

CSP INC /MA/
Form DEF 14A
March 30, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

SCHEDULE 14A

(Rule 14a-101)

INFORMATION REQUIRED IN PROXY STATEMENT

SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a) of the
Securities Exchange Act of 1934 (Amendment No.)

Filed by the Registrant ☒ Filed by a Party other than the Registrant ☐

Check the appropriate box:

☐ Preliminary Proxy Statement

☐ **Confidential, for Use of the Commission only** (as permitted by Rule 14a-6(e)(2))

☒ Definitive Proxy Statement

☐ Definitive Additional Materials

☐ Soliciting Material Pursuant to Sec. 240.14a-12

CSP INC.

(Name of Registrant as Specified In Its Charter)

Not Applicable

(Name of Person(s) Filing Proxy Statement)

Payment of Filing Fee (Check the appropriate box)

☒ No fee required.

☐ Fee computed on table below per Exchange Act Rules 14a-6(i) (1) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid:

☐ Fee paid previously with preliminary materials.

☐ Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the form or schedule and the date of its filing.

(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

CSP INC.

March 30, 2007

Dear Stockholders:

You are cordially invited to attend the 2007 Annual Meeting of Stockholders of CSP Inc. Our Annual Meeting will be held Tuesday, May 8, 2007 at 9:00 a.m. at our executive offices located at 43 Manning Road, Billerica, Massachusetts 01821.

We describe in detail the actions we expect to take at our Annual Meeting in the attached Notice of 2007 Annual Meeting of Stockholders and proxy statement.

Your vote is very important to us, regardless of the number of shares that you own. Whether or not you plan to attend the Annual Meeting, please vote as soon as possible to make sure your shares are represented at the meeting. To simplify this process, your vote may be cast by mail.

We look forward to seeing you at the Annual Meeting.

Sincerely,

Alexander R. Lupinetti

Chief Executive Officer

CSP INC.

NOTICE OF 2007 ANNUAL MEETING OF STOCKHOLDERS

Date: Tuesday, May 8, 2007

Time: 9:00 a.m.

Place: CSP Inc. Executive Offices
43 Manning Road
Billerica, Massachusetts 01821

At the Annual Meeting you will be asked to:

1. Elect two Class II directors as members of the Board of Directors;
2. Approve and adopt our 2007 Stock Incentive Plan, which covers 250,000 shares of our common stock and provides for the grant of incentive and non-statutory stock options and awards of restricted and unrestricted stock; and
3. Consider any other matters that may properly be brought before the meeting.

By order of the Board of Directors,

Gary W. Levine

Secretary

Billerica, Massachusetts

March 30, 2007

**PLEASE VOTE BY COMPLETING, SIGNING, DATING AND RETURNING
THE PROXY CARD AS PROMPTLY AS POSSIBLE.**

CSP INC.

(A Massachusetts Corporation)

PROXY STATEMENT

Annual Meeting of Stockholders

May 8, 2007

INFORMATION CONCERNING THE PROXY MATERIALS AND THE ANNUAL MEETING

Our Board of Directors is soliciting proxies to be voted at the 2007 Annual Meeting of Stockholders to be held on May 8, 2007. Your vote is very important. For this reason, our Board is requesting that you permit your common stock to be represented at the Annual Meeting by the persons named as proxies on the enclosed card. This proxy statement contains important information for you to consider when deciding how to vote on the matters brought before the Annual Meeting. Please read it carefully.

Voting materials, which include this proxy statement, the proxy card and our annual report on Form 10-K for the fiscal year ended September 30, 2006, were mailed to stockholders beginning March 30, 2007. CSP Inc.'s principal executive offices are located at 43 Manning Road, Billerica, Massachusetts 01821. CSP Inc.'s main telephone number is (978) 663-7598. In this proxy statement, CSP Inc. is referred to as the Company and CSPI.

QUESTIONS AND ANSWERS REGARDING THE ANNUAL MEETING

Where and when is the Annual Meeting of the stockholders?

Our annual meeting of stockholders will be held at our executive offices, 43 Manning Road, Billerica, Massachusetts at 9:00 a.m. local time on May 8, 2007.

Who may vote at the Annual Meeting?

You may vote if our records show that you owned your shares on March 12, 2007, which is the record date. At the close of business on the record date, 3,782,980 shares of our common stock were issued and outstanding and eligible to vote. You may cast one vote for each share of common stock held of record by you on the record date on all matters presented.

What is the difference between holding shares as a stockholder of record and beneficial owner?

Most of our stockholders hold their shares through a broker, bank or other nominee rather than directly in their own name. As summarized below, there are some distinctions between shares held of record and those owned beneficially.

Stockholder of Record. If your shares are registered directly in your name with our transfer agent, American Stock Transfer Co., you are considered the stockholder of record with respect to those shares, and these proxy materials are being sent directly to you by us. As the stockholder of record, you have the right to grant your voting proxy directly to us or to vote in person at the annual meeting. We have enclosed a proxy card for you to use.

Beneficial Owner. If your shares are held in a stock brokerage account or by a bank or other nominee, you are considered the beneficial owner of shares, which are held in street name, and these proxy materials are being forwarded to you by your broker, bank or nominee who is considered the stockholder of record with respect to those shares. As the beneficial owner, you have the right to direct your broker, bank or nominee on how to vote and are also invited to attend the Annual Meeting. However, since you are not the stockholder of record, you may not vote these shares in person at the Annual Meeting, unless you request, complete and deliver a proxy from your broker, bank or nominee. Your broker, bank or nominee has enclosed a voting instruction card for you to use in directing the broker, bank or nominee regarding how to vote your shares.

How many votes can be cast by all stockholders?

Each share of our common stock is entitled to one vote. There is no cumulative voting. We had 3,782,980 shares of common stock outstanding and entitled to vote on the record date.

How many votes must be present to hold the Annual Meeting?

We must have a quorum in order to hold the Annual Meeting and conduct business. A majority of our issued and outstanding shares as of the record date constitutes a quorum. Shares are counted if you are present at the Annual Meeting or a proxy card has been properly submitted by you or on your behalf. In general, abstentions and broker non-votes are counted as present for the purpose of determining the presence of a quorum. The vote on each matter submitted to stockholders is tabulated separately. American Stock Transfer & Trust Company will tabulate the votes.

How many votes are required to elect directors?

Directors are elected by a *plurality* of the votes cast. This means that the two individuals nominated for election to the Board of Directors who receive the most FOR votes (among votes properly cast in person or by proxy) will be elected; nominees do not need to receive a majority to be elected. If you withhold authority to vote with respect to the election of some or all of the nominees, your shares will not be voted with respect to those nominees indicated. Your shares will be counted for purposes of determining whether there is a quorum.

How many votes are required to approve the 2007 Stock Incentive Plan?

If a quorum is present, approval of the 2007 Stock Incentive Plan requires a majority of the total votes cast on the proposal in person or by proxy to be FOR votes. Although they are counted as present for quorum purposes, broker non-votes are not treated as votes cast.

What if I don't vote for the item listed on my proxy card or voting instruction card?

If you return your signed proxy card or voting instruction card in the enclosed envelope, but do not mark selections, it will be voted in accordance with the recommendations of the Board of Directors. If you indicate a choice with respect to any matter to be acted upon on your proxy card or voting instruction card, the shares will be voted in accordance with your instructions.

If you are a beneficial owner and hold your shares through a broker and do not return the voting instruction card, the broker or other nominee will determine if it has discretionary authority to vote on the particular matter. Under the rules that govern brokers who are voting with respect to shares held in street name, brokers have discretion to vote such shares on routine matters, but not on non-routine matters. Routine matters include the election of directors (excluding contested elections of directors) and ratification of auditors. Non-routine matters include matters such as the adoption of stock plans. If the broker determines it does not have discretionary authority to vote on a particular matter, it will indicate a broker non-vote for such matter in the proxy. Broker non-votes are treated as present for purposes of determining the presence of a quorum,

but are also treated as not entitled to vote.

Can I change or revoke my vote after I return my proxy card?

Yes. Even if you sign the proxy card or voting instruction card in the form accompanying this proxy statement, you retain the power to revoke your proxy or change your vote. You can revoke your proxy or change your vote at any time before it is exercised by giving written notice to our secretary, specifying such revocation. You may change your vote by timely delivery of a valid, later-dated proxy or by voting by ballot at the Annual Meeting if you are a record holder.

Who can attend the Annual Meeting?

All stockholders as of the record date, or their duly appointed proxies, may attend. Each stockholder may also bring guests to the meeting if there is space available.

Where can I find more information?

We file annual, quarterly and current reports, proxy statements, and other information with the Securities and Exchange Commission (SEC). Our common stock is traded on the NASDAQ Global Market (NASDAQ) under the symbol **CSPI**. You may read and copy any document that we file at the SEC's Public Reference Room at 100 F. Street, N.E., Washington, D.C. 20549. Our SEC filings are also available to the public on the SEC's website at <http://www.sec.gov>.

Who can help answer your questions?

If you have additional questions about the matters proposed for consideration at the Annual Meeting, you should contact:

CSP Inc.

43 Manning Road

Billerica, MA 01821

Attn: Gary W. Levine, Chief Financial Officer

Phone: (978) 663-7598 ext. 1200

What should I do now?

Carefully read this document and indicate on the proxy card how you want to vote. Sign, date and mail your proxy card in the enclosed prepaid return envelope as soon as possible. You should indicate your vote now even if you expect to attend the Annual Meeting and vote in person. Indicating your vote now will not prevent you from later canceling or revoking your proxy right until the meeting, and will ensure that your shares are voted if you later find you cannot attend the Annual Meeting.

How do I find out the voting results?

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Preliminary voting results will be announced at the Annual Meeting, and the final voting results will be published in our quarterly report on Form 10-Q for the quarter ending June 30, 2007, which we will file with the SEC.

After the Form 10-Q is filed, you may obtain a copy by visiting our website or the SEC's website, or by contacting our investor relations department by calling 978-663-7598 or by writing to Investor Relations, CSP Inc., 43 Manning Road, Billerica, Massachusetts 01821.

What if I have questions about lost stock certificates or I need to change my mailing address?

Stockholders may contact our transfer agent, American Stock Transfer Co., 59 Maiden Lane, New York, New York 10038.

PROPOSAL ONE:

ELECTION OF DIRECTORS

Our Board currently consists of five members and is divided into three classes, referred to as Class I, Class II and Class III. The directors in each class serve for a term of three years and until their successors are duly elected and qualified. As the term of one class expires, a successor class is elected at the annual meeting of stockholders for that year. We currently have two Class II Directors, whose term will expire at the Annual Meeting to be held on May 8, 2007; two Class III Directors, whose terms will expire at the 2008 Annual Meeting; and one Class I director, whose term will expire at the 2009 Annual Meeting.

Our Nominating Committee has nominated Messrs. Lyons and Hall to serve as Class II Directors for a three-year term.

If you withhold authority to vote with respect to the election of some or all of the nominees, your shares will not be voted with respect to those nominees indicated. Your shares will be counted for purposes of determining whether there is a quorum.

Messrs. Lyons and Hall are currently members of our Board. Although we expect each nominee to accept nomination and to serve if elected, if he is unable to serve at the time of election, then proxies will be voted for another nominee or the Board may fix the number of directors at a lesser number.

Nominees for election

Listed below are the nominees with their ages, the year each was first elected as a director of the Company, and their business affiliations.

Name, Age and Class	Year first became Director, Principal Occupation during past five years and Certain Directorships
J. David Lyons (68) Class II	Director of CSPI since March 1997; Managing Director for the Carter Group, an executive search firm from September 2002 to June 2004; President of Aubin International, Inc., an executive search firm from 1996 to October 2002; Executive Vice President at National Data Corp. from 1993 to 1996; Executive Vice President -- Sales and Marketing, Syncordia from 1991 to 1993.
Christopher J. Hall (48) Class II	Director of CSPI since November 2002, self employed as a municipal bond investor from 1998 to present; Founder and Chief Financial Officer of Howe, Solomon, & Hall, a registered broker-dealer operating primarily as a municipal securities broker-dealer from 1985 to 1998.

The Board recommends that you vote FOR the election of the nominees for director listed in this proxy statement.

Directors

Listed below are the Company's continuing directors, with information showing the age of each, the year each was first elected as one of our directors, and the business affiliations of each. Messrs. James and Lupinetti are Class III Directors, whose terms will expire in 2008. Mr. Williams is a Class I Director, whose term will expire in 2009.

Name, Age and Class	Business Affiliations
C. Shelton James (67) Class III Director	Director of CSPI since 1994; Principal, C. Shelton James Associates, a business consulting firm, from 1990 to present; President from 1993 until June 1998 and Director from 1993 until February 2000 of Fundamental Management Corporation; Director until March 2000 and Chief Executive Officer from August 1998 to March 1999 of Cyberguard Corp.; Director from August, 1998 to July 2002 and Chief Executive Officer from December 2001 to July 2002 of Technisource, Inc.; Chief Executive Officer and Chairman of the Board of Elcotel from May 1991 to February 2000; Director of DRS Technologies and Concurrent Computer Corporation.
Alexander R. Lupinetti (61) Class III Director	Director of CSPI since 1996; Chairman of the Board of Directors since January 1998; Chief Executive Officer and President of CSPI since October 1996; Director of Vertical Buyer, Inc. from February 2000 until March 2001.
Robert M. Williams (68) Class I Director	Director of CSPI since July 1998; from 1995 to his retirement in March 1999, served as Vice President for Asia, Africa and the Near East of International Executive Corps, a company that directs technology and business programs as a contractor for the US Foreign Aid Program; consultant to RM Williams Associations Technology from 1993 to 1995; Vice President of Worldwide Development, Industrial Sector Division for International Business Machines Corp., and served in various positions from 1963 to 1993.

Executive Officers

In addition to Mr. Lupinetti, the Company has two executive officers, who are listed below with information showing their ages and business affiliations.

Name and Age	Business Affiliations
Gary W. Levine (58)	Vice President of Finance and Chief Financial Officer of CSPI since September 1983; Controller of CSPI from May 1983 to September 1983.
William E. Bent, Jr. (50)	Vice President of CSPI and General Manager of MultiComputer Division since July 2000; Vice President of Engineering for MultiComputer Division from October 1999 to July 2000; Director of Engineering for MultiComputer Group from March 1996 to October 1999; Senior Technical Manager of Optronics, an Intergraph Division, from 1989 to March 1996.

Executive compensation

Summary compensation table. The following table sets forth certain information about the compensation we paid or accrued with respect to our chief executive officer and our most highly compensated officers (other than our chief executive officer) who served as executive officers during fiscal 2006 and whose annual compensation exceeded \$100,000 for fiscal 2006.

Other annual compensation in the form of perquisites and other personal benefits has been omitted as the aggregate amount of those perquisites and other personal benefits was less than \$50,000 and constituted less than ten percent (10%) of the executive officers' respective total annual salary and bonus.

SUMMARY COMPENSATION TABLE

Name and Principal Position	Year	Annual Compensation		Long Term Compensation	
		Salary	Bonus	Securities Underlying Options	All Other Compensation
Alexander R. Lupinetti Chairman, President and Chief Executive Officer	2006	\$ 341,936	\$	20,000	\$ 64,741(1)
	2005	\$ 314,995	\$ 146,475	40,000	\$ 67,481(2)
	2004	\$ 310,520	\$ 436,300		\$ 64,363(3)
Gary W. Levine Vice President of Finance and Chief Financial Officer	2006	\$ 155,143	\$	4,000	\$ 35,268(4)
	2005	\$ 155,581	\$ 42,771	8,000	\$ 37,238(5)
	2004	\$ 143,905	\$ 127,546		\$ 36,023(6)
William Bent	2006	\$ 253,721	\$	2,500	\$ 3,707(7)

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Vice President and General Manager of	2005	\$ 220,264	\$ 49,694	5,000	\$	7,124(7)
CSP MultiComputer Division	2004	\$ 201,822	\$ 49,011	2,000	\$	4,988(7)

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- (1) Consists of a \$ 9,666 contribution by the Company to Mr. Lupinetti's 401(k) plan and \$55,075 for a split dollar life insurance policy for his benefit.
 - (2) Consists of a \$12,031 contribution by the Company to Mr. Lupinetti's 401(k) plan and \$55,450 for a split dollar life insurance policy for his benefit.
 - (3) Consists of a \$8,733 contribution by the Company to Mr. Lupinetti's 401(k) plan and \$55,630 for a split dollar life insurance policy for his benefit.

- (4) Consists of a \$4,858 contribution by the Company to Mr. Levine's 401(k) plan and \$30,410 for a split dollar life insurance policy for his benefit.
- (5) Consists of a \$6,743 contribution by the Company to Mr. Levine's 401(k) plan and \$30,495 for a split dollar life insurance policy for his benefit.
- (6) Consists of a \$5,293 contribution by the Company to Mr. Levine's 401(k) plan and \$30,730 for a split dollar life insurance policy for his benefit.
- (7) Represents contributions by the Company to the officer's 401(k) plan.

Option Grants Table. The following table sets forth certain information about stock options granted during the fiscal year ended September 30, 2006 by the Company to the executive officers named in the Summary Compensation Table:

OPTIONS GRANTED IN LAST FISCAL YEAR

Name	Option	% of Total Options Granted Employees in	Exercise Price Per Share	Expiration	Potential Realized	
					Value at Assumed	
					Annual Rates of Stock	
					Price Appreciation for	
	Grants	Fiscal Year	(\$/SH)(1)	Date	Option Terms (2)	
					5%	10%
William Bent	2,500	5%	\$ 6.50	1/17/16	\$ 10,220	\$ 25,898
Gary W. Levine	4,000	8%	\$ 6.50	1/17/16	\$ 16,351	\$ 41,437
Alexander R. Lupinetti	20,000	42%	\$ 6.50	1/17/16	\$ 81,756	\$ 207,187

- (1) Stock options were granted at an exercise price equal to the fair market value of the Company's common stock on the date of the grant. The stock options expire ten years from the date of grant.
- (2) Amounts reported in these columns represent amounts that may be realized upon exercise. These values have not been and may never be realized. Actual gains, if any, will depend on the value of the common stock on the date of sale of the shares.

Fiscal Year-End Option Table. The following table sets forth certain information regarding stock options held as of September 30, 2006 by the executive officers named in the Summary Compensation Table.

AGGREGATED OPTION EXERCISES IN LAST FISCAL YEAR AND FISCAL YEAR-END OPTION VALUES

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Name	Shares Acquired	Value	Number of Securities Underlying Unexercised Options at Fiscal Year-End		Value of Unexercised In-the-Money Options at Fiscal Year-End (1)	
	on Exercise	Realized	Exercisable	Unexercisable	Exercisable	Unexercisable
Alexander R. Lupinetti	32,060	\$ 44,258	280,615	43,125	\$ 955,227	\$ 57,025
Gary W. Levine	295	\$ 988	23,417	10,000	\$ 73,866	\$ 8,720
William Bent		\$	15,582	9,250	\$ 53,951	\$ 12,615

- (1) Value is based on the last sales price of our common stock (\$8.68) on September 30, 2006, the last day of fiscal 2006 on which a trade in the common stock was reported by NASDAQ, less the applicable option exercise price. These values have not been and may never be realized. Actual gains, if any, will depend on the value of the common stock on the date of sale of the shares.

Employment contracts and termination of employment and change-in-control arrangements

We have an employment agreement with Mr. Lupinetti dated September 12, 1996, pursuant to which he became one of our directors and our Chief Executive Officer and President. Effective November 14, 2006, Mr. Lupinetti's base salary under the agreement was increased to \$340,000. Mr. Lupinetti is also eligible to receive a bonus based on the attainment of certain financial objectives. Mr. Lupinetti has received stock options periodically since his initial employment, and he currently holds stock options to acquire 316,500 shares of our common stock. These options vest quarterly over a period of four years from date of grant. However, if we are acquired by way of a sale of substantially all of our assets or by merger, the options will fully vest at the time of such acquisition. We also provide Mr. Lupinetti with an automobile. In the event that Mr. Lupinetti's employment is terminated by us other than for cause (as defined), he will be entitled to 12 months of severance pay at his then effective monthly salary, plus the annual bonus and health benefits for the severance period. If there is a change in control (as defined) and Mr. Lupinetti's employment is terminated or his services are no longer needed, then he will receive 24 months of severance pay at this then effective monthly salary, plus each year's annual bonus and health benefits for the severance period.

Compensation of directors

During fiscal 2006, each non-employee director received a quarterly fee of \$5,750 for being a director, a quarterly fee of \$138 for each Board committee of which he is a member, and a fee of \$550, plus expenses, for each Board meeting he attended. In addition, the chairman of the Audit Committee received a quarterly fee of \$1,000 and the chairman of the Compensation Committee received a quarterly fee of \$500. On November 14, 2006, the fee for attending each Board meeting was increased to \$1,500, plus expenses.

Each non-employee director receives a grant of 200 unrestricted shares of our common stock annually as additional compensation. These shares cannot be sold for one year from the date of issuance. Each non-employee director also receives an annual non-discretionary grant of 2,500 stock options on the day after we release our first quarter earnings. These stock options have an exercise price per share equal to the fair market value of the common stock on the date of grant, have a term of three years and are fully vested and exercisable after six months. In fiscal 2006, we granted options to purchase an aggregate of 10,000 shares of our common stock to our non-employee directors, each with an exercise price of \$7.15 per share.

VOTING SECURITIES AND PRINCIPAL STOCKHOLDERS

Our only issued and outstanding class of voting securities is our common stock. Holders of common stock are entitled to one vote per share of such stock held by them of record at the close of business on March 12, 2007 upon each matter which may come before the Annual Meeting. At the close of business on March 12, 2007, there were 3,758,054 shares of common stock issued and outstanding.

Security Ownership of Certain Beneficial Owners and Management

The following table sets forth certain information as of March 12, 2007 regarding each person known by us to own beneficially more than 5% of our common stock, each director and nominee for director of the Company, each executive officer named in the Summary Compensation Table, and all directors and executive officers of the Company as a group.

Name	Shares Beneficially Owned (1)	Percent of Class (2)
Eliot Rose Asset Management, LLC and Gary S. Siperstein 10 Webosset Street, Suite 401 Providence, RI 02903	657,474(3)	15.8%
Daniel Zeff C/O Daniel Zeff Holding Co. 50 California Street, Suite 1500 San Francisco, CA 94111	324,703(4)	7.8%
Sterling Capital Management William G. and Janice Lauber 12300 Old Tesson Road, Suite 100C St. Louis, MO 63128	275,288(5)	6.6%
Julian DeMora P.O. Box 220139 Hollywood, FL 33022	222,514(6)	5.4%
Alexander R. Lupinetti	300,901(7)	7.2%
Christopher J. Hall (*)	378,450(8)	9.1%
C. Shelton James	11,600(9)	**
J. David Lyons (*)	10,343(10)	**
Robert M. Williams	10,100(11)	**
Gary W. Levine	32,172(12)	**
William Bent	17,973(13)	**
All directors and executive officers as a group (7 persons)	761,539(14)	18.3%

* Nominee for Director

** Owns less than one percent

(1) Except as otherwise noted, all persons and entities have sole voting and investment power over their shares. All amounts shown in this column include shares obtainable upon exercise of stock options exercisable within 60 days of the date of this proxy statement.

(2) Computed pursuant to Rule 13d-3 under the Exchange Act.

(3) Eliot Rose Asset Management, LLC and Gary S. Siperstein have filed a joint report on Schedule 13D dated January 12, 2006 in which Eliot Rose acts pursuant to a special arrangement as investment advisor to certain persons with respect to 657,474 shares of our common stock and has the right to receive, or the power to direct receipt of dividends from, or the power to direct receipt of proceeds from the sale

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of, the common stock purchased or held pursuant to such arrangement. Gary S. Siperstein is deemed to be the beneficial owner of the number of securities reflected in the table.

- (4) Daniel Zeff filed a 13G on February 13, 2007 in which it states that Daniel Zeff indirectly owns 324,703 shares in his capacity as the sole manager and member of Zeff Holding Co., LLP, which serves as the general partner of Zeff Capital Partner I, LP.
- (5) Sterling Capital Management Inc., William G. and Janice Lauber filed a joint report on Schedule 13G dated February 13, 2007 for 275,288 shares, in which it states that Sterling, as a registered investment advisor, owns 233,578 shares and has beneficial interest and discretion over and shared power to dispose of such shares. William G. Lauber, President of Sterling, owns 32,710 shares as an individual, and William G. and Janice Lauber jointly own 9,000 shares.
- (6) Mr. Julian Demora has furnished the Company with a report dated May 18, 2005, in which it states that Mr. Demora has direct ownership with respect to 222,514 shares of the Company's common stock.
- (7) Represents 35,401 shares owned by Mr. Lupinetti as an individual and 265,500 shares obtainable upon exercise of stock options.
- (8) Includes 373,950 shares that Mr. Hall has sole voting and investment power with respect to. There are 22,200 shares owned by The Hemisphere Trust, a Belize company owned by Mr. Hall and 351,750 shares are owned by Mr. Hall as an individual. Mr. Hall has 4,500 shares obtainable upon exercise of stock options.
- (9) Includes 7,100 shares owned by Mr. James and 4,500 shares obtained upon exercise of stock options.
- (10) Includes 5,843 shares owned by Mr. Lyons and 4,500 shares obtainable upon exercise of stock options.
- (11) Includes 5,600 shares owned by Mr. Williams and 4,500 shares obtainable upon exercise of stock options.
- (12) Includes 25,050 shares obtainable upon exercise of stock options.
- (13) Includes 15,670 shares obtainable upon exercise of stock options.
- (14) Includes 342,521 shares obtainable upon exercise of stock options.

CORPORATE GOVERNANCE

We believe that good corporate governance and fair and ethical business practices are crucial not only to the proper operation of our company, but also to building and maintaining confidence in the integrity, reliability and transparency of the securities markets. We have kept abreast of the actions taken in the past few years by Congress, the SEC and NASDAQ to improve and enhance corporate governance, and we take our responsibilities in this area very seriously. This section explains some of the things we have done, or are considering, to improve the way we can run CSPI.

Code of ethics

Pursuant to Section 406 of the Sarbanes-Oxley Act of 2002 and NASDAQ rules, we have adopted a code of ethics that applies to all our executive officers, directors and employees, which is available on our website at www.cspi.com under the investor relations section. A copy of the code of ethics can also be obtained, without charge, by written request to Investor Relations, CSP Inc., 43 Manning Road, Billerica, Massachusetts 01821.

Board, committee and stockholder meetings

Our Board met four times during the fiscal year ended September 30, 2006. In addition, the Audit Committee met eight times, and each of the Compensation Committee and the Nominating Committee met once. During fiscal 2006, each director attended at least 75% of the meetings of the Board and of the committees of which he was a member.

It is our policy that all members of the Board attend the annual meeting of stockholders in person, although we recognize that our directors occasionally may be unable to attend for personal or professional reasons. We generally hold a meeting of the Board on the same date as the annual meeting of stockholders. In 2006, all directors attended the annual meeting.

Independence

Board of Directors: Rules and regulations of the SEC and NASDAQ require that a majority of our Board be independent. The Board has reviewed those rules and regulations and has determined that Messrs. Lyons, Hall, James and Williams are independent directors. As required by NASDAQ rules, the independent directors convene regularly scheduled meetings at which only independent directors are present.

Compensation Committee: Our Compensation Committee is composed of Messrs. Lyons (chairman), James and Hall, each of whom is independent. This committee is charged with reviewing and approving executive officers' compensation and administering our stock option plans. NASDAQ rules require that the compensation of the chief executive officer be determined, or recommended to the Board for its determination, by either a majority of independent directors or a wholly-independent Compensation Committee. NASDAQ rules prohibit a company's CEO from being present during voting or deliberations with respect to his compensation. Compensation of all other executive officers is required to be determined in the same manner, except that the CEO is permitted to be present. Our Compensation Committee adopted a written charter, a current copy of which is available in the investor relations section (under corporate governance) of our web site at www.cspi.com.

Audit Committee: Our Audit Committee consists of Messrs. James (chairman), Hall and Williams. Each of the members of the Audit Committee is independent as defined under the rules and regulations of the SEC and NASDAQ. The Board determined that the members of our Audit Committee are not only independent, but also are financially literate for purposes of NASDAQ rules (that is, able to read and understand financial statements). In addition, the Board has found that Mr. James qualifies as an audit committee financial expert. Mr. James was a CPA and worked in public accounting from 1962 to 1965. He was chief financial officer of Systems & Engineering Laboratories in Ft. Lauderdale, Florida from 1969 to 1980, has served on numerous audit committees and currently serves on the audit committees of Concurrent Computers and DRS Technologies.

Our Audit Committee is responsible for overseeing our accounting and financial reporting processes and the audits of our financial statements. The committee acts in an oversight capacity and relies on the work and assurances of both management, which has primary responsibilities for our financial statements, and our independent auditors, who are responsible for expressing an opinion on the conformity of our audited financial statements to generally accepted accounting principles. The Audit Committee adopted a written charter, which was amended during fiscal 2003 in response to new regulatory requirement