soloway, Chief Executive Officer. The loss of his services could have a material adverse effect on the Company's business and prospects. There is currently no succession plan.

Our Business Could Be Materially Adversely Affected by an Increase in the

Exchange Rate of the Dominican Peso

We are exposed to foreign currency risks due to our significant operations in the Dominican Republic. We have significant operations in the Dominican Republic which are denominated in Dominican pesos. We are subject to the risk that currency exchange rates between the United States and the Dominican Republic will fluctuate, potentially resulting in an increase in some of our expenses when US dollars are transferred to Dominican pesos to pay these expenses.

The Company's Debt Repayments Relating to the Recent Acquisition of Marks Require Substantially Higher Cashflows

The Marks acquisition requires quarterly principal debt repayments of approximately $893,000, plus interest, that are in addition to the Company's historical cash-flow requirements. A significant decline in the Company's cashflows could put at risk the Company's ability to repay this debt as well as to failing to meet certain financial covenants within the Revolving Credit Agreement and the Term Loan.

ITEM 1B: UNRESOLVED STAFF COMMENTS.

Not applicable.

ITEM 2: PROPERTIES.

The Company owns executive offices and production and warehousing facilities at 333 Bayview Avenue, Amityville, New York. This facility consists of a fully-utilized 90,000 square foot building on a six acre plot. This six-acre plot provides the Company with space for expansion of office, manufacturing and storage capacities. The Company is planning on expanding this facility to replace the 35,000 square foot leased building as discussed below. The Company intends on moving the operations of its Marks acquisition into this expanded facility upon completion of construction of this extension. The Company believes that the move should be completed within approximately one year.

The Company leases a building of approximately 35,000 square feet in Amityville, NY. This facility provides all of the administrative, production and warehousing space for the Company's recent Marks acquisition. The lease commenced in August 2008, expires in August 2009 and provides for extensions thereafter.

The Company's foreign subsidiary located in the Dominican Republic, NAPCO/Alarm Lock Grupo International, S.A. (formerly known as NSS Caribe, S.A.), owns a building of approximately 167,000 square feet of production and warehousing space in the Dominican Republic. That subsidiary also leases the land associated with this building under a 99-year lease expiring in the year 2092. As of June 30, 2008, a majority of the Company's products were manufactured at this facility, utilizing U.S. quality control standards.

The Company's foreign subsidiary located in the United Kingdom, Napco Group Europe Ltd, leases office space of approximately 167 square feet. This lease expired in May 2008 at which time the Company obtained a month-by-month extension as it prepares to move its offices to another location of similar size and at similar terms and conditions.

The Company's joint venture located in the United Arab Emirates leases office and warehouse space of approximately 1,100 square feet. This lease expires in

February 2009 and provides for an annual renewal at substantially the same terms and conditions.

Management believes that these facilities are more than adequate to meet the needs of the Company in the foreseeable future.

ITEM 3: LEGAL PROCEEDINGS.

There are no pending or threatened material legal proceedings to which NAPCO or its subsidiaries or any of their property is subject.

In the normal course of business, the Company is a party to claims and/or litigation. Management believes that the settlement of such claims and/or litigation, considered in the aggregate, will not have a material adverse effect on the Company's financial position and results of operations.

ITEM 4: SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

Not Applicable

PART II

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

Principal Market

NAPCO's Common Stock is traded on the NASDAQ Stock Market, Global Market System, under the symbol NSSC.

The tables set forth below reflect the range of high and low sales of the Common Stock in each quarter of the past two fiscal years as reported by the NASDAQ Global Market System.

	Quarter Ended Fiscal 2008		
Common Stock	Sept. 30	Dec. 31	March 31
High	$ 6.94	$6.25	$6.45
Low	$ 5.35	$4.83	$4.65

	Quarter Ended Fiscal 2007		
Common Stock	Sept. 30	Dec. 31	March 31
High	$10.80	$6.67	$6.05
Low	$ 5.96	$5.38	$4.62

Approximate Number of Security Holders

The number of holders of record of NAPCO's Common Stock as of September 25, 2008 was 128 (such number does not include beneficial owners of stock held in nominee name).

Dividend Information

NAPCO has declared no cash dividends during the past two years with respect to its Common Stock, and the Company does not anticipate paying any cash dividends in the foreseeable future. Any cash dividends must be approved by the Company's lenders.

Equity Compensation Plan Information as of June 30, 2008

PLAN CATEGORY	NUMBER OF SECURITIES TO BE ISSUED UPON EXERCISE OF OUTSTANDING OPTIONS (a)	WEIGHTED AVERAGE EXERCISE PRICE OF OUTSTANDING OPTIONS (b)	NUM REMAI F (EXC REFLE
Equity compensation plans approved by security holders:	1,323,480	$2.80	
Equity compensation plans not approved by security holders:	__	__	
Total	1,323,480	$2.80	

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ITEM 6: SELECTED FINANCIAL DATA.

The table below summarizes selected financial information. For further information, refer to the audited consolidated financial statements and the notes thereto beginning on page FS-1 of this report.

	Fiscal Year Ended and June 30 (In thousands, except share and per sha			
	2008	2007(1)	2006(1)	
Statement of earnings data:				
Net Sales	$ 68,367	$ 66,202	$ 69,548	$
Gross Profit	20,412	23,998	26,956	
Income from Operations	3,137	6,501	9,523	
Net Income	3,718	4,217	6,119	
Cash Flow Data:				
Net cash flows provided by (used in) operating activities	3,784	(3,674)	(168)	
Net cash flows used in investing activities	(1,045)	(1,294)	(1,679)	
Net cash flows (used in) provided by financing activities	(1,722)	3,978	3,407	
Per Share Data:				
Net earnings per common share:				
Basic	$ .19	$ .21	$ .31	$

Diluted	$ .19	$ .20	$ .30	$
Weighted average common shares outstanding:				
Basic	19,263,000	19,961,000	19,785,000	1
Diluted	19,802,000	20,599,000	20,605,000	2
Cash Dividends declared per common share (3)	$ .00	$ .00	$ .00	$
Balance sheet data (4):				
Working capital	$ 41,293	$ 40,527	$ 36,321	$
Total assets	76,723	76,785	71,198	
Long-term debt	12,400	10,900	4,700	
Stockholders' equity	53,542	53,257	50,850	

(1) Certain expenses in Cost of sales have been reclassified to Selling, general and administrative expense to conform with the current years presentation.

(2) Share and per share data have been restated to reflect the effect of a 2:1 stock split effective April 2004, a 20% stock dividend effective November 2004, a 3:2 stock split effective December 2005 and a 3:2 stock split effective June 2006.

(3) The Company has never paid a dividend on its common stock. It is the policy of the Board of Directors to retain earnings for use in the Company's business. Any dividends must be approved by the Company's primary lenders.

(4) Working capital is calculated by deducting Current Liabilities from Current Assets.

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

Overview

The Company is a diversified manufacturer of security products, encompassing intrusion and fire alarms, building access control systems and electronic locking devices. These products are used for commercial, residential, institutional, industrial and governmental applications, and are sold worldwide principally to independent distributors, dealers and installers of security equipment. International sales accounted for approximately 18% of our revenues for fiscal year 2008 and 14% of revenues for fiscal year 2007.

The Company owns and operates manufacturing facilities in Amityville, New York and the Dominican Republic. A significant portion of our operating costs are fixed, and do not fluctuate with changes in production levels or utilization of our manufacturing capacity. As production levels rise and factory utilization increases, the fixed costs are spread over increased output, which should improve profit margins. Conversely, when production levels decline our fixed costs are spread over reduced levels, thereby decreasing margins.

On August 18, 2008, the Company acquired substantially all of the assets and business of G. Marks Hardware, Inc. ("Marks") for $25 million, the repayment of $1 million of bank debt and the assumption of certain current liabilities. The Marks business involves the manufacturing and distribution of door-locking devices.

The security products market is characterized by constant incremental innovation in product design and manufacturing technologies. Generally, the Company devotes 7-8% of revenues to research and development (R&D) on an annual basis. Products

resulting from our R&D investments in fiscal 2008 did not contribute materially to revenue during this fiscal year, but should benefit the Company over future years. In general, the new products introduced by the Company are initially shipped in limited quantities, and increase over time. Prices and manufacturing costs tend to decline over time as products and technologies mature.

Economic and Other Factors

The post-September 11 era has generally been characterized by increased demand for electronic security products and services. The Company believes the security equipment market is likely to continue to exhibit healthy growth, particularly in industrial sectors, due to ongoing concerns over the adequacy of security safeguards. The Company's business is also affected by the housing markets.

Seasonality

The Company's fiscal year begins on July 1 and ends on June 30. Historically, the end users of Napco's products want to install its products prior to the summer; therefore sales of its products peak in the period April 1 through June 30, the Company's fiscal fourth quarter, and are reduced in the period July 1 through September 30, the Company's fiscal first quarter. To a lesser degree, sales in Europe are also adversely impacted in the Company's first fiscal quarter because of European vacation patterns, i.e., many distributors and installers are closed for the month of August. In addition, demand is affected by the housing and construction markets.

Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in conformity with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses reported in those financial statements. These judgments can be subjective and complex, and consequently actual results could differ from those estimates. Our most critical accounting policies relate to revenue recognition; concentration of credit risk; inventories; goodwill; and income taxes.

Revenue Recognition

Revenues from merchandise sales are recorded at the time the product is shipped or delivered to the customer pursuant to the terms of sale. We report our sales levels on a net sales basis, which is computed by deducting from gross sales the amount of actual returns received and an amount established for anticipated returns and other allowances.

Our sales return accrual is a subjective critical estimate that has a direct impact on reported net sales and income. This accrual is calculated based on a history of gross sales and actual sales returns, as well as management's estimate of anticipated returns and allowances. As a percentage of gross sales, sales returns, rebates and allowances were 6%, 8% and 7% in fiscal 2008, 2007 and 2006, respectively.

Concentration of Credit Risk

An entity is more vulnerable to concentrations of credit risk if it is exposed to risk of loss greater than it would have had if it mitigated its risk through diversification of customers. Such risks of loss manifest themselves

differently, depending on the nature of the concentration, and vary in significance.

The Company had two customers with accounts receivable balances that aggregated 34% and 38% of the Company's accounts receivable at June 30, 2008 and 2007, respectively. Sales to neither of these customers exceeded 10% of net sales in any of the past three fiscal years.

In the ordinary course of business, we have established a reserve for doubtful accounts and customer deductions in the amount of $405,000 and $365,000 as of June 30, 2008 and 2007, respectively. Our reserve for doubtful accounts is a subjective critical estimate that has a direct impact on reported net earnings. This reserve is based upon the evaluation of accounts receivable agings, specific exposures and historical trends.

Inventories

Inventories are valued at the lower of cost or fair market value, with cost being determined on the first-in, first-out (FIFO) method. The reported net value of inventory includes finished saleable products, work-in-process and raw materials that will be sold or used in future periods. Inventory costs include raw materials, direct labor and overhead. The Company's overhead expenses are applied based, in part, upon estimates of the proportion of those expenses that are related to procuring and storing raw materials as compared to the manufacture and assembly of finished products. These proportions, the method of their application, and the resulting overhead included in ending inventory, are based in part on subjective estimates and approximations and actual results could differ from those estimates.

In addition, the Company records an inventory obsolescence reserve, which represents the difference between the cost of the inventory and its estimated market value, based on various product sales projections. This reserve is calculated using an estimated obsolescence percentage applied to the inventory based on age, historical trends, requirements to support forecasted sales, and the ability to find alternate applications of its raw materials and to convert finished product into alternate versions of the same product to better match customer demand. There is inherent professional judgment and subjectivity made by both production and engineering members of management in determining the estimated obsolescence percentage. For the fiscal years 2008, 2007 and 2006, charges/(recoveries) and balances in these reserves amounted to $0 and $1,200,000, $213,000 and $1,200,000; $(531,000) and $987,000, respectively. In addition, and as necessary, the Company may establish specific reserves for future known or anticipated events.

The Company also regularly reviews the period over which its inventories will be converted to sales. Any inventories expected to convert to sales beyond 12 months from the balance sheet date are classified as non-current.

Goodwill

The Company accounts for Goodwill in accordance with Statement of Financial Accounting Standards (SFAS) No. 141, Business Combinations and SFAS No. 142, Goodwill and Other Intangible Assets. These statements established accounting and reporting standards for acquired goodwill and other intangible assets. Specifically, the standards address how acquired intangible assets should be accounted for both at the time of acquisition and after they have been recognized in the financial statements. In accordance with SFAS No. 142, intangible assets, including purchased goodwill, must be evaluated for impairment. Those intangible assets that are classified as goodwill or as other intangibles with indefinite lives are not amortized.

Impairment testing is performed in two steps: (i) the Company determines impairment by comparing the fair value of a reporting unit with its carrying value, and (ii) if there is an impairment, the Company measures the amount of impairment loss by comparing the implied fair value of goodwill with the carrying amount of that goodwill. The Company has performed its annual impairment evaluation required by this standard and determined that its goodwill is not impaired.

Income Taxes

The Company adopted the provisions of FIN 48 as of July 1, 2007. As a result the Company increased its accrued income tax liability by $715,000, from $1,836,000 to $2,551,000, to provide for additional reserves for uncertain income tax positions, relating to fiscal years 2004 through 2007. The increase in the accrued income tax liability of $715,000 was offset in part by a $230,000 increase to a deferred income tax asset, resulting in a net reduction to retained earnings of $485,000 (representing the cumulative effect of adopting FIN 48).

During the year ended June 30, 2008 the Company decreased its reserve for uncertain income tax positions by $ 1,888,000. As of June 30, 2008 the Company has a long-term accrued income tax liability of $ 249,000. The Company's practice is to recognize interest and penalties related to income tax matters in income tax expense and accrued income taxes. As of June 30, 2008, the Company had accrued interest totaling $45,000 and $194,000 of unrecognized net tax benefits (including the related accrued interest and net of the related deferred income tax benefit of $100,000) that, if recognized, would favorably affect the company's effective income tax rate in any future period.

For the year ended June 30, 2008, the company recognized a net benefit to income tax expense of $2,127,000 ($2,257,000 liability reversal including interest, less the related $130,000 reversal of deferred tax asset). This benefit relates predominantly to the Company's domestication election, for which the statute of limitations expired during the third quarter.

The difference between the statutory U.S. Federal income tax rate and the Company's effective tax rate as reflected in the consolidated statements of income for fiscal 2008 is as follows (dollars in thousands):

	Amount	% of Pre-tax Income
Tax at Federal statutory rate	$ 785	34.0%
Increases (decreases) in taxes resulting from:		
Meals and entertainment	59	2.6%
State income taxes, net of Federal income tax benefit	(16)	(0.7)%
Foreign source income and taxes	(258)	(11.1)%
Stock based compensation expense	66	2.9%
Alternative Minimum Tax Credit utilization	--	--
Tax reserve reversal	(2,127)	(92.1)%
Other, net	83	3.6%
Provision for income taxes	$(1,408)	(61.0)%

Liquidity and Capital Resources

The Company's cash on hand combined with proceeds from operating and financing activities during fiscal 2008 were adequate to meet the Company's capital expenditure needs and long-term debt obligations. The Company's primary internal source of liquidity is the cash flow generated from operations. The primary source of financing related to borrowings under an $25,000,000 secured revolving credit facility. The Company expects that cash generated from operations and cash available under the Company's bank line of credit will be adequate to meet its short-term liquidity requirements. As of June 30, 2008, the Company's unused sources of funds consisted principally of $2,765,000 in cash and approximately $12,600,000, which represents the unused portion of its secured revolving credit facility.

The Company is a party to an amended and restated secured revolving credit agreement with its primary bank, pursuant to which borrowing capacity as of June 30, 2008 was $25,000,000. Amounts under the amended revolving credit agreement are secured by all the accounts receivable, inventory and certain other assets of the Company, including a first and second mortgage on the Company's headquarters in Amityville, New York and common stock of certain of the Company's subsidiaries. As of June 30, 2008 the Company was not in compliance with the covenant relating to Tangible Net Worth required under the $25,000,000 facility which was in effect as of June 30, 2008. The Company has received the appropriate waiver from its bank during September 2008.

On August 18, 2008, the Company and its banks amended and restated the revolving credit agreement described above. The amended facility is $50,000,000 and provides for a $25,000,000 revolving credit line as well as a $25,000,000 term portion of which the entire $25,000,000 was utilized to finance the asset purchase agreement as described in Note 12 to the accompanying Consolidated Financial Statements. The amended revolving credit agreement and term loan is secured by all the accounts receivable, inventory, the Company's headquarters in Amityville, New York and certain other assets of Napco Security Systems, Inc. and the common stock of three of the Company's subsidiaries. The agreements bear interest at either the Prime Rate or an alternate rate based on LIBOR as described in the agreement. As of June 30, 2008 the interest rate on the outstanding portion of the facility was 4.1%. The August amendment extended the revolving credit agreement to August 2012. Any outstanding borrowings are to be repaid or refinanced on or before that time. The term loan is to be repaid in 19 quarterly installments of $893,000 each commencing in December 2007 and a final payment of $8,033,000 due in August 2013. The agreements contain various restrictions and covenants including, among others, restrictions on payment of dividends, restrictions on borrowings and compliance with certain financial ratios, as defined in the agreement.

Management believes that current working capital, cash flows from operations and its revolving credit agreement will be sufficient to fund the Company's operations through at least the first quarter of fiscal 2010.

The Company takes into consideration a number of factors in measuring its liquidity, including the ratios set forth below:

	2008	2007	2006
Current Ratio	5.7 to 1	5.3 to 1	4.1 to 1
Sales to Receivables	2.7 to 1	2.6 to 1	2.8 to 1
Total debt to equity	.23 to 1	.20 to 1	.09 to 1

As of June 30, 2008, the Company had no material commitments for capital expenditures or inventory purchases other than purchase orders issued in the normal course of business. On April 26, 1993, the Company's foreign subsidiary entered into a 99-year land lease of approximately 4 acres of land in the Dominican Republic, at an annual cost of approximately $288,000.

On August 18, 2008, Napco Security Systems, Inc. (the "Company") pursuant to an Asset Purchase Agreement with G. Marks Hardware, Inc. ("Marks") of Amityville, New York, acquired substantially all of the assets and business of Marks for $25 million, the repayment of $1 million of bank debt and the assumption of current liabilities as described more fully in the Asset Purchase Agreement. The Marks business involves the manufacturing and distribution of door-locking devices. The Company funded the acquisition with a term loan from its lenders as described above.

The acquisition described above will be accounted for as a purchase and was valued based on management's estimate of the fair value of the assets acquired and liabilities assumed. The estimates of fair value are preliminary and subject to adjustment for a period of up to one year from the date of acquisition, and any such adjustments are not expected to be material. Costs in excess of identifiable net assets acquired will be allocated to goodwill in the first quarter of fiscal 2009.

Working Capital. Working capital increased by $766,000 to $41,293,000 at June 30, 2008 from $40,527,000 at June 30, 2007. The increase in working capital was primarily the result of the increase in long-term debt as partially offset by the decrease in inventories. Working capital is calculated by deducting Current Liabilities from Current Assets.

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Accounts Receivable. Accounts Receivable increased by $244,000 to $25,823,000 at June 30, 2008 from $25,579,000 at June 30, 2007. This increase resulted primarily from the higher net sales during the fourth quarter of fiscal 2008 as compared to the fourth quarter of fiscal 2007.

Inventories. Inventories decreased by $951,000 to $27,272,000 at June 30, 2008 as compared to $28,223,000 at June 30, 2007. The decrease in inventory levels was primarily the result of the Company having high inventory levels at the end of fiscal 2007, which it utilized to fill sales orders in fiscal 2008.

Accounts Payable and Accrued Expenses. Accounts payable and accrued expenses decreased by $581,000 to $8,733,000 as of June 30, 2008 as compared to $9,314,000 at June 30, 2007. This decrease is primarily due to decreased purchases of raw materials during the month of June 2008 as compared to June 2007, which was part of the Company's program to reduce its inventory levels from the increased levels at mid-year as previously discussed.

Off-Balance Sheet Arrangements

The Company does not maintain any off-balance sheet arrangements.

Contractual Obligations

The following table summarizes the Company's contractual obligations by fiscal year:

Payments due by period

Contractual obligations	Total	Less than 1 year	1-3 years	3-5 years	Mor
Long-term debt obligations	$37,400,000	$ 2,679,000	$ 7,144,000	$19,544,000	$ 8
Land lease (86 years remaining) (1)	24,192,000	288,000	576,000	576,000	22
Operating lease obligations	586,000	420,000	162,000	4,000	
Other long-term obligations (employment agreements) (1)	1,753,000	1,105,000	648,000	--	
Total	$63,931,000	$ 4,492,000	$ 8,530,000	$20,124,000	$30

(1) see footnote 10 to the consolidated financial statements.

Results of Operations

Fiscal 2008 Compared to Fiscal 2007

	Fiscal year ended June 30, 2008	2007	% Increase/ (decrease)
Net sales	$ 68,367	$ 66,202	3.3%
Gross profit	20,412	23,998	(14.9)%
Gross profit as a % of net sales	29.9%	36.2%	(6.3)%
Selling, general and administrative	17,275	17,497	(1.3)%
Income from operations	3,137	6,501	(51.7)%
Interest expense, net	819	637	28.6%
Other expense, net	42	17	147.1%
Provision (benefit)for income taxes	(1,408)	1,922	(173.3)%
Net income	3,718	4,217	11.8%

Net sales in fiscal 2008 increased by 3.3% to $68,367,000 from $66,202,000 in fiscal 2007. The increase in sales was due primarily to increases in the Company's international sales ($2,853,000) as partially offset by a decrease in domestic intrusion detection and access control products ($510,000). International sales has increased primarily as a result of improved sales efforts and customer relations. Management believes its sales of intrusion products continues to be impacted by the slowdown in the U.S. housing market.

The Company's gross profit decreased $3,586,000 to $20,412,000 or 29.9% of net sales in fiscal 2008 as compared to $23,998,000 or 36.2% of net sales in fiscal 2007. The decrease in gross profit in both absolute dollars and as a percentage of net sales was due primarily to the recognition of increased overhead expenses that had been capitalized in ending inventory at June 30, 2007. As these products were sold during fiscal 2008, the Company recognized the higher expense of these costs which resulted in a lower gross profit in the current period. In addition, a higher proportion of the Company's sales were to its international customers. Sales to these customers typically have lower gross margins than sales to its domestic customers because the selling prices in these markets are lower than those in the U.S. market.

Selling, general and administrative expenses as a percentage of net sales decreased to 25.3% in fiscal 2008 from 26.4% in fiscal 2007. Selling, general and administrative expenses for fiscal 2008 remained relatively constant at $17,275,000 from $17,497,000 in fiscal 2007. The decrease as a percentage of net sales resulted primarily from the Company's incremental sales in fiscal 2008 being to its international customers. Sales to these customers typically have lower variable selling expenses associated with them as compared to sales to the Company's domestic customers.

Interest expense for fiscal 2008 increased by $182,000 to $819,000 from $637,000 for the same period a year ago. The increase in interest expense is primarily the result of the increase in outstanding debt.

Other expenses increased slightly to $42,000 in fiscal 2008 as compared to $17,000 in fiscal 2007.

The Company's provision for income taxes for fiscal 2008 decreased by $3,330,000 to a benefit of $1,408,000 as compared to a provision of $1,922,000 for the same period a year ago. The decrease in provision for income taxes resulted primarily from the Company recognizing a net tax benefit to income tax expense of $2,131,000 as described in Note 5 to the Consolidated financial statements. In addition, in December 2007 the Company completed a corporate restructuring for which new offshore companies were formed. As a result, the Company's effective rate for fiscal 2008, prior to the effect of the $2,127,000 benefit described above, was 31%, which reflected this restructuring.

Net income for fiscal 2008 decreased by $499,000 to $3,718,000 as compared to $4,217,000 in fiscal 2007. This resulted primarily from the decrease in Gross profit of $3,586,000 as partially offset by the $2,127,000 tax accrual reversal, both of which are discussed above.

Fiscal 2007 Compared to Fiscal 2006

	Fiscal year ended June 30,		
	2007	2006	% Increase/ (decrease)
Net sales	$66,202	$69,548	(4.8)%
Gross profit	23,998	26,956	(11.0)%
Gross profit as a % of net sales	36.2%	38.8%	(2.6)%
Selling, general and administrative	17,497	17,433	0.4%
Income from operations	6,501	9,523	(31.7)%
Interest expense, net	637	258	146.9%
Other expense, net	17	14	21.4%
Provision for income taxes	1,922	3,264	(41.1)%
Net income	4,217	6,119	(31.1)%

Net Sales. Net sales in fiscal 2007 decreased by 4.8% to $66,202,000 from $69,548,000 in fiscal 2006. The decrease in sales was primarily due to decreased sales of the Company's burglar alarm products ($6,407,000), which management believes was impacted by the slowdown in the U.S. housing market and reduced demand in the Company's European market, as partially offset by increased sales of door-locking and access control products ($2,290,000).

Gross Profit. The Company's gross profit decreased $2,958,000 to $23,998,000 or 36.2% of net sales in fiscal 2007 as compared to $26,956,000 or 38.8% of net sales in fiscal 2006. The decrease in gross profit in both absolute dollars and as a percentage of net sales was due primarily to the decreased overhead

absorption resulting in the Company's reduction in its production levels in the second half of fiscal 2007 which was due to the decrease in net sales during the year.

Selling, general and administrative expenses as a percentage of net sales increased to 26.4% in fiscal 2007 from 25.1% in fiscal 2006. Selling, general and administrative expenses for fiscal 2007 increased by $64,000 to $17,497,000 from $17,433,000 in fiscal 2006. These increases are due primarily to increases in certain salesman compensation expenses ($497,000) as partially offset by decreases in the Company's executive compensation costs ($206,000), Sarbanes-Oxley compliance costs ($107,000) and bad debt expense ($125,000).

Interest expense for fiscal 2007 increased by $379,000 to $637,000 from $258,000 for the same period a year ago. The increase in interest expense is primarily the result of the increase in outstanding debt and an increase in interest rates available to the Company during fiscal 2007.

Other Expenses. Other expenses remained relatively constant at $17,000 in fiscal 2007 as compared to $14,000 in fiscal 2006.

Stock Dividend and Stock Split

On May 10, 2006 the Company's Board of Directors approved a 3-for-2 stock split of its common stock, to be paid in the form of a 50% stock dividend to stockholders of record on May 24, 2006. The Company delivered the shares on June 7, 2006. Upon completion of the split, the total number of shares of common stock outstanding increased from approximately 13,300,000 to approximately 19,950,000.

In November 2005 the Company's Board of Directors approved a 3-for-2 split of its common stock, payable in the form of a 50% stock dividend to stockholders of record on December 14, 2005. The additional shares were distributed on December 28, 2005. Upon completion of the split, the total number of shares of common stock outstanding increased from approximately 8,795,000 to approximately 13,192,000.

All share and per share amounts (except par value) have been retroactively adjusted to reflect the stock splits and dividend. There was no net effect on total stockholders' equity as a result of these transactions.

Forward-looking Information

This Annual Report on Form 10-K and the information incorporated by reference may include "Forward-Looking Statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Exchange Act of 1934. The Company intends the Forward-Looking Statements to be covered by the Safe Harbor Provisions for Forward-Looking Statements. All statements regarding the Company's expected financial position and operating results, its business strategy, its financing plans and the outcome of any contingencies are Forward-Looking Statements. The Forward-Looking Statements are based on current estimates and projections about our industry and our business. Words such as "anticipates," "expects," "intends," "plans," "believes," "seeks," "estimates," or variations of such words and similar expressions are intended to identify such Forward-Looking Statements. The Forward-Looking Statements are subject to risks and uncertainties that could cause actual results to differ materially from those set forth or implied by any Forward-Looking Statements. For example, the Company is highly dependent on its Chief Executive Officer for strategic planning. If he is unable to perform his services for any significant period of time, the Company's ability to continue growing could be adversely affected. In

addition, factors that could cause actual results to differ materially from the Forward-Looking Statements include, but are not limited to, adverse tax consequences of offshore operations, distribution problems, unforeseen environmental liabilities and the uncertain military, political and economic conditions in the world. The Company's Risk Factors are discussed in more detail in Item 1A.

ITEM 7A: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's principal financial instrument is long-term debt (consisting of a revolving credit facility) that provides for interest at a spread below the prime rate. The Company is affected by market risk exposure primarily through the effect of changes in interest rates on amounts payable by the Company under this credit facility. At June 30, 2008, an aggregate principal amount of approximately $12,400,000 was outstanding under the Company's credit facility with a weighted average interest rate of approximately 4.1%. If principal amounts outstanding under the Company's credit facility remained at this year-end level for an entire year and the prime rate increased or decreased, respectively, by 1% the Company would pay or save, respectively, an additional $124,000 in interest that year.

A significant number of foreign sales transactions by the Company are denominated in U.S. dollars. As such, the Company has shifted foreign currency exposure onto many of its foreign customers. As a result, if exchange rates move against foreign customers, the Company could experience difficulty collecting unsecured accounts receivable, the cancellation of existing orders or the loss of future orders. The foregoing could materially adversely affect the Company's business, financial condition and results of operations. In addition, the Company transacts certain sales in Europe in British Pounds Sterling, therefore exposing itself to a certain amount of foreign currency risk. Management believes that the amount of this exposure is immaterial. We are also exposed to foreign currency risk relative to expenses incurred in Dominican Pesos ("RD$"), the local currency of the Company's production facility in the Dominican Republic. The result of a 10% strengthening in the U.S. dollar to our RD$ expenses would result in an annual decrease in income from operations of approximately $314,000.

ITEM 8: FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

a. Financial Statements: Financial statements required pursuant to this Item are presented on pages FS-1 through FS-25 of this report as follows:

NAPCO SECURITY SYSTEMS, INC. AND SUBSIDIARIES

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Report of Independent Registered Public Accounting Firm	FS-3
Consolidated Financial Statements:	
Consolidated Balance Sheets as of June 30, 2008 and 2007	FS-4

Consolidated Statements of Income for the Fiscal Years Ended June 30, 2008, 2007 and 2006 FS-6

Consolidated Statements of Stockholders' Equity for the Fiscal Years Ended June 30, 2008, 2007 and 2006 FS-7

Consolidated Statements of Cash Flows for the Fiscal Years Ended June 30, 2008, 2007 and 2006 FS-8

Notes to Consolidated Financial Statements, June 30, 2008 FS-9

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MANAGEMENT REPORT ON INTERNAL CONTROLS OVER FINANCIAL REPORTING

Management is responsible for the preparation of Napco Security Systems, Inc. (Napco Security Systems) consolidated financial statements and related information. Management uses its best judgment to ensure that the consolidated financial statements present fairly, in all material respects, Napco Security Systems consolidated financial position and results of operations in conformity with generally accepted accounting principles.

The financial statements have been audited by an independent registered public accounting firm in accordance with the standards of the Public Company Accounting Oversight Board. Their report expresses the independent accountant's judgment as to the fairness of management's reported operating results, cash flows and financial position. This judgment is based on the procedures described in the second paragraph of their report.

Napco Security Systems management is responsible for establishing and maintaining adequate internal control over financial reporting. Under the supervision of management, we 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 of Sponsoring Organizations of the Treadway Commission published in 1992 and subsequent guidance prepared specifically for smaller public companies.

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 the registrant's annual or interim financial statements will not be prevented or detected on a timely basis. As a result of our evaluation, management identified material weaknesses in our internal controls over financial reporting, as of June 30, 2008. To address these weaknesses described below, we performed additional analysis and performed other procedures to ensure the consolidated financial statements were prepared in accordance with generally accepted accounting principles. Accordingly, management believes that the consolidated financial statements included in this Annual Report on Form 10-K, fairly present, in all material respects, our financial condition, results of operations and cash flows for the periods presented in accordance with generally accepted accounting principles.

We identified the following material weaknesses relating to internal control of inventory and our interim reporting:

1. Costing of inventory: Management's key controls over detecting inaccuracies in costing were not operating effectively. Management has certain controls in place to detect significant costing inaccuracies, however certain of these were not performed because management had time constraints associated with the efforts involved with its acquisition, an event that is not typical during the financial reporting process. As part of its remediation efforts, management plans on revising its inventory controls to ensure that the proper procedures are carried out in future periods.

2. Interim reporting: Management did not have controls in place to sufficiently refine its method for adjusting the estimates involved in quantifying cost of goods sold and inventory amounts based on changes in the business and new variables. This caused the recognition of expenses in cost of sales for the three interim periods to be understated, thus reporting an undue proportion of these expenses during the fourth quarter. Because the estimates used causing these understatements are only used for interim reporting, as of this Annual Report on 10-K, total expenses are recorded correctly. Management intends to develop new controls that will permit it to identify new variables and changes in the business when they occur in order to estimate its interim inventory and cost of sales.

Previously Reported Material Weaknesses

All other material weaknesses previously noted in our past filings have been remediated and the results of management's current year assessment have confirmed that remediation efforts put in place by management have sufficiently reduced or eliminated the risk of misstatement associated with these former material weaknesses. During the fourth quarter of 2008, management implemented internal controls to addresses the material weakness related to the valuation of inventory. With respect to its overhead estimation methodology, while the technique used to make this estimate has not changed, the amount of the costs used in the estimate has significantly decreased since the prior year and is expected to continue to decrease. Thus, management does not believe that its use of this estimation technique continues to have a material impact on its financial information. Furthermore, management incorporated additional reviews of obsolete and slow moving parts by additional members of management.

Management also prepared a draft obsolescence review prior to the end of the year to facilitate the formal year-end review. Management now conducts weekly meetings to update the status of obsolete or slow moving parts. Management has previously disclosed its remediation efforts of the material weakness related to the classification of inventory, and this weakness has been fully remediated. We will continue to monitor the effectiveness of our internal controls and procedures on an ongoing basis and will take further actions, as appropriate.

Notwithstanding the above, management believes that the consolidated financial statements included in this Annual Report on Form 10-K, fairly present, in all material respects, our financial condition, results of operations and cash flows for the periods presented in accordance with generally accepted accounting principles.

There have not been any other changes in our internal control over financial reporting that occurred during our first fiscal quarter that have materially affected or are reasonably likely to affect our internal control over financial reporting.

Marcum & Kliegman LLP, an independent registered public accounting firm, that audited our consolidated financial statements included in this Annual Report on Form 10-K, has issued an attestation report on management's assessment of Napco Security System's internal control over financial reporting.

The Board of Directors of Napco Security Systems has an Audit Committee comprised of three non-management directors. The Committee meets periodically

with financial management and the independent auditors to review accounting, control, audit and financial reporting matters. Marcum & Kliegman have full and free access to the Audit Committee, with and without the presence of management.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING

To the Audit Committee of the
Board of Directors and Stockholders
of NAPCO Security Systems, Inc.

We have audited NAPCO Security Systems, Inc. and Subsidiaries' (the "Company") internal control over financial reporting as of June 30, 2008, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying "Management Report on Internal Control over Financial Reporting". Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that degree of compliance with the policies or procedures may deteriorate.

A material weakness is a control deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable

possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis. The following material weaknesses have been identified and included in management's annual report on internal control over financial reporting:

(1) With respect to inventory valuation, management's controls were not operating effectively to ensure that it is recording inventory at the correct cost. This resulted in component part costing errors and overhead calculation errors.

(2) Management uses certain estimates with respect to the calculation of inventory and cost of sales during the interim periods. These estimations were not effective

These material weaknesses were considered in determining the nature, timing and extent of audit tests applied in our audit of the fiscal 2008 consolidated financial statements and financial statement schedule, and this report does not affect our report dated September 30, 2008.

In our opinion, because of the effect of the material weaknesses described above on the achievement of the objectives of the control criteria, NAPCO Security Systems, Inc. and Subsidiaries has not maintained effective internal control over financial reporting as of June 30, 2008, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets as of June 30, 2008 and 2007, and the related consolidated statements of income, stockholders' equity and cash flows of NAPCO Security Systems, Inc. and Subsidiaries for each of the three years in the period ended June 30, 2008, and our report dated September 30, 2008 expressed an unqualified opinion.

Marcum & Kliegman LLP
Melville, NY
September 30, 2008

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Audit Committee of the Board of Directors and Stockholders of NAPCO Security Systems, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of NAPCO Security Systems, Inc. and Subsidiaries (the "Company") as of June 30, 2008 and 2007, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended June 30, 2008. Our audits also included the financial statement schedule as of and for the years ended June 30, 2008, 2007 and 2006 listed in the index at item 15. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit also includes examining,

on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of NAPCO Security Systems, Inc. and Subsidiaries, as of June 30, 2008 and 2007, and the results of its operations and its cash flows for each of the three years in the period ended June 30, 2008 in conformity with generally accepted accounting principles in the United States. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole presents fairly, in all material aspects, the information set forth therein.

As discussed in Note 5 to the consolidated financial statements, the Company changed its method of accounting for uncertain tax positions in accordance with FASB Interpretation 48 "Accounting for Uncertainty in Income Taxes - an Integration of FASB Statement No. 109" on July 1, 2007.

Melville, New York
September 30, 2008

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NAPCO SECURITY SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

June 30, 2008 and 2007
(In Thousands)

ASSETS

	2008	2007
CURRENT ASSETS		
Cash and cash equivalents	$ 2,765	$ 1,748
Accounts receivable, net of reserves	25,823	25,579
Inventories	19,548	20,389
Prepaid expenses and other current assets	1,121	1,171
Deferred income taxes	769	1,050
Total Current Assets	50,026	49,937
Inventories - non-current, net	7,724	7,834
Property, plant and equipment, net	8,989	9,135
Goodwill, net	9,686	9,686
Other assets	298	193
TOTAL ASSETS	$76,723	$76,785

See accompanying notes to consolidated financial statements.

NAPCO SECURITY SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

June 30, 2008 and 2007
(In Thousands, Except Share Data)

LIABILITIES AND STOCKHOLDERS' EQUITY

	2008	20
CURRENT LIABILITIES		
Accounts payable	$ 4,857	$ 5,
Accrued expenses	1,333	1,
Accrued salaries and wages	2,543	2,
Accrued income taxes	--	
Total Current Liabilities	8,733	9,
Long-term debt	12,400	10,
Accrued income taxes	294	1,
Deferred income taxes	1,607	1,
Minority interest in subsidiary	147	
Total Liabilities	23,181	23,
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY		
Common stock, par value $0.01 per share; 40,000,000 shares authorized; 20,092,473 and 20,090,313 shares issued; 19,092,473 and 19,665,141 shares outstanding, respectively	201	
Additional paid-in capital	13,424	13,
Retained earnings	45,532	42,
	59,157	55,
Less: Treasury Stock, at cost (1,000,000 and 425,172 shares, respectively)	(5,615)	(2,
TOTAL STOCKHOLDERS' EQUITY	53,542	53,
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 76,723	$ 76,

See accompanying notes to consolidated financial statements.

NAPCO SECURITY SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

Years Ended June 30, 2008, 2007, and 2006
(In Thousands, Except Share and Per Share Data)

	2008	2007	2006
Net sales	$ 68,367	$ 66,202	$ 69,548
Cost of sales	47,955	42,204	42,592
Gross Profit	20,412	23,998	26,956
Selling, general, and administrative expenses	17,275	17,497	17,433
Operating Income	3,137	6,501	9,523
Other expense:			
Interest expense, net	(819)	(637)	(258
Other, net	(42)	(17)	(14
	(861)	(654)	(272
Income Before Minority Interest and Income Taxes	2,276	5,847	9,251
Minority interest in loss of subsidiary	34	292	132
Income Before (Benefit) Provision for Income Taxes	2,310	6,139	9,383
(Benefit) Provision for income taxes	(1,408)	1,922	3,264
Net Income	$ 3,718	$ 4,217	$ 6,119
Earnings per share:			
Basic	$ 0.19	$ 0.21	$ 0.31
Diluted	$ 0.19	$ 0.20	$ 0.30
Weighted average number of shares outstanding:			
Basic	19,263,000	19,961,000	19,785,000
Diluted	19,802,000	20,599,000	20,605,000

See accompanying notes to consolidated financial statements.

NAPCO SECURITY SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

Years Ended June 30, 2008, 2007 and 2006
(In Thousands, Except Share Data)

	Common stock			Treasury Stoc	
	Number of Shares Issued	Amount	Additional Paid-in Capital	Number of Shares	A
BALANCE - June 30, 2005	19,474,173	195	11,520	--	
Exercise of employee stock options	476,280	5	442	--	
Tax benefit in connection with exercise of stock options	--	--	210	--	
Non-cash stock-based compensation expense	--	--	396	--	
Net income	--	--	--	--	
BALANCE - June 30, 2006	19,950,453	200	12,568	--	
Exercise of employee stock options	139,860	1	167	--	
Non-cash stock-based compensation expense	--	--	412	--	
Repurchase of Treasury shares	--	--	--	(425,172)	
Net income	--	--	--	--	
BALANCE - June 30, 2007	20,090,313	201	13,147	(425,172)	
Exercise of employee stock options	2,160	--	3	--	
Non-cash stock-based compensation expense	--	--	274	--	
Repurchase of Treasury shares	--	--	--	(574,828)	
FIN48 adjustment to retained earnings	--	--	--	--	
Net income	--	--	--	--	
BALANCE - June 30, 2008	20,092,473	$ 201	$ 13,424	(1,000,000)	$

See accompanying notes to consolidated financial statements.

NAPCO SECURITY SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended June 30, 2008, 2007, and 2006 (In Thousands)

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 3,718	$ 4,217
Adjustments to reconcile net income to net cash Provided by (used in) operating activities:		
Depreciation and amortization	1,191	1,201
Charge (Recovery) to obsolescence reserve	--	213
(Recovery) Provision for doubtful accounts	40	(55)

Deferred income taxes	653	(170)
Excess tax benefit from exercise of stock options	--	--
Non-cash stock based compensation expense	274	412
Changes in operating assets and liabilities:		
Accounts receivable	(284)	(371)
Inventories	951	(5,770)
Prepaid expenses and other current assets	52	(416)
Other assets	(106)	(43)
Accounts payable, accrued expenses, accrued salaries and wages, accrued income taxes and minority interest	(2,705)	(2,893)
Net Cash Provided by (Used in) Operating Activities	3,784	(3,674)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property, plant, and equipment	(1,045)	(1,294)
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash paid for purchase of Treasury Stock	(3,225)	(2,390)
Principal payments on long-term debt	(3,500)	(1,100)
Proceeds from long-term debt	5,000	7,300
Proceeds from exercise of employee stock options	3	168
Excess tax benefit from exercise of stock options	--	--
Loan costs paid	--	--
Net Cash (Used In) Provided By Financing Activities	(1,722)	3,978
Net Increase (Decrease) In Cash and Cash Equivalents	1,017	(990)
CASH AND CASH EQUIVALENTS - Beginning	1,748	2,738
CASH AND CASH EQUIVALENTS - Ending	$ 2,765	$ 1,748
SUPPLEMENTAL CASH FLOW INFORMATION		
Interest paid, net	$ 776	$ 520
Income taxes paid	$ 108	$ 4,280
NON-CASH INVESTING ACTIVITIES:		
Adjustment to Retained earnings relating to adoption of FIN 48	$ (485)	$ --

See accompanying notes to consolidated financial statements.

NAPCO SECURITY SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - Nature of Business and Summary of Significant Accounting Policies

Nature of Business

Napco Security Systems, Inc. and subsidiaries (the "Company") is a diversified manufacturer of security products, encompassing intrusion and fire alarms, building access control systems and electronic locking devices. These products are used for commercial, residential, institutional, industrial and governmental applications, and are sold worldwide principally to independent distributors, dealers and installers of security equipment.

Principles of Consolidation

The consolidated financial statements include the accounts of Napco Security Systems, Inc. and all of its wholly-owned subsidiaries. The Company has also consolidated a 51%-owned joint venture. The 49% interest, held by a third party, is reflected as minority interest. All inter-company balances and transactions have been eliminated in consolidation.

Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent gains and losses at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Critical estimates include management's judgments associated with revenue recognition, concentration of credit risk, inventories, goodwill and income taxes. Actual results could differ from those estimates. Gross profit for the fourth quarter of fiscal 2008 was adversely affected by the recognition of certain material and factory expenses in the fourth quarter that should have been charged to cost of goods sold during the first nine months of fiscal 2008. This was due to certain inaccuracies in the estimates used for interim reporting in quantifying cost of goods sold and inventory amounts based on changes in the business.

Cash and Cash Equivalents

Cash and cash equivalents include approximately $1,753,000 and $195,000 of short-term time deposits at June 30, 2008 and 2007, respectively. The Company considers all highly liquid investments with original maturities of three months or less to be cash equivalents. The Company has cash balances in banks in excess of the maximum amount insured by the FDIC and other international agencies as of June 30, 2008 and 2007.

Accounts Receivable

Accounts receivable is stated net of the reserves for doubtful accounts of $405,000 and $365,000 and for returns and other allowances of $1,130,000 and $1,385,000 as of June 30, 2008 and June 30, 2007, respectively. Our reserves for doubtful accounts and for returns and other allowances are subjective critical estimates that have a direct impact on reported net earnings. These reserves are based upon the evaluation of accounts receivable agings, specific exposures, sales levels and historical trends.

Inventories

Inventories are valued at the lower of cost or fair market value, with cost being determined on the first-in, first-out (FIFO) method. The reported net

value of inventory includes finished saleable products, work-in-process and raw materials that will be sold or used in future periods. Inventory costs include raw materials, direct labor and overhead. The Company's overhead expenses are applied based, in part, upon estimates of the proportion of those expenses that are related to procuring and storing raw materials as compared to the manufacture and assembly of finished products. These proportions, the method of their application, and the resulting overhead included in ending inventory, are based in part on subjective estimates and approximations and actual results could differ from those estimates.

In addition, the Company records an inventory obsolescence reserve, which represents the difference between the cost of the inventory and its estimated market value, based on various product sales projections. This reserve is calculated using an estimated obsolescence percentage applied to the inventory based on age, historical trends, requirements to support forecasted sales, and the ability to find alternate applications of its raw materials and to convert finished product into alternate versions of the same product to better match customer demand. There is inherent professional judgment and subjectivity made by both production and engineering members of management in determining the estimated obsolescence percentage. For the fiscal years 2008, 2007 and 2006, charges/(recoveries) and balances in these reserves amounted to $0 and $1,200,000, $213,000 and $1,200,000; $(531,000) and $987,000, respectively. In addition, and as necessary, the Company may establish specific reserves for future known or anticipated events.

The Company also regularly reviews the period over which its inventories will be converted to sales. Any inventories expected to convert to sales beyond 12 months from the balance sheet date are classified as non-current.

Property, Plant, and Equipment

Property, plant, and equipment are carried at cost less accumulated depreciation. Expenditures for maintenance and repairs are charged to expense as incurred; costs of major renewals and improvements are capitalized. At the time property and equipment are retired or otherwise disposed of, the cost and accumulated depreciation are eliminated from the asset and accumulated depreciation accounts and the profit or loss on such disposition is reflected in income.

Depreciation is recorded over the estimated service lives of the related assets using primarily the straight-line method. Amortization of leasehold improvements is calculated by using the straight-line method over the estimated useful life of the asset or lease term, whichever is shorter.

Goodwill

The Company accounts for goodwill in accordance with Statement of Financial Accounting Standards (SFAS) No. 141, Business Combinations and SFAS No. 142, Goodwill and Other Intangible Assets. These statements established accounting and reporting standards for acquired goodwill and other intangible assets. Specifically, the standards address how acquired intangible assets should be accounted for both at the time of acquisition and after they have been recognized in the financial statements. In accordance with SFAS No. 142, purchased goodwill must be evaluated for impairment on an annual basis. Those intangible assets that are classified as goodwill or as other intangibles with indefinite lives are not amortized.

Impairment testing is performed in two steps: (i) the Company determines impairment by comparing the fair value of a reporting unit with its carrying

value, and (ii) if there is an impairment, the Company measures the amount of impairment loss by comparing the implied fair value of goodwill with the carrying amount of that goodwill. The Company has performed its annual impairment evaluation required by this standard and determined that the goodwill is not impaired.

Long-Lived Assets

In accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets in question may not be recoverable. An impairment would be recorded in circumstances where undiscounted cash flows expected to be generated by an asset are less than the carrying value of that asset.

Revenue Recognition

In accordance with SEC Staff Accounting Bulletin Topic 13, Revenue Recognition, the Company recognizes revenue when the following criteria are met: (i) persuasive evidence of an agreement exists, (ii) there is a fixed and determinable price for the Company's product, (iii) shipment and passage of title occurs, and (iv) collectibility is reasonably assured. Revenues from merchandise sales are recorded at the time the product is shipped or delivered to the customer pursuant to the terms of the sale. The Company reports its sales levels on a net sales basis, with net sales being computed by deducting from gross sales the amount of actual sales returns and other allowances and the amount of reserves established for anticipated sales returns and other allowances.

Sales Returns and Other Allowances

The Company analyzes sales returns in accordance with SFAS No. 48 "Revenue Recognition When Right of Return Exists". The Company is able to make reasonable and reliable estimates of product returns based on the Company's past history. Estimates for sales returns are based on several factors including actual returns and based on expected return data communicated to it by its customers. Accordingly, the Company believes that its historical returns analysis is an accurate basis for its allowance for sales returns. Actual results could differ from those estimates.

Advertising and Promotional Costs

Advertising and promotional costs are included in "Selling, General and Administrative" expenses in the consolidated statements of income and are expensed as incurred. Advertising expense for the fiscal years ended June 30, 2008, 2007 and 2006 was $1,256,000, $1,374,000 and $1,318,000, respectively.

Research and Development Costs

Research and development costs incurred by the Company are charged to expense in the year incurred. Company-sponsored research and development costs of $5,500,000, $5,319,000 and $5,109,000 were charged to expense for the fiscal years ended June 30, 2008, 2007 and 2006, respectively, and are included in "Cost of Sales" in the consolidated statements of income.

Income Taxes

The Company accounts for income taxes in accordance with SFAS No. 109, "Accounting for Income Taxes," as amended. This statement establishes financial

accounting and reporting standards for the effects of income taxes that result from an enterprise's activities during the current and preceding years. It requires an asset and liability approach for financial accounting and reporting of income taxes.

In June 2006, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. ("FIN") 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109" ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109. FIN 48 prescribes a two-step evaluation process for tax positions taken, or expected to be taken, in a tax return. The first step is recognition and the second is measurement. FIN 48 also provides guidance on derecognition, measurement, classification, disclosures, transition and accounting for interim periods. In May 2007, the FASB issued FASB Staff Position ("FSP") No. FIN 48-1, "Definition of Settlement in FASB Interpretation No. 48, an amendment of FASB Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes" ("FSP No. FIN 48-1"). FSP No. FIN 48-1 provides guidance on how to determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits. The Company adopted the provisions of FIN 48, as amended, effective July 1, 2007. See Note 5.

Stock Dividend and Stock Split

On May 10, 2006 the Company's Board of Directors approved a 3-for-2 stock split of its common stock, to be paid in the form of a 50% stock dividend to stockholders of record on May 24, 2006. The Company delivered the shares on June 7, 2006. Upon completion of the split, the total number of shares of common stock outstanding increased from approximately 13,300,000 to approximately 19,950,000.

On November 29, 2005 the Company's Board of Directors approved a 3-for-2 split of its common stock, payable in the form of a 50% stock dividend to stockholders of record on December 14, 2005. The additional shares were distributed on December 28, 2005. Upon completion of the split, the total number of shares of common stock outstanding increased from approximately 8,795,000 to approximately 13,192,000.

All share and per share amounts (except par value) have been retroactively adjusted to reflect the stock splits and dividend. There was no net effect on total stockholders' equity as a result of these transactions.

Earnings Per Share

The Company follows the provisions of SFAS No. 128, Earnings Per Share. Basic net income per common share (Basic EPS) is computed by dividing net income by the weighted average number of common shares outstanding. Diluted net income per common share (Diluted EPS) is computed by dividing net income by the weighted average number of common shares and dilutive common share equivalents and convertible securities then outstanding. SFAS No. 128 requires the presentation of both Basic EPS and Diluted EPS on the face of the consolidated statements of income.

The following provides a reconciliation of information used in calculating the per share amounts for the fiscal years ended June 30 (in thousands, except per share data):

	Net income			Weighted Average Shares			Net income per	
	2008	2007	2006	2008	2007	2006	2008	2007
Basic EPS:	$3,718	$4,217	$6,119	19,263	19,961	19,785	$ 0.19	$ 0.21
Effect of Dilutive Securities: Employee Stock options	--	--	--	539	638	820	--	(.01)
Diluted EPS:	$3,718	$4,217	$6,119	19,802	20,599	20,605	$ 0.19	$ 0.20

Options to purchase 187,700, 87,674 and 37,500 shares of common stock for the three fiscal years ended June 30, 2008, 2007 and 2006, respectively, were not included in the computation of Diluted EPS because the exercise prices exceeded the average market price of the common shares for the respective periods and, accordingly, their inclusion would be anti-dilutive. These options were still outstanding at the end of the respective periods.

Stock-Based Compensation

The Company has established two share incentive programs as discussed in Note 7.

Effective July 1, 2005, the Company adopted SFAS No. 123(R), "Share-Based Payment" ("SFAS No. 123(R)"). This statement replaces SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123") and supersedes APB No. 25. SFAS No. 123(R) requires that all stock-based compensation be recognized as an expense in the financial statements and that such cost be measured at the fair value of the award. This statement was adopted using the modified prospective method of application, which required the Company to recognize compensation expense on a prospective basis. Therefore, prior period financial statements have not been restated. Under this method, in addition to reflecting compensation expense for new share-based awards, expense is also recognized to reflect the remaining service period of awards that had been included in pro-forma disclosures in prior periods. SFAS No. 123(R) also requires that excess tax benefits related to stock option exercises be reflected as financing cash inflows instead of operating cash inflows.

Stock-based compensation costs of $274,000, $412,000 and $396,000 were recognized for fiscal years 2008, 2007 and 2006, respectively. The effect on both Basic and Diluted Earnings per share was $0.01 for fiscal year 2008, $0.02 for fiscal year 2007 and $0.02 for fiscal year 2006.

Foreign Currency

All assets and liabilities of foreign subsidiaries are translated into U.S. Dollars at fiscal year-end exchange rates. Income and expense items are translated at average exchange rates prevailing during the fiscal year. The realized and unrealized gains and losses associated with foreign currency translation, as well as related other comprehensive income, were not material for the three years ended June 30, 2008.

Comprehensive Income

The Company follows the provisions of SFAS No. 130, Reporting Comprehensive Income, which established rules for the reporting of comprehensive income and its components. For the fiscal years ended June 30, 2008, 2007 and 2006, the Company's operations did not give rise to material items includable in comprehensive income, which were not already included in net income.

Accordingly, the Company's comprehensive income approximates its net income for all periods presented.

Segment Reporting

The Company follows the provisions of SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information. Pursuant to this pronouncement, the reportable operating segments are determined based on the Company's management approach. The management approach, as defined by SFAS No. 131, is based on the way that the chief operating decision maker organizes the segments within an enterprise for making operating decisions and assessing performance. The Company's results of operations are reviewed by the chief operating decision maker on a consolidated basis and the Company operates in only one segment. The Company has presented required geographical data in Note 11, and no additional segment data has been presented.

Fair Value of Financial Instruments

The Company calculates the fair value of financial instruments and includes this additional information in the notes to the financial statements where the fair value is different than the book value of those financial instruments. When the fair value approximates book value, no additional disclosure is made. The Company uses quoted market prices whenever available to calculate these fair values. When quoted market prices are not available, the Company uses standard pricing models for various types of financial instruments which take into account the present value of estimated future cash flows. At June 30, 2008 and 2007, management of the Company believes the carrying value of all financial instruments approximated fair value.

Shipping and Handling Revenues and Costs

Emerging Issues Task Force (EITF) Issue No. 00-10, Accounting for Shipping and Handling Revenues and Costs requires that all shipping and handling billed to customers should be reported as revenue and the costs associated with these revenues may be classified as either cost of sales, or selling, general, and administrative costs, with footnote disclosure as to classification of these costs. The Company records the amount billed to customers in net sales ($584,000 and $490,000 in fiscal years 2008 and 2007, respectively) and classifies the costs associated with these revenues in cost of sales ($882,000 and $912,000 in fiscal years 2008 and 2007, respectively).

New Accounting Pronouncements

In May 2008, the FASB issued SFAS No. 162, "The Hierarchy of Generally Accepted Accounting Principles". This Statement identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (GAAP) in the United States (the GAAP hierarchy). This Statement is effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles. The Board does not expect that this Statement will result in a change in current practice. However, transition provisions have been provided in the unusual circumstance that the application of the provisions of this Statement results in a change in practice.

In March 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities - an amendment of FASB Statement No. 133. This statement changes the disclosure requirements for derivative instruments

and hedging activities. Entities are required to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under Statement 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS No. 161 is effective for fiscal years and interim periods beginning after November 15, 2008. The Company's adoption of SFAS No. 161 is not expected to have a material effect on its condensed consolidated financial statements.

In February 2008, the FASB issued FASB Staff Position ("FSP") No. FAS 157-1, "Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13." This FSP amends SFAS No. 157 to exclude certain leasing transactions accounted for under previously existing accounting guidance. However, this scope exception does not apply to assets acquired and liabilities assumed in a business combination, regardless of whether those assets and liabilities are related to leases.

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In February 2008, the FASB issued FSP No. FAS 157-2, "Effective Date of FASB Statement No. 157". This FSP delays the effective date of SFAS No. 157, "Fair Value Measurements", for 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). This FSP defers the effective date of SFAS No. 157 to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years for items within the scope of this FSP.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), "Business Combinations" ("SFAS No. 141(R)"). SFAS No. 141(R) replaces SFAS No. 141, "Business Combinations," however, it retains the fundamental requirements of the former Statement that the acquisition method of accounting (previously referred to as the purchase method) be used for all business combinations and for an acquirer to be identified for each business. SFAS No. 141(R) defines the acquirer as the entity that obtains control of one or more businesses in the business combination and establishes the acquisition date as the date that the acquirer achieves control. Among other requirements, SFAS No. 141(R) requires the acquiring entity in a business combination to recognize the identifiable assets acquired, liabilities assumed and any non-controlling interest in the acquiree at their acquisition-date fair values, with limited exceptions; acquisition-related costs generally will be expensed as incurred. SFAS No. 141(R) requires certain financial statement disclosures to enable users to evaluate and understand the nature and financial effects of the business combination. SFAS No. 141(R) must be applied prospectively to business combinations that are consummated beginning in the Company's fiscal 2010. The Company's adoption of SFAS No. 141(R) is not expected to have a material effect on its condensed consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, "Non-controlling Interests in Consolidated Financial Statements, an Amendment of ARB No. 51" ("SFAS No. 160") to establish accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. Among other requirements, SFAS No. 160 clarifies that a non-controlling interest in a subsidiary, which is sometimes referred to as minority interest, is to be reported as a separate component of equity in the consolidated financial statements. SFAS No. 160 also requires consolidated net income to include the amounts attributable to both the parent and the non-controlling interest and to disclose those amounts on the face of the consolidated statement of income. SFAS No. 160 must be applied prospectively for fiscal years, and interim periods

within those fiscal years, beginning in the Company's fiscal 2010, except for the presentation and disclosure requirements, which will be applied retrospectively for all periods. The Company's adoption of SFAS No. 160 is not expected to have a material effect on its condensed consolidated financial statements.

In December 2007, the U.S. Securities and Exchange Commission issued Staff Accounting Bulletin No. 110 ("SAB 110"). This staff accounting bulletin ("SAB") expresses the views of the staff regarding the use of a "simplified" method, as discussed in SAB No. 107 ("SAB 107"), in developing an estimate of expected term of "plain vanilla" share options in accordance with SFAS No. 123 (revised 2004), Share-Based Payment. In particular, the staff indicated in SAB 107 that it will accept a company's election to use the simplified method, regardless of whether the company has sufficient information to make more refined estimates of expected term. At the time SAB 107 was issued, the staff believed that more detailed external information about employee exercise behavior (e.g., employee exercise patterns by industry and/or other categories of companies) would, over time, become readily available to companies. Therefore, the staff stated in SAB 107 that it would not expect a company to use the simplified method for share option grants after December 31, 2007. The staff understands that such detailed information about employee exercise behavior may not be widely available by December 31, 2007. Accordingly, the staff will continue to accept, under certain circumstances, the use of the simplified method beyond December 31, 2007. The Company's adoption of SAB 111 is not expected to have a material effect on its condensed consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities". SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. Most of the provisions of this Statement apply only to entities that elect the fair value option. However, the amendment to SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities", applies to all entities with available-for-sale and trading securities. Some requirements apply differently to entities that do not report net income. SFAS No. 159 will become effective for the Company in its fiscal year ending June 30, 2009. The Company's adoption of SFAS No. 159 is not expected to have a material effect on its condensed consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements". SFAS No. 157 provides guidance for using fair value to measure assets and liabilities. In addition, this statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. Where applicable, this statement simplifies and codifies related guidance within generally accepted accounting principles. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company's adoption of SFAS No. 157 is not expected to have a material effect on its condensed consolidated financial statements.

Reclassification.

Certain expenses in Cost of sales for 2007 and 2006 have been reclassified to Selling, general and administrative expenses and certain amounts in current inventory in 2007 were reclassified to non-current inventory to conform with the

current years presentation.

NOTE 2 - Business and Credit Concentrations

The Company had two customers with accounts receivable balances that aggregated 34% and 38% of the Company's accounts receivable at June 30, 2008 and 2007, respectively. Sales to neither of these customers exceeded 10% of net sales in any of the past three years.

NOTE 3 - Inventories

Inventories, net of reserves are valued at lower of cost (first-in, first-out method) or market. The Company regularly reviews parts and finished goods inventories on hand and, when necessary, records a provision for excess or obsolete inventories. The Company also regularly reviews the period over which its inventories will be converted to sales. Any inventories expected to convert to sales beyond 12 months from the balance sheet date are classified as non-current.

Inventories, net of reserves consist of the following:

	June 30, 2008	June 30, 2007
	(In thousands)	
Component parts	$ 12,924	$ 15,139
Work-in-process	4,114	3,139
Finished product	10,234	9,945
	$ 27,272	$ 28,223

Classification of inventories, net of reserves:

	2008	2007
Current	$ 19,548	$ 20,389
Non-current	7,724	7,834
	$ 27,272	$ 28,223

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NOTE 4 - Property, Plant, and Equipment

Property, plant and equipment consist of the following:

	June 30, 2008	June 30, 2007	Useful Life
	(In thousands)		

Land	$ 904	$ 904	--
Buildings	8,911	8,911	30 to 40
Molds and dies	4,995	4,925	3 to 5
Furniture and fixtures	1,652	1,630	5 to 10
Machinery and equipment	16,116	15,163	7 to 10
Leasehold improvements	190	190	Shorter of the le
	32,768	31,723	
Less: accumulated depreciation and amortization	23,779	22,588	
	$ 8,989	$ 9,135	

Depreciation and amortization expense on property, plant, and equipment was approximately $1,193,000, $1,201,000 and $1,174,000 in fiscal 2008, 2007 and 2006, respectively.

NOTE 5 - Income Taxes

The (Benefit) provision for income taxes consists of the following:

	For the Years Ended June 30,		
	2008	2007	2006
	(In thousands)		
Current income taxes:			
Federal	$(2,291)	$ 2,069	$ 3,107
State	(8)	15	15
Foreign	8	8	11
	(2,291)	2,092	3,133
Deferred income tax expense (benefit)	883	(170)	131
(Benefit) provision for income taxes	$(1,408)	$ 1,922	$ 3,264

The difference between the statutory U.S. Federal income tax rate and the Company's effective tax rate as reflected in the consolidated statements of income is as follows (dollars in thousands):

	For the Years Ended June 30,				
	2008		2007		2
	Amount	% of Pre-tax Income	Amount	% of Pre-tax Income	Amount
Tax at Federal statutory rate	$ 785	34.0%	$ 2,087	34.0%	$ 3,190
Increases (decreases) in taxes resulting from:					

Meals and entertainment	59	2.6%	60	1.0%	62
State income taxes, net of Federal income tax benefit	(16)	(0.7)%	10	.2%	10
Foreign source income and taxes	(258)	(11.1)%	(5)	(.1)%	(7)
Stock based compensation expense	66	2.9%	99	1.6%	96
Alternative Minimum Tax Credit utilization	--	--	--	--	43
Tax reserve reversal	(2,127)	(92.1)%	(407)	(6.6)%	--
Other, net	83	3.6%	78	1.2	(130)
(Benefit) provision for income taxes	$(1,408)	(61.0)%	$ 1,922	31.3%	$ 3,264

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Deferred tax assets and deferred tax liabilities at June 30, 2008 and 2007 are as follows (in thousands):

	Current Deferred Tax Assets (Liabilities)		Long-Term Deferred Tax Assets (Liabilities)	
	2008	2007	2008	2007
Accounts receivable	$ 26	$ 26	$ --	$ --
Inventories	470	770	273	646
Accrued liabilities	273	254	--	--
State net operating loss carryforward	--	480	--	--
Stock based compensation expense	--	--	107	80
Goodwill	--	--	(1,311)	(1,140)
Property, plant and equipment	--	--	(775)	(821)
FIN 48 Adjustment	0	0	99	0
	769	1,530	(1,607)	(1,235)
Valuation allowance	--	(480)	--	--
Net deferred taxes	$ 769	$ 1,050	$(1,607)	$(1,235)

The Company adopted the provisions of FIN 48 as of July 1, 2007. The Company has identified its U.S. Federal income tax return and its State return in New York as its major tax jurisdictions. As a result the Company increased its accrued income tax liability by $715,000, from $1,836,000 to $2,551,000, to provide for additional reserves for uncertain income tax positions for U.S. Federal and State income tax purposes. The fiscal 2005 and forward years are still open for examination. The increase in the accrued income tax liability of $715,000 was offset in part by a $230,000 increase to a deferred income tax asset, resulting in a net reduction to retained earnings of $485,000 (representing the cumulative effect of adopting FIN 48).

During the year ending June 30, 2008 the Company decreased its reserve for uncertain income tax positions by $ 1,888,000. As of June 30, 2008 the Company has a long-term accrued income tax liability of $ 249,000. The Company's practice is to recognize interest and penalties related to income tax matters in income tax expense and accrued income taxes. As of June 30, 2008, the Company had accrued interest totaling $454,000 and $1,954,000 of unrecognized net tax

benefits (including the related accrued interest and net of the related deferred income tax benefit of $100,000) that, if recognized, would favorably affect the company's effective income tax rate in any future period.

For the year ended June 30, 2008, the company recognized a net benefit to income tax expense of $2,127,000 ($2,257,000 liability reversal including interest, less the related $130,000 reversal of deferred tax asset). This benefit relates predominantly to the company's domestication election, for which the statute of limitations expired during the third quarter.

	Tax	Interest
Balance of gross unrecognized tax benefits as of July 1, 2007	$ 2,137,000	$ 414,000
Reductions to unrecognized tax benefits as a result of a lapse of the applicable statute of limitations	(1,888,000)	(369,000)
Balance of gross unrecognized tax benefits as of June 30, 2008	$ 249,000	$ 45,000

During the quarter ended December 31, 2007 the Company completed a corporate restructuring for which new offshore companies were formed (Napco DR, S.A. and Napco Americas). These newly formed wholly-owned subsidiaries are included in the Company's condensed consolidated financial statements. The existing US-based companies ("Napco US") and these newly formed offshore companies entered into technology licenses and research and development cost sharing agreements. Napco DR. S.A. purchased the majority of the operating assets previously held by the existing Dominican subsidiary. Napco DR, S.A. is doing business in a Free Zone Park in the Dominican Republic and as such is not subject to Dominican corporate income taxes.

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Napco US plans to permanently reinvest a substantial portion of its foreign earnings and as such has not provided US corporate taxes on the permanently reinvested earnings. As of June 30, 2008, the Company had not provided Federal income taxes on approximately $645,000 of undistributed earnings of foreign subsidiaries. The determination and estimation of the future income tax consequences in all relevant taxing jurisdictions involves the application of highly complex tax laws in the countries involved particularly in the United States, and is based on the tax profile of the Company in the year of earnings repatriation. Accordingly, it is not practicable to determine the amount of tax associated with such undistributed earnings.

As of June 30, 2008 the Company generated a US tax loss of approximately $204,000 which is available to be carried back to the fiscal year ended June 30, 2006.

NOTE 6 - Long-Term Debt

As of June 30, 2008, Long-term debt consists of a revolving credit loan facility of $25,000,000 with outstanding borrowings of $12,400,000 at June 30, 2008 and $10,900,000 at June 30, 2007. As of June 30, 2008 the Company was not in compliance with the covenant relating to Tangible Net Worth required under the $25,000,000 facility which was in effect as of June 30, 2008. The Company has

received the appropriate waiver from its bank.

On August 18, 2008, the Company and its banks amended and restated the revolving credit agreement described above. The amended facility is $50,000,000 and provides for a $25,000,000 revolving credit line as well as a $25,000,000 term portion of which the entire $25,000,000 was utilized to finance the asset purchase agreement as described in Note 12. The amended revolving credit agreement and term loan is secured by all the accounts receivable, inventory, the Company's headquarters in Amityville, New York and certain other assets of Napco Security Systems, Inc. and the common stock of three of the Company's subsidiaries. The agreements bear interest at either the Prime Rate or an alternate rate based on LIBOR as described in the agreement. As of June 30, 2008 the interest rate on the outstanding portion of the facility was 4.1%. The August amendment extended the revolving credit agreement to August 2012. Any outstanding borrowings are to be repaid or refinanced on or before that time. The term loan is to be repaid in 19 quarterly installments of $893,000 each commencing in December 2008 and a final payment of $8,033,000 due in August 2013. The agreements contain various restrictions and covenants including, among others, restrictions on payment of dividends, restrictions on borrowings and compliance with certain financial ratios, as defined in the agreement.

NOTE 7 - Stock Options

In December 2002, the stockholders approved the 2002 Employee Stock Option Plan (the 2002 Plan). The 2002 Plan authorizes the granting of awards, the exercise of which would allow up to an aggregate of 1,836,000 shares of the Company's common stock to be acquired by the holders of such awards. Under the 2002 Plan, the Company may grant stock options, which are intended to qualify as incentive stock options (ISOs), to key employees. Any plan participant who is granted ISOs and possesses more than 10% of the voting rights of the Company's outstanding common stock must be granted an option with a price of at least 110% of the fair market value on the date of grant.

Under the 2002 Plan, stock options have been granted to key employees with a term of 10 years at an exercise price equal to the fair market value on the date of grant and are exercisable in whole or in part at 20% per year from the date of grant. At June 30, 2008, 1,371,480 stock options were granted, 464,520 stock options were available for grant, and 1,153,948 stock options were exercisable under this plan.

The fair value of each option granted during fiscal 2008 and 2007 were estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

	2008	2007
Risk-free interest rates	4.65%	4.7%
Expected lives	10 years	7.15 years
Expected volatility	59%	59%
Expected dividend yields	0%	0%

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The following table reflects activity under the 1992 and 2002 Plans for the fiscal years ended June 30,:

2008	2007	2006

	Options	Weighted average exercise price	Options	Weighted average exercise price	Options	We a ex p
Outstanding at beginning of year	1,255,640	$ 2.41	1,333,050	$ 2.41	1,544,940	$
Granted	40,000	5.69	66,500	6.25	161,250	
Exercised	(2,160)	1.62	(139,860)	1.21	(346,680)	
Forfeited	--	--	(4,050)	1.62	(24,300)	
Cancelled/lapsed	--	--	--	--	(2,160)	
Outstanding at end of year	1,293,480	$ 2.84	1,255,640	$ 2.41	1,333,050	$
Exercisable at end of year	1,153,948	$ 2.43	1,048,288	$ 2.24	940,098	$
Weighted average fair value at grant date of options granted	$ 3.62		$ 3.88		$ 6.69	
Total intrinsic value of options exercised	$ 8,000		$ 73,000		$ 191,000	
Total intrinsic value of Options outstanding	$1,506,000					
Total intrinsic value of Options exercisable	$1,081,000					

Cash received from option exercises for fiscal years 2008, 2007 and 2006 was $2,000, $168,000 and $447,000, respectively. The actual tax benefit realized for the tax deductions from option exercises totaled $0, $0 and $210,000 for fiscal years 2008, 2007 and 2006, respectively.

The following table summarizes information about stock options outstanding under the 2002 Plan at June 30, 2008:

	Options outstanding			Options exercisable	
Range of exercise prices	Number outstanding at June 30, 2008	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable at June 30, 2008	Weighted average exercise price
$0.72 to $ 4.00	1,065,730	5.1	$ 1.89	1,030,598	$ 1.89
$4.01 to $ 7.50	190,250	9.5	5.70	100,850	5.70
$7.51 to $11.16	37,500	7.7	11.16	22,500	11.16
	1,293,480	5.5	$ 2.75	1,153,948	$ 2.41

As of June 30, 2008, there was $451,000 of total unearned stock-based compensation cost related to non-vested share-based compensation arrangements granted under the 2002 Plan. That cost is expected to be recognized over a weighted average period of 7 years. The total fair value of the options vested during fiscal 2008 under the 2002 Plan was $255,000.

In September 2000, the stockholders approved a 10 year extension of the already existing 1990 non-employee stock option plan (the 2000 Plan) to encourage

non-employee directors and consultants of the Company to invest in the Company's stock. The 2000 Plan provided for the granting of non-qualified stock options, the exercise of which would allow up to an aggregate of 270,000 shares of the Company's common stock to be acquired by the holders of the stock options. The 2000 Plan provided that the option price will not be less than 100% of the fair market value of the stock at the date of grant. Options were exercisable at 20% per year and expire five years after the date of grant. Compensation cost is recognized for the fair value of the options granted to non-employee directors and consultants as of the date of grant. $19,000 of compensation expense was recorded for stock options granted to directors under the 2000 Plan. There are 24,000 options available for future grants under the 2000 Plan.

The following table reflects activity under the 2000 Plan for the fiscal years ended June 30,:

	2008		2007		2006
	Options	Weighted average exercise price	Options	Weighted average exercise price	Options
Outstanding at beginning of year	30,000	$ 5.03	--	$ --	129,600
Granted	--	--	30,000	5.03	--
Exercised	--	--	--	--	(129,600)
Forfeited	--	--	--	--	--
Cancelled/lapsed	--	--	--	--	--
Outstanding at end of year	30,000	$ 5.03	30,000	$ 5.03	--
Exercisable at end of year	12,000	$ 5.03	6,000	5.03	--
Weighted average fair value at grant date of options granted	n/a		$ 3.16		n/a
Total intrinsic value of options exercised	n/a		n/a		$42,000
Total intrinsic value of Options outstanding	$95,000				
Total intrinsic value of Options exercisable	$38,000				

As of June 30, 2008, there was $51,000 of total unearned stock-based compensation cost related to non-vested share-based compensation arrangements granted under the 2000 Plan. That cost is expected to be recognized over a weighted average period of 3 years.

NOTE 8 - Treasury Stock

On March 16, 2007, the Company announced that its Board of Directors authorized the repurchase of up to one million (1,000,000) shares of its common stock. As of June 30, 2008, the Company has repurchased all 1,000,000 of these shares at a

weighted average price of $5.62 per share.

NOTE 9 - 401(k) Plan

The Company maintains a 401(k) plan covering all U.S. employees with one or more years of service. The plan is qualified under Sections 401(a) and 401(k) of the Internal Revenue Code. The Company provides for matching contributions of 50% of the first 2% of employee contributions. Company contributions to the plan totaled approximately $95,000, $91,000, and $89,000 for the fiscal years ended 2008, 2007 and 2006, respectively.

NOTE 10 - Commitments and Contingencies

Leases

The Company is committed under various operating leases, which do not extend beyond fiscal 2012.

Minimum lease payments through the expiration dates of these leases, with the exception of the land leases referred to below, are as follows:

Year Ending June 30,	Amount
2009	$ 420,000
2010	132,000
2011	30,000
	--
2012	4,000
Total	$ 586,000

Rent expense, with the exception of the land lease referred to below, totaled approximately $167,000, $178,000 and $136,000 for the fiscal years ended June 30, 2008, 2007 and 2006, respectively.

Land Lease

On April 26, 1993, one of the Company's foreign subsidiaries entered into a 99 year lease, expiring in 2092, for approximately four acres of land in the Dominican Republic, at an annual cost of approximately $288,000, on which the Company's principal production facility is located.

Letters of Credit

At June 30, 2008, the Company was committed for approximately $150,000 under open commercial letters of credit.

Litigation

In the normal course of business, the Company is a party to claims and/or litigation. Management believes that the settlement of such claims and/or litigation, considered in the aggregate, will not have a material adverse effect on the Company's financial position and results of operations.

Employment Agreements

As of June 30, 2008, the Company was obligated under three employment agreements and one severance agreement. Compensation under the agreements includes annual salaries approximating $1,105,000. The employment agreements provide for annual bonuses based upon sales and profits, or a formula to be determined by the Board of Directors, and various severance payments as defined in each agreement. The agreement with the Company's Chief Executive Officer provides for a salary of $587,000, includes additional compensation of 25,000 stock options that vest 20% per year or upon a change in control, as defined, and a termination payment in an amount equal to 299% of the average of the prior five calendar year's compensation, subject to certain limitations, as defined. The employment agreements expire at various times through October 2010.

NOTE 11 - Geographical Data

The Company is engaged in one major line of business: the development, manufacture, and distribution of security alarm products and door security devices for commercial and residential use. Sales to unaffiliated customers are primarily shipped from the United States. The Company has customers worldwide with major concentrations in North America, Europe, and South America.

The Company observes the provisions of SFAS No. 131. The following represents selected consolidated geographical data for and as of the fiscal years ended June 30, 2007, 2006, and 2005:

	2008	2007	2006
		(in thousands)	
Sales to external customers(1):			
Domestic	$56,122	$56,810	$58,549
Foreign	12,245	9,392	10,999
Total Net Sales	$68,367	$66,202	$69,548
Identifiable assets:			
United States	$50,056	$47,636	
Dominican Republic (2)	19,841	21,246	
Other foreign countries	6,826	7,903	
Total Identifiable Assets	$76,723	$76,785	

(1) All of the Company's sales occur in the United States and are shipped primarily from the Company's facilities in the United States and United Kingdom. There were no sales into any one foreign country in excess of 10% of total net sales.

(2) Consists primarily of inventories and fixed assets, which are located at the Company's principal manufacturing facility in the Dominican Republic.

NOTE 12 - Subsequent Event

On August 18, 2008, the Company acquired substantially all of the assets and business of G. Marks Hardware, Inc. ("Marks") for $25 million, the repayment of

$1 million of bank debt and the assumption of current liabilities as described more fully in the Asset Purchase Agreement. The Marks business involves the manufacturing and distribution of door-locking devices. The Company completed this acquisition at a price in excess of the value of the net identifiable assets because it believes that the combination of the two companies offers the potential for manufacturing and operational synergies as the Company combines the Marks operations and production into its own door-locking operations and production structure. The Company funded the acquisition with a term loan from its lenders as described in Note 6.

The acquisition described above will be accounted for as a purchase and was valued based on management's estimate of the fair value of the assets acquired and liabilities assumed. The estimates of fair value are preliminary and subject to adjustment for a period of up to one year from the date of acquisition. Costs in excess of identifiable net assets acquired will be allocated to goodwill in the first quarter of fiscal 2009.

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SCHEDULE II

NAPCO SECURITY SYSTEMS, INC. AND SUBSIDIARIES
VALUATION AND QUALIFYING ACCOUNTS

Years Ended June 30, 2008, 2007, and 2006 (In Thousands)

Column A	Column B	Column C	Column D	Column E
Description	Balance at Beginning of period	Charged to costs and expenses	Deductions/ (recoveries) (1)	Balance at end of period
For the year ended June 30, 2006:				
Allowance for doubtful accounts (deducted from accounts receivable)	$380	$ 70	$ 30	$420
For the year ended June 30, 2007:				
Allowance for doubtful accounts (deducted from accounts receivable)	$420	$(55)	$ --	$365
For the year ended June 30, 2008:				
Allowance for doubtful accounts (deducted from accounts receivable)	$365	$ 44	$ 4	$405

(1) Deductions relate to uncollectible accounts charged off to valuation accounts, net of recoveries.

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b. SUPPLEMENTARY FINANCIAL DATA (UNAUDITED)

QUARTERLY RESULTS

The following table sets forth unaudited financial data for each of the Company's last eight fiscal quarters (in thousands except for per share data):

	Fiscal Year Ended June 30, 2008,			
	First Quarter(1)	Second Quarter(1)	Third Quarter(1)	Fou
Net Sales	$ 13,876	$ 16,166	$ 16,222	
Gross Profit as previously reported (2)	5,129	5,256	5,523	
Reclassification (2)	95	191	193	
Gross Profit as Reclassified (2)	5,224	5,447	5,716	
Income (loss) from Operations	803	1,285	1,568	
Net Income (loss)	374	1,172	3,277	
Net Income (loss) Per Share(1):				
Basic EPS	.02	.06	.17	
Diluted EPS	.02	.06	.17	

	Fiscal Year Ended June 30, 2007,		
	First Quarter	Second Quarter	Third Quarter
Net Sales	$ 14,029	$ 16,077	$ 15,566
Gross Profit as previously reported (2)	5,559	5,825	5,494
Reclassification (2)	203	182	209
Gross Profit as Reclassified (2)	5,762	6,007	5,703
Income from Operations	1,561	1,844	1,268
Net Income	952	1,144	1,132
Net Income Per Share			
Basic EPS	.05	.06	.06
Diluted EPS	.05	.06	.06

(1) Gross profit for the fourth quarter of fiscal 2008 was adversely affected by the recognition of certain material and factory expenses in the fourth quarter that should have been charged to cost of goods sold during the first nine months of fiscal 2008. This was due to certain changes in the business not considered when applying the gross profit method of estimating inventory and cost of sales for the interim reporting periods.

(2) Certain expenses in Cost of sales for 2007 have been reclassified to Selling, general and administrative expenses

Seasonality

The Company's fiscal year begins on July 1 and ends on June 30. Historically, the end users of Napco's products want to install its products prior to the summer; therefore sales of its products peak in the period April 1 through June 30, the Company's fiscal fourth quarter, and are reduced in the period July 1 through September 30, the Company's fiscal first quarter. To a lesser degree, sales in Europe are also adversely impacted in the Company's first fiscal quarter because of European vacation patterns, i.e., many distributors and installers are closed for the month of August.

ITEM 9: CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None

ITEM 9A: CONTROL AND PROCEDURES

Evaluation of Disclosure Controls and Procedures. At the conclusion of the period ended June 30, 2008, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective.

Management's Annual Report on Internal Control Over Financial Reporting. Management's Report on Internal Control Over Financial Reporting on page FS-1 is incorporated herein by reference.

Attestation Report of the Registered Public Accounting Firm. Report of Independent Registered Public Accounting Firm on page FS-2 is incorporated herein by reference.

Changes in Internal Control Over Financial Reporting. During the fourth quarter of 2008, there were changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. Management implemented internal controls to addresses the material weakness reported in its prior year Annual Report on Form 10-K related to the valuation of inventory. With respect to its overhead estimation methodology, while the technique used to make this estimate has not changed, the amount of the costs used in the estimate has significantly decreased since the prior year and is expected to continue to decrease. Thus, management does not believe that its use of this estimation technique continues to have a material impact on its financial information. Furthermore, management incorporated additional reviews of obsolete and slow moving parts by additional members of management. Management also prepared a draft obsolescence review prior to the end of the year to facilitate the formal review. Management now conducts weekly meetings to update the status of obsolete or slow moving parts. Management has previously disclosed its remediation efforts of the material weakness related to the classification of inventory, and this weakness has been fully remediated. Additionally, management's current year assessment over it's internal controls identified conditions which they deemed to be material weaknesses, (as defined by standards established by the SEC and the Public Company Accounting Oversight Board) with respect to detecting inaccuracies in the costing of inventory and the recognition of expenses in cost of sales for our interim reporting. Management has informed its independent auditors and the Audit Committee that it has certain controls in place to detect significant costing inaccuracies, however certain of these were not performed because management had time constraints associated with the efforts involved with its acquisition, an event that is not typical during the financial reporting process. As part of its remediation efforts, management plans on revising its inventory controls to ensure that the proper procedures are carried out in future periods. Management also has informed its independent auditors and the Audit Committee that it intends to develop new controls that will permit it to identify new variables and changes in the business when they occur in order to better estimate its interim inventory and cost of sales. Management will continue to monitor the effectiveness of these actions and will make any other changes or take such additional actions as management determines to be appropriate. Management expects to complete this action during fiscal 2009.

ITEM 9B: OTHER INFORMATION

None

PART III

The information called for by Part III is hereby incorporated by reference from the information set forth under the headings "Election of Directors", "Corporate Governance and Board Matters", "Executive Compensation", "Beneficial Ownership of Common Stock" and "Principal Accountant Fees" in the Company's definitive proxy statement for the 2008 Annual Meeting of Stockholders, to be filed with the Securities and Exchange Commission pursuant to Regulation 14A within 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K.

We have adopted a Code of Ethics which applies to our senior executive and financial officers, among others. The Code is posted on our website, www.napcosecurity.com under the "Investors - Other" captions. We intend to make all required disclosures regarding any amendment to, or waiver of, a provision of the Code of Ethics for senior executive and financial officers by posting such information on our website.

PART IV

ITEM 15: EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.

(a)1. Financial Statements

The following consolidated financial statements of NAPCO Security Systems, Inc. and its subsidiaries are included in Part II, Item 8:

	Page
Management Report on Internal Controls Over Financial Reporting	FS-1
Report of Independent Registererd Public Accounting Firm on Internal Control Over Financial Reporting	FS-2
Report of Independent Registered Public Accounting Firm	FS-3
Consolidated Financial Statements:	
Consolidated Balance Sheets as of June 30, 2008 and 2007	FS-4
Consolidated Statements of Income for the Fiscal Years Ended June 30, 2008, 2007 and 2006	FS-6
Consolidated Statements of Stockholders' Equity for the Fiscal Years Ended June 30, 2008, 2007 and 2006	FS-7
Consolidated Statements of Cash Flows for the Fiscal Years Ended June 30, 2008, 2007 and 2006	FS-8

Notes to Consolidated Financial Statements, June 30, 2008 FS-9

(a)2. Financial Statement Schedules

The following consolidated financial statement schedules of NAPCO Security Systems, Inc. and its subsidiaries are included in Part II, Item 8:

	Page
II: Valuation and Qualifying Accounts	FS-21
B. Supplementary Financial Data	FS-22

Schedules other than those listed above are omitted because of the absence of the conditions under which they are required or because the required information is shown in the consolidated financial statements and/or notes thereto.

(a)3 and (b). Exhibits

Management Contracts designated by asterisk.

Exhibit No.	Title	
Ex-3.(i)	Certificate of Amendment of Certificate of Incorporation	Exhibit-3.(i fiscal year
Ex-3.(ii)	Certificate of Incorporation as amended	Exhibit-3.(i fiscal year
Ex-3.(iii)	Amended and Restated By-Laws	Exhibit 3.(i fiscal year
Ex-10.A (i)	Amended and Restated 1992 Incentive Stock Option Plan	Exhibit 10.A fiscal year
Ex-10.A (ii)	2002 Employee Stock Option Plan	E-10.A
Ex-10.B	2000 Non-Employee Stock Option Plan	Exhibit-10.B fiscal year
Ex-10.C	Loan and Security Agreement with Marine Midland Bank dated as of May 12, 1997	Exhibit 10-C fiscal year
Ex-10.D	Revolving Credit Note #1 to Marine Midland Bank dated as of May 12, 1997	Exhibit 10-D fiscal year
Ex-10.E	Revolving Credit Note #2 to Marine Midland Bank dated as of May 12, 1997	Exhibit 10-E fiscal year

Exhibit No.	Title	
Ex-10.F	Promissory Note to Marine Midland Bank dated as of May 12, 1997	Exhibit 10-F fiscal year
Ex-10.G	Amendment No.1 to the Loan and Security Agreement with Marine Midland Bank dated as of May 28, 1998	Exhibit 10-G fiscal year
Ex-10.H	Term Loan Note to Marine Midland Bank dated as of May 28, 1998	Exhibit 10-H fiscal year
*Ex-10.I	Amended and Restated Employment Agreement with Richard Soloway	Exhibit 10.I fiscal year
*Ex-10.J	Employment Agreement with Jorge Hevia	Exhibit 10-J fiscal year
Ex-10.K	Amendment No. 2 to the Loan and Security Agreement with HSBC Bank dated as of June 30, 1999	Exhibit 10-K fiscal year
*Ex-10.L	Employment Agreement with Michael Carrieri	Exhibit 10-L fiscal year
*Ex-10.M	Indemnification Agreement dated August 9, 1999	Exhibit 10-M fiscal year
Ex-10.O	Amendment No. 4 to Loan and Security Agreement	Exhibit 10-O fiscal year
Ex-10.P	Amendment No. 8 to Loan and Security Agreement	Exhibit-10.P fiscal year
Ex-10.Q	Note Modification Agreement	Exhibit 10.X fiscal year
Ex-10.R	Amendment No. 10 to the Loan and Security Agreement	Exhibit 10.R fiscal year
Ex-10.S	Amendment No. 3 to the Loan and Security Agreement	Exhibit 10-S fiscal year
Ex-10.T	Amendment No. 9 to the Loan and Security Agreement	Exhibit 10-T fiscal year
Ex-10.U	Amendment No. 11 to the Loan and Security Agreement	Exhibit 10-U fiscal year
Ex-10.V	Amendment No. 12 to the Loan and Security Agreement	Exhibit 10-V fiscal year
Ex-10.W	Amendment No. 13 to the Loan and Security Agreement	Exhibit 10-W fiscal year
Ex-14.0	Code of Ethics	Exhibit 14.0 fiscal year

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Exhibit No.	Title	
Ex-21.0	Subsidiaries of the Registrant	E-18
Ex-23.1	Consent of Independent Auditors	E-19
Ex-31.1	Section 302 Certification of Chief Executive Officer	E-20
Ex-31.2	Section 302 Certification of Chief Financial Officer	E-21
Ex-32.1	Certification of Chief Executive Officer Pursuant to 18 USC Section 1350 and Section 906 of Sarbanes - Oxley Act of 2002	E-22
Ex-32.2	Certification of Chief Financial Officer Pursuant to 18 USC Section 1350 and Section 906 of Sarbanes - Oxley Act of 2002	E-23

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SIGNATURES

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

September 30, 2008

NAPCO SECURITY SYSTEMS, INC.
(Registrant)

By: /s/RICHARD SOLOWAY

Richard Soloway
Chairman of the Board of
Directors, President and Secretary
(Principal Executive Officer)

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

Signature	Title	Date
/s/RICHARD SOLOWAY Richard Soloway	Chairman of the Board of Directors, President and Secretary and Director (Principal Executive Officer)	September 30, 2008

/s/KEVIN S. BUCHEL ---------------------- Kevin S. Buchel	Senior Vice President of Operations and Finance and Treasurer and Director (Principal Financial and Accounting Officer)	September 30, 2008
/s/PAUL STEPHEN BEEBER ---------------------- Paul Stephen Beeber	Director	September 30, 2008
/s/RANDY B. BLAUSTEIN ---------------------- Randy B. Blaustein	Director	September 30, 2008
/s/ARNOLD BLUMENTHAL ---------------------- Arnold Blumenthal	Director	September 30, 2008
/s/DONNA SOLOWAY ---------------------- Donna Soloway	Director	September 30, 2008
/s/ANDREW J. WILDER ---------------------- Andrew J. Wilder	Director	September 30, 2008