Hallwood Group Inc
Form PRER14A
March 05, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of the

Securities Exchange Act of 1934

(Amendment No. 2)

Filed by the Registrant x Filed by a Party other than the Registrant ¨

Check the appropriate box:

x 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 under Rule 14a-12

The Hallwood Group Incorporated

(Name of the Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

¨ No fee required.

x 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:

   Common stock, par value $0.10 per share
2. Aggregate number of securities to which transaction applies:

   523,591 shares of common stock

Per unit price or other underlying value of transaction computed pursuant to Exchange Act

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):

   In accordance with Exchange Act Rule 0-11(c), the filing fee of $876.69 was determined by multiplying 0.0001288 by the maximum aggregate Merger Consideration of $6,806,683. The maximum aggregate Merger Consideration was calculated as the product of (a) 523,591 outstanding shares of common stock as of March 3, 2014 to be acquired in the merger and (b) the maximum per share Merger Consideration of $13.00.
4. Proposed maximum aggregate value of transaction: $6,806,683

5. Total fee paid: $876.69 ($202.30 paid herewith)

¨ Fee paid previously with preliminary materials.

x 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: $674.39

2. Form, Schedule or Registration Statement No.: Preliminary Proxy Statement on Schedule 14A, File No. 001-08303

3. Filing Party: The Hallwood Group Incorporated

4. Date Filed: November 14, 2013

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PRELIMINARY COPY SUBJECT TO COMPLETION

NOTICE OF SPECIAL MEETING

OF

STOCKHOLDERS

THE HALLWOOD GROUP INCORPORATED

3710 Rawlins, Suite 1500

Dallas, Texas 75219

Telephone: (214) 528-5588

[ ], 2014

To the Stockholders of The Hallwood Group Incorporated:

You are cordially invited to attend a special meeting of the stockholders of The Hallwood Group Incorporated, a Delaware corporation (the Company, we or us), which we will hold at 3710 Rawlins, Suite 1500, Dallas, Texas 75219 on April , 2014, at [ ], Central Time.

At the special meeting, holders of our common stock, par value $0.10 per share (Common Stock), will be asked to consider and vote on a proposal to adopt the Agreement and Plan of Merger, dated as of June 4, 2013, by and among the Company, Hallwood Financial Limited, a corporation organized under the laws of the British Virgin Islands (Parent), and HFL Merger Corporation, a Delaware corporation and wholly owned subsidiary of Parent (Merger Sub), as amended by that certain Amendment to Agreement and Plan of Merger, dated as of July 11, 2013, and as further amended by that certain Second Amendment to Agreement and Plan of Merger, dated as of February 7, 2014 (as it may be further amended from time to time, the Merger Agreement), a copy of which is attached as Annex A to the accompanying proxy statement. Parent is controlled by Anthony J. Gumbiner, Chairman and Chief Executive Officer of the Company, and members of his family, and Parent currently owns 1,001,575 shares, or 65.7%, of the issued and outstanding shares of Common Stock.

Pursuant to the Merger Agreement, Merger Sub will merge with and into the Company, with the Company continuing as the surviving corporation and a wholly owned subsidiary of Parent (the Merger), and each share of Common Stock outstanding immediately prior to the effective time of the Merger (other than certain excluded and dissenting shares of Common Stock) will be cancelled and converted into the right to receive $13.00 in cash, without interest, less a proportionate deduction for any incentive fee and attorney s fees (the Merger Consideration) that may be awarded by the Delaware Court of Chancery (the Court) in connection with the Stipulation of Settlement, filed on February 7, 2014, relating to the purported class and, in the alternative, derivative action filed by Gary L. Sample against the Company and other defendants, asserting, among other things, that the original Merger Consideration was unfair and did not reflect the true value of the Company and all of its assets (the Sample Litigation). The Sample Litigation is more fully described in the accompanying proxy statement under the section entitled *Special Factors Litigation.* The plaintiff and plaintiff s attorneys in the Sample Litigation intend to petition the Court for an award of an incentive fee of $15,000 to plaintiff and attorney s fees and expenses not exceeding $310,000, which if granted in its entirety is equivalent to approximately $0.62 per share. Therefore, the Company expects that if the settlement is approved, the

Merger Consideration will be at least $12.38 per share and may be more if the Court does not approve the full amount requested by the plaintiff and the plaintiff s counsel. The following excluded and dissenting shares of Common Stock will not be entitled to the Merger Consideration: (i) shares held by Parent, Merger Sub, the Company or any wholly owned subsidiary of the Company or held in the Company s treasury and (ii) shares outstanding immediately prior to the effective time of the Merger held by a stockholder who has neither voted in favor of the Merger nor consented thereto in writing and who has demanded properly in writing appraisal for such shares and otherwise properly perfected and not withdrawn or lost the right to an appraisal of such dissenting shares pursuant to Section 262 of the General Corporation Law of the State of Delaware. In the event that the Court does not approve the settlement, the parties to the Merger Agreement have agreed to proceed with the consummation of the Merger based on the Original Merger Consideration of $10.00 per share, without the $3.00 per share increase to the Merger Consideration contemplated by the Second Amendment, which would involve the solicitation of stockholder approval at such $10.00 price per share.

The board of directors of the Company (the Board) formed a special committee (the Special Committee), consisting of three independent directors of the Company, to evaluate the Merger and other alternatives available to the Company. The Special Committee unanimously determined that the transactions contemplated by the Merger Agreement, including the Merger, are advisable and in the best interests of the Company and its stockholders (other than the persons and entities associated with Mr. Gumbiner), and unanimously recommended that the Board approve and declare advisable the Merger Agreement and the transactions contemplated thereby, including the Merger, and that the Company s stockholders vote for the adoption of the Merger Agreement. Based in part on that recommendation, the Board (other than Mr. Gumbiner, who did not participate due to his interest in the Merger) unanimously (i) determined that the transactions contemplated by the Merger Agreement, including the Merger, are advisable and in the best interests of the Company and its stockholders (other than the persons and entities

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associated with Mr. Gumbiner), (ii) approved and declared advisable the execution, delivery and performance of the Merger Agreement and the consummation of the transactions contemplated thereby, including the Merger and (iii) resolved to recommend that the Company s stockholders vote for the adoption of the Merger Agreement. **Accordingly, the Board (without Mr. Gumbiner s participation) unanimously recommends that the stockholders of the Company vote FOR the proposal to adopt the Merger Agreement.**

As of June 4, 2013 and March 3, 2014, Hallwood Trust and Mr. Gumbiner beneficially owned through Parent, in the aggregate, 1,001,575 shares of Common Stock, or approximately 65.7% of the total number of outstanding shares of Common Stock.

We urge you to read the accompanying proxy statement in its entirety, including annexes and the documents referred to in, or incorporated by reference into, the proxy statement, because it describes the Merger Agreement and the Merger and provides specific information concerning the special meeting and other important information related to the Merger. In addition, you may obtain information about us from documents filed with the U.S. Securities and Exchange Commission (SEC).

Your vote is very important, regardless of the number of shares of Common Stock you own. The closing of the Merger is subject to a non-waivable condition that the Merger Agreement be adopted by (i) the affirmative vote of the holders of a majority of the outstanding shares of Common Stock entitled to vote on the adoption of the Merger Agreement, voting together as a single class, and (ii) the affirmative vote of the holders of a majority of the outstanding shares of Common Stock, voting together as a single class, excluding all shares of Common Stock owned by Parent, Merger Sub, Mr. Gumbiner or any of their respective affiliates (other than the Company and its subsidiaries), or by any director, officer or other employee of the Company or any of its subsidiaries.

While stockholders may exercise their right to vote their shares in person, we recognize that many stockholders may not be able to, or do not desire to, attend the special meeting. Accordingly, we have enclosed a proxy that will enable your shares to be voted on the matters to be considered at the special meeting even if you are unable or do not desire to attend. If you desire your shares to be voted in accordance with the Board s recommendation, you need only sign, date and return the proxy in the enclosed postage-paid envelope. Otherwise, please mark the proxy to indicate your voting instructions; date and sign the proxy; and return it in the enclosed postage-paid envelope. You also may submit a proxy by using a toll-free telephone number or the Internet. We have provided instructions on the proxy card for using these convenient services.

Submitting a proxy will not prevent you from voting your shares in person if you subsequently choose to attend the special meeting. Even if you plan to attend the special meeting in person, we request that you complete, sign, date and return the enclosed proxy and thus ensure that your shares will be represented at the special meeting if you are unable to attend.

Sincerely,

Charles A. Crocco, Jr.

Chairman of the Special Committee and Audit Committee

Neither the SEC nor any state securities regulatory agency has approved or disapproved the Merger, passed upon the merits or fairness of the Merger or passed upon the adequacy or accuracy of the disclosure in the accompanying proxy statement. Any representation to the contrary is a criminal offense.

This proxy statement is dated [ ], 2014 and is first being mailed to stockholders on or about [ ], 2014.

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THE HALLWOOD GROUP INCORPORATED

3710 Rawlins, Suite 1500

Dallas, Texas 75219

Telephone: (214) 528-5588

NOTICE OF SPECIAL MEETING OF STOCKHOLDERS

To the Stockholders of The Hallwood Group Incorporated:

NOTICE IS HEREBY GIVEN that a special meeting of the stockholders of The Hallwood Group Incorporated, a Delaware corporation (the Company, we or us), will be held at 3710 Rawlins, Suite 1500, Dallas, Texas 75219 on April , 2014, at [ ], Central Time, for the following purposes:

to consider and vote on a proposal to adopt the Agreement and Plan of Merger, dated as of June 4, 2013, by and among the Company, Hallwood Financial Limited, a corporation organized under the laws of the British Virgin Islands (Parent), and HFL Merger Corporation, a Delaware corporation and wholly owned subsidiary of Parent (Merger Sub), as amended by that certain Amendment to Agreement and Plan of Merger, dated as of July 11, 2013, as further amended by that certain Second Amendment to Agreement and Plan of Merger, dated as of February 7, 2014 (as it may be further amended from time to time, the Merger Agreement);

to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement; and

to act upon other business as may properly come before the special meeting or any adjournment or postponement thereof by or at the direction of the Board.

The holders of record of our common stock, par value $0.10 per share (Common Stock), at the close of business on March , 2014, are entitled to notice of and to vote at the special meeting or at any adjournment or postponement thereof. All stockholders of record are cordially invited to attend the special meeting in person.

Your vote is important, regardless of the number of shares of Common Stock you own. The closing of the Merger is subject to a non-waivable condition that the Merger Agreement be adopted by (i) the affirmative vote of the holders of a majority of the outstanding shares of Common Stock entitled to vote on the adoption of the Merger Agreement, voting together as a single class, and (ii) the affirmative vote of the holders of a majority of the outstanding shares of Common Stock, voting together as a single class, excluding all shares of Common Stock owned by Parent, Merger Sub, Mr. Gumbiner or any of their respective affiliates (other than the Company and its subsidiaries), or by any director, officer or other employee of the Company or any of its subsidiaries. Even if you plan to attend the special meeting in person, we request that you complete, sign, date and return the enclosed proxy and thus ensure that your shares will be represented at the special meeting if you are unable to attend. You also may submit your proxy by using a toll-free telephone number or the Internet. We have provided instructions on the proxy

card for using these convenient services.

If you sign, date, and return your proxy card without indicating how you wish to vote, your proxy will be voted in favor of the proposal to adopt the Merger Agreement and in favor of the proposal to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies. If you fail to vote or submit your proxy, the effect will be that your shares will not be counted for purposes of determining whether a quorum is present at the special meeting and will have the same effect as a vote against the proposal to adopt the Merger Agreement. Your proxy may be revoked at any time before the vote at the special meeting by following the procedures outlined in the accompanying proxy statement. If you are a stockholder of record, attend the special meeting and wish to vote in person, you may revoke your proxy and vote in person.

BY ORDER OF THE BOARD OF DIRECTORS

Richard Kelley

Corporate Secretary

Dated [ ], 2014

Dallas, Texas

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SUMMARY TERM SHEET

This summary term sheet discusses material information contained in this proxy statement, including with respect to the Merger Agreement (as defined below) and the Merger (as defined below). We encourage you to read carefully this entire proxy statement, including its annexes and the documents referred to in, or incorporated by reference into, this proxy statement, as this summary term sheet may not contain all of the information that may be important to you. The items in this summary term sheet include page references directing you to a more complete description of the applicable topic in this proxy statement.

The Parties to the Merger (page 52)

The Hallwood Group Incorporated

The Hallwood Group Incorporated (the Company, we us) is a Delaware corporation. Founded in September 1981, the Company operates its principal business in the textile products industry through its wholly owned subsidiary, Brookwood Companies Incorporated (Brookwood). Brookwood is an integrated textile firm that develops and produces innovative fabrics and related products through specialized finishing, treating and coating processes. For more information, see the sections entitled *Important Information Regarding the Company* beginning on page 68 and *The Parties to the Merger The Company* on page 52.

Additional information about the Company is contained in its public filings, which are incorporated by reference into this proxy statement. See the section entitled *Where You Can Find Additional Information* on page 83.

Parent and Merger Sub

Hallwood Financial Limited (Parent) is a corporation organized under the laws of the British Virgin Islands. HFL Merger Corporation (Merger Sub) is a Delaware corporation and wholly owned subsidiary of Parent. Parent is controlled by Anthony J. Gumbiner, Chairman and Chief Executive Officer of the Company, and members of his family, and Parent currently owns 1,001,575 shares, or 65.7%, of the issued and outstanding shares of common stock, par value $0.10 per share, of the Company (Common Stock). Merger Sub was formed solely for the purpose of engaging in the Merger (as defined below) and other related transactions. Merger Sub has not engaged in any business other than in connection with the Merger (as defined below) and other related transactions. For more information, see the section entitled *The Parties to the Merger Parent and Merger Sub* on page 52.

The Purpose of the Special Meeting (page 53)

You will be asked to consider and vote on the proposal to adopt the Agreement and Plan of Merger, dated as of June 4, 2013, by and among Parent, Merger Sub and the Company, as amended by that certain Amendment to Agreement and Plan of Merger, dated as July 11, 2013, as further amended by that certain Second Amendment to Agreement and Plan of Merger, dated as of February 7, 2014 (as it may be further amended from time to time, the Merger Agreement). The Merger Agreement provides that Merger Sub will be merged with and into the Company (the Merger), at the effective time of the Merger (the Effective Time), whereupon the separate corporate existence of Merger Sub will cease, and the Company will continue as the surviving company in the Merger (the Surviving Corporation) and a wholly owned subsidiary of Parent. At the Effective Time, each share of Common Stock outstanding immediately prior to the Effective Time (other than shares held by Parent, Merger Sub, the Company or any wholly owned subsidiary of the Company or held in the Company s treasury (such shares, Excluded Shares) and shares outstanding immediately prior to the Effective Time held by any stockholder who has neither voted in favor of the Merger nor consented thereto in writing and who has demanded properly in writing appraisal for such shares or

otherwise properly perfected and not withdrawn or lost his or her rights of appraisal under the General Corporation Law of the State of Delaware (the DGCL) (such shares, Dissenting Shares) will be converted into the right to receive $13.00 in cash, without interest, less a proportionate deduction for any incentive fee and attorney s fees (the Merger Consideration) that may be awarded by the Court in connection with the Stipulation of Settlement, filed on February 7, 2014, relating to the purported class and, in the alternative, derivative action filed by Gary L. Sample against the Company and other defendants, asserting, among other things, that the original Merger Consideration was unfair and did not reflect the true value of the Company and all of its assets (the Sample Litigation), whereupon all such shares will be automatically cancelled upon the conversion thereof and will cease to exist, and the holders of such shares will cease to have any rights with respect thereto other than the right to receive the Merger Consideration. Excluded Shares will not be entitled to receive the Merger Consideration. The plaintiff and the plaintiff s attorneys in the Sample Litigation intend to petition the Court for a $15,000 incentive fee and attorney s fees and expenses not exceeding $310,000 which, if granted in its entirety, is equivalent to approximately $0.62 per share. Therefore, the Company expects that if the settlement is approved, the Merger Consideration will be at least $12.38 per share and may be more if the Court does not approve the full amount requested by the plaintiff and the plaintiff s attorneys. In the event that the Court does

not approve the settlement, the parties to the Merger Agreement have agreed to proceed with the consummation of the Merger based on the Original Merger Consideration of $10.00 per share, without the $3.00 per share increase to the Merger Consideration contemplated by the Second Amendment, which would involve the solicitation of stockholder approval at such $10.00 price per share. The Sample Litigation is more fully described under the section entitled *Special Factors Litigation.* Parent will be entitled to deduct and withhold from the Merger Consideration otherwise payable any amounts that are required to be withheld or deducted under the Internal Revenue Code of 1986, as amended (the Code), or any provision of U.S., state, local or foreign tax laws. To the extent that amounts are withheld or deducted, those withheld or deducted amounts will be treated for all purposes as having been paid to the holder of the shares of Common Stock in respect of which such deduction and withholding were made.

Deregistration of the Company s Common Stock (page 37)

Following, and as a consequence of, the Merger, the Company will become a privately held company and a wholly owned subsidiary of Parent. Shares of our Common Stock will no longer be listed and publicly traded and will be deregistered under the Securities Exchange Act of 1934, as amended (the Exchange Act),

Market Price of the Company s Common Stock (page 37)

Shares of Common Stock are traded on the NYSE MKT under the ticker symbol HWG . The closing price of our Common Stock on the NYSE MKT on June 4, 2013, the last trading day prior to our public announcement of the Merger Agreement on June 5, 2013, was $8.05 per share. On February 7, 2014, the last trading day prior to our public announcement of the Second Amendment to Agreement and Plan of Merger, dated as of February 7, 2014, by and among Parent, Merger Sub and the Company (the Second Amendment) and the increase in Merger Consideration, the closing price of our Common Stock was $9.73. On March 3, 2014, the closing price of our Common Stock on the NYSE MKT was $12.35 per share. The Company has not paid any cash dividends on its Common Stock since 2008. You are encouraged to obtain current market quotations for our Common Stock.

The Special Meeting (page 53)

The special meeting of stockholders will be held at 3710 Rawlins, Suite 1500, Dallas, Texas 75219, on April , 2014 at [ ], Central Time.

Record Date and Quorum

The holders of record of Common Stock as of the close of business on March , 2014, the record date for determination of stockholders entitled to notice of and to vote at the special meeting (the Record Date), are entitled to receive notice of and to vote at the special meeting.

The presence at the special meeting, in person or by proxy, of the holders of a majority of the shares of Common Stock entitled to vote on the Record Date will constitute a quorum, permitting the Company to conduct its business at the special meeting. Given Parent s ownership of 65.7% of the issued and outstanding shares of Common Stock, Parent s attendance at the special meeting will, by itself, constitute a quorum.

The Proposals

At the special meeting, you will be asked to (i) consider and vote on a proposal to adopt the Merger Agreement, (ii) approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement and

(iii) act upon other business as may properly come before the special meeting or any adjournment or postponement thereof by or at the direction of the Board.

Required Vote

For the Company to consummate the Merger, under the DGCL, stockholders holding at least a majority of the shares of Common Stock outstanding and entitled to vote at the close of business on the Record Date must vote **FOR** the proposal to adopt the Merger Agreement. In addition, the Merger Agreement provides that the closing of the Merger (the Closing) is subject to a non-waivable condition that the Merger Agreement be adopted by (i) the affirmative vote of the holders of a majority of the outstanding shares of Common Stock entitled to vote on the adoption of the Merger Agreement, voting together as a single class, and (ii) the affirmative vote of the holders of a majority of the outstanding shares of Common Stock, voting together as a single class, excluding all shares of Common Stock owned by Parent, Merger Sub, Mr. Gumbiner or any of their respective affiliates

(other than the Company and its subsidiaries), or by any director, officer or other employee of the Company or any of its subsidiaries. See *The Special Meeting Required Vote* on page 54.

Voting; Proxies; Revocation (page 54)

Attendance

All holders of shares of Common Stock as of the close of business on the Record Date including stockholders of record and beneficial owners of Common Stock registered in the street name of a bank, broker or other nominee, are invited to attend the special meeting. If you wish to attend the special meeting and are a stockholder of record, please be prepared to provide proper identification, such as a driver s license. If you hold your shares in street name, you will need to provide proof of ownership, such as a recent account statement or letter from your bank, broker or other nominee, along with proper identification.

Voting in Person

Stockholders of record will be able to vote in person at the special meeting. If you are not a stockholder of record, but instead hold your shares in street name through a bank, broker or other nominee, you must provide a proxy executed in your favor from your bank, broker or other nominee in order to be able to vote in person at the special meeting.

Providing Voting Instructions by Proxy

To ensure that your shares are represented at the special meeting, we recommend that you provide voting instructions promptly by proxy, even if you plan to attend the special meeting in person.

If you are a stockholder of record, you may provide voting instructions by proxy by completing, signing, dating and returning the enclosed proxy card. You may alternatively follow the instructions on the enclosed proxy card for Internet or telephone submissions.

For more information, see the section entitled *The Special Meeting Voting; Proxies; Revocation* beginning on page 54.

Revocation of Proxies (page 55)

Your proxy is revocable. If you are a stockholder of record, you may revoke your proxy at any time before the vote is taken at the special meeting by:

- submitting a new proxy with a later date, by using the telephone or Internet proxy submission procedures described in the proxy card, or by completing, signing, dating and returning a new proxy card by mail to the Company;

- attending the special meeting and voting in person; or

sending written notice of revocation to the Corporate Secretary of the Company at The Hallwood Group Incorporated, Attn: Corporate Secretary, 3710 Rawlins, Suite 1500, Dallas, Texas 75219.

Attending the special meeting in person without taking one of the actions described above will not in itself revoke a previously submitted proxy. Please note that if you want to revoke your proxy by mailing a new proxy card to the Company or by sending a written notice of revocation to the Company, you should ensure that you send your new proxy card or written notice of revocation in sufficient time for it to be received by the Company before the day of the special meeting.

If you hold your shares in street name through a bank, broker or other nominee, you will need to follow the instructions provided to you by your bank, broker or other nominee in order to revoke your proxy or submit new voting instructions.

Abstentions (page 56)

Abstentions will be included in the calculation of the number of shares of Common Stock represented at the special meeting for purposes of determining whether a quorum has been achieved. Abstaining from voting will have the same effect as a vote **AGAINST** the proposal to adopt the Merger Agreement and **AGAINST** the proposal to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement.

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Appraisal Rights (pages 56, 77, and Annex C)

Pursuant to Section 262 of the DGCL (Section 262), stockholders who do not vote in favor of the Merger and who comply with the applicable requirements of Section 262 and do not withdraw or otherwise lose the rights to an appraisal are entitled to statutory appraisal rights under Delaware law in connection with the Merger. This means that if you comply precisely with the requirements of Section 262, you are entitled to seek appraisal of the fair value of your shares of Common Stock determined by the Court of Chancery of the State of Delaware and to receive payment based on that valuation instead of receiving the Merger Consideration. If you validly exercise (and do not withdraw or lose) appraisal rights, the ultimate amount you may be entitled receive in an appraisal proceeding may be more than, the same as or less than the amount you would have received under the Merger Agreement. To exercise your appraisal rights, (i) you must submit a written demand for appraisal to us before the vote is taken on the Merger Agreement, (ii) you must NOT vote in favor of the proposal to adopt the Merger Agreement and (iii) you must otherwise comply with the requirements of Section 262. Your failure to follow precisely the procedures specified under Delaware law could result in the loss of your appraisal rights. See the section entitled *Rights of Appraisal* beginning on page 77 and the text of the Delaware appraisal rights statute, Section 262, which is reproduced in its entirety as Annex C to this proxy statement. Assuming you have otherwise complied with the requirements of Section 262, your right to seek appraisal under Section 262 is not released under the Settlement, but if the Settlement is approved, you may not claim value related to or arising from the derivative claims that are released, settled, and dismissed with prejudice pursuant to the Settlement.

Adjournments and Postponements (page 56)

Although it is not currently expected, the special meeting may be adjourned or postponed for the purpose of soliciting additional proxies. In the event that there is present, in person or by proxy, sufficient favorable voting power to secure the vote of the stockholders of the Company necessary to approve the proposal to adopt the Merger Agreement, the Company does not anticipate that it will adjourn or postpone the special meeting unless it is advised by counsel that such adjournment or postponement is necessary under applicable law to allow additional time for any disclosure. Any signed proxies received by the Company in which no voting instructions are provided on such matter will be voted in favor of an adjournment in these circumstances. The time and place of the adjourned meeting will be announced at the time the adjournment is taken, and no other notice need be given, unless the adjournment is for more than 30 days. Any adjournment or postponement of the special meeting for the purpose of soliciting additional proxies will allow the Company s stockholders who have already sent in their proxies to revoke them at any time prior to their use at the special meeting as adjourned or postponed.

Structure of the Merger (page 58)

Upon and subject to the terms of the Merger Agreement and in accordance with DGCL, at the Effective Time, Merger Sub will merge with and into the Company, whereupon the separate corporate existence of Merger Sub will cease, and the Company will continue as the Surviving Corporation in the Merger and a wholly owned subsidiary of Parent.

Merger Consideration (page 44)

As a consequence of the Merger, each share of Common Stock issued and outstanding immediately prior to the Effective Time (other than Excluded Shares and any Dissenting Shares) will be converted automatically into and will thereafter represent the right to receive the Merger Consideration. All Shares (other than Excluded Shares and any Dissenting Shares) will, upon conversion, cease to be outstanding and will automatically be cancelled and will cease to exist, and each holder of (i) a certificate that immediately prior to the Effective Time represented such shares or (ii) uncertificated shares represented by book-entry that immediately prior to the Effective Time represented such

shares will cease to have any rights with respect thereto, except the right to receive the Merger Consideration, without interest, upon surrender of such certificate or book-entry shares in accordance with the Merger Agreement.

Payment Procedures and Exchange of Certificates (page 59)

At or prior to the Effective Time, Parent will deposit, or will cause to be deposited, with a U.S. bank or trust company that will be appointed by Parent (that is reasonably acceptable to the Company) to act as paying agent under the Merger Agreement (the Paying Agent), in trust for the benefit of the holders of our Common Stock, sufficient cash to pay to the holders of our Common Stock (other than the holders of the Excluded Shares and Dissenting Shares) the Merger Consideration. In the event any Dissenting Shares cease to be Dissenting Shares, Parent will deposit, or will cause to be deposited, with the Paying Agent sufficient cash to pay to the holders of such Common Stock the Merger Consideration of $13.00 per share, without interest, less a proportionate deduction for any incentive fee and attorney s fees that may be awarded by the Court in connection with the Stipulation of Settlement, filed on February 7, 2014, relating to the Sample Litigation. The plaintiff and plaintiff s attorneys in

the Sample Litigation intend to petition the Court for a $15,000 incentive fee and attorney s fees and expenses not exceeding $310,000, which, if granted in their entirety, is equivalent to approximately $0.62 per share. Therefore, the Company expects that if the Settlement is approved, the Merger Consideration will be at least $12.38 per share and may be more if the Court does not approve the full amount requested by the plaintiff and the plaintiff s counsel. In the event that the Court does not approve the Settlement, the parties to the Merger Agreement have agreed to proceed with the consummation of the Merger based on the Original Merger Consideration of $10.00 per share, without the $3.00 per share increase to the Merger Consideration contemplated by the Second Amendment, which would involve the solicitation of stockholder approval at such $10.00 price per share. The Sample Litigation is more fully described under the section entitled *Special Factors Litigation.*

As soon as reasonably practicable after the Effective Time and in any event no later than the fifth business day following the Effective Time, the Paying Agent will mail to each record holder of shares of Common Stock that were converted into the Merger Consideration a letter of transmittal and instructions for use in effecting the surrender of certificates that formerly represented shares of the Common Stock or non-certificated shares represented by book-entry in exchange for the Merger Consideration. For more information regarding the exchange of certificates, see the section entitled *The Merger Agreement Payment Procedures and Exchange of Certificates* beginning on page 59.

Conditions to the Merger (page 64)

The obligations of each of the Company, Parent and Merger Sub to consummate the Merger are subject to several conditions. For a more detailed discussion of these conditions, see the section entitled *The Merger Agreement Conditions to the Merger* beginning on page 61.

When the Merger Becomes Effective (page 58)

The Merger will become effective when the Company files a certificate of merger with the Secretary of State of the State of Delaware or at such later date or time as Parent and the Company may agree in writing and specify in the certificate of merger in accordance with the DGCL.

The Closing will take place on a date which will be no later than the fifth business day after the satisfaction or waiver (to the extent permitted by applicable law) of the closing conditions stated in the Merger Agreement (other than those conditions that by their nature are to be satisfied at the Closing, but subject to the satisfaction or waiver of such conditions) or at such other time and date as the Company and Parent may agree in writing.

The Company currently expects the Closing to occur soon after the special meeting. The Company, however, can provide no assurance that the Closing will occur by any particular date, if at all. Because the Closing is subject to a number of conditions, the exact timing of the Closing cannot be determined at this time.

Reasons for the Merger; Fairness of the Merger; Recommendations of the Special Committee and the Board (page 23)

The Board, acting upon the unanimous recommendation of a special committee of the Board consisting of three independent directors of the Company (the Special Committee), determined that the Merger was substantively and procedurally fair to minority and unaffiliated stockholders, and was advisable and in the best interests of the Company and its minority and unaffiliated stockholders. The Board (without Mr. Gumbiner s participation) unanimously recommended that the stockholders of the Company vote **FOR** the proposal to adopt the Merger Agreement. For a description of the reasons considered by the Special Committee and the Board in deciding to recommend approval of

the proposal to adopt the Merger Agreement, see the section entitled *Special Factors Background of the Merger Reasons for the Merger; Fairness of the Merger; Recommendations of the Special Committee and the Board* beginning on page 23.

Opinion of Southwest Securities (page 27 and Annex B)

The Special Committee retained Southwest Securities, Inc. (Southwest Securities) to act as its independent financial advisor in connection with the proposed Merger. At the Special Committee meeting held on June 4, 2013, Southwest Securities rendered its oral opinion, and subsequently confirmed in writing, that as of June 4, 2013, and based upon and subject to the factors and assumptions set forth therein, the consideration to be paid to the holders of Common Stock (other than Excluded Shares and Dissenting Shares) in the proposed Merger was fair, from a financial point of view, to such stockholders.

The full text of the written opinion of Southwest Securities, dated June 4, 2013, is attached to this proxy statement as Annex B and is incorporated into this proxy statement by reference. The opinion sets forth, among other things, the assumptions made, procedures followed, matters considered and limits on the review undertaken by Southwest Securities in rendering its opinion.

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You are urged to read the opinion carefully and in its entirety. Southwest Securities written opinion that was provided to the Special Committee and the Board, is directed only to the fairness from a financial point of view of the Merger Consideration originally agreed to be paid in the proposed Merger and it does not constitute a recommendation to any stockholder of the Company as to how such stockholder should vote with respect to the Merger or any other matter, nor does Southwest Securities intend to update its opinion or further opine on any matters related hereto. For a further discussion of Southwest Securities opinion, see the section entitled *Special Factors Background of the Merger Opinion of Southwest Securities* beginning on page 27 and Annex B to this proxy statement.

Purposes and Reasons of the Company for the Merger (page 23)

The Company s purpose for engaging in the Merger is to enable its minority and unaffiliated stockholders to receive the Merger Consideration. The original Merger Consideration of $10.00 per share, without interest, represented a premium of approximately 78.3% above the closing price of our Common Stock on November 8, 2012, the last trading day prior to the Company s public announcement of the proposal received from Parent. If the Settlement is approved, the increased Merger Consideration of at least $12.38 per share (assuming the Court approves an incentive fee and attorney s fees totaling $325,000, which is equivalent to $0.62 per share) represents a premium of at least 120% above the closing price of our Common Stock on November 8, 2012. For more information on the Company s purposes and reasons for engaging in the Merger, see the section entitled *Special Factors Background of the Merger Reasons for the Merger; Fairness of the Merger; Recommendations of the Special Committee and the Board* beginning on page 23.

Certain Effects of the Merger (page 38)

If the conditions to the Closing are either satisfied or, to the extent permitted, waived, Merger Sub will be merged with and into the Company with the Company surviving the Merger as a wholly owned subsidiary of Parent. Upon the Closing, shares of Common Stock (other than Excluded Shares and Dissenting Shares) will be converted into the right to receive the Merger Consideration, all such shares will be automatically cancelled upon the conversion thereof and will cease to exist, and the holders of such shares will cease to have any rights with respect thereto other than the right to receive the Merger Consideration. Following the Closing, Common Stock will no longer be publicly traded, and current stockholders (other than Parent and its affiliates) will cease to have any ownership interest in the Company. For more information, see the section entitled *Special Factors Certain Effects of the Merger* beginning on page 38.

Interests of the Company s Directors and Executive Officers in the Merger (page 43)

As of June 4, 2013, Hallwood Trust and Mr. Gumbiner, a director and the chief executive officer of the Company, beneficially owned through Parent 1,001,575 shares of Common Stock, in the aggregate, or approximately 65.7% of the total number of outstanding shares of Common Stock. Common Stock beneficially owned by Hallwood Trust and Mr. Gumbiner will be cancelled in the Merger without consideration, and the outstanding shares of Merger Sub will be converted into, and constitute the only outstanding shares, of the Surviving Corporation, with the result that Parent will be the sole stockholder of the Surviving Corporation after the Effective Time, as discussed in the section entitled *Special Factors Interests of the Company s Directors and Executive Officers in the Merger* beginning on page 43. Mr. Charles A. Crocco, Jr., a director of the Company and Chairman of the Special Committee, owned 9,996 shares of Common Stock, or approximately 0.7% of the total number of outstanding shares of Common Stock, as of March 3, 2014. The Special Committee and the Board were aware of the different or additional interests set forth herein and considered such interests along with other matters in approving the Merger Agreement and the transactions contemplated thereby, including the Merger, and recommending that the Company s stockholders vote to adopt the Merger Agreement.

Financing the Merger (page 43)

Parent will satisfy the funding required for the Merger from the working capital and personal funds of Parent and its affiliates. For more information, see the section entitled *Special Factors Financing the Merger* beginning on page 43.

Material U. S. Federal Income Tax Consequences of the Merger (page 44)

If you are a U.S. holder, the receipt of cash in exchange for shares of Common Stock pursuant to the Merger will generally be a taxable transaction for U.S. federal income tax purposes. You should consult your own tax advisors regarding the particular tax consequences to you of the exchange of shares of Common Stock for cash pursuant to the Merger in light of your particular circumstances (including the application and effect of any state, local or foreign income and other tax laws). For more information, see the section entitled *Special Factors Material U.S. Federal Income Tax Consequences of the Merger* beginning on page 44.

Regulatory Approvals (page 47)

The Company does not believe that the filing of notification and report forms under the Hart-Scott-Rodino Act will be necessary to complete the Merger. However, at any time before or after the Merger, the U.S. Department of Justice, the Federal Trade Commission, a state attorney general or a foreign competition authority could take such action under antitrust laws as it deems necessary or desirable in the public interest, including seeking to enjoin the Merger or seeking divestiture of substantial assets of the Company or Merger Sub or their respective subsidiaries. Private parties may also bring legal actions under the antitrust laws under certain circumstances. Notwithstanding the fact that no such filings are required, there can be no assurance that a challenge to the Merger on antitrust grounds will not be made or, if a challenge is made, of the result of such challenge.

Litigation (page 47)

On August 23, 2013, a complaint was filed in the Delaware Court of Chancery (the Court) captioned Sample v. Gumbiner et al., Civil Action No. 8833-VCN. The action named as defendants the directors of the Company, and also named as defendants Parent and Merger Sub. The Company is also named as a defendant, or in the alternative, as a nominal defendant. The plaintiff and defendants have entered into a Stipulation of Settlement (the Stipulation), filed with the Court on February 7, 2014, relating to the Sample Litigation. A hearing for final approval of the settlement set forth in the Stipulation (the Settlement) is set to be held on March 25, 2014. For a more information, see the section entitled *Special Factors Litigation* beginning on page 47.

No Solicitation (page 63)

Until the Effective Time, the Company, its subsidiaries and their respective representatives are subject to customary no shop restrictions on their ability to initiate, solicit, knowingly encourage (including by providing information) or knowingly facilitate any inquiries, proposals or offers with respect to, or the making or completion of, an Alternative Proposal (as defined below). However, if following the date of the Merger Agreement and prior to the Company obtaining the required stockholder approvals, (i) the Company receives an unsolicited written Alternative Proposal, (ii) the Company has not breached the no shop provision, (iii) the Board (acting through the Special Committee, if then in existence) determines, in good faith, after consultation with its outside counsel and financial advisors, that such Alternative Proposal constitutes or is reasonably likely to result in a Superior Proposal (as defined below) and (iv) after consultation with its outside counsel, the Board of Directors (acting through the Special Committee, if then in existence) determines in good faith that failure to take such action could reasonably be expected to be inconsistent with its fiduciary duties under applicable law, then the Company may (A) furnish information with respect to the Company and its subsidiaries to the person making such Alternative Proposal and its representatives pursuant to a customary confidentiality agreement with a standstill provision and (B) participate in discussions or negotiations with such person and its representatives regarding such Alternative Proposal. As used in the Merger Agreement, Alternative Proposal means any inquiry, proposal or offer from any person or group of persons other than Parent or one of its subsidiaries (1) for a merger, reorganization, consolidation, recapitalization or other business combination, liquidation, dissolution or similar transaction involving the Company or any of its subsidiaries, (2) for the issuance by the Company of over 20% of its equity securities as consideration for the assets or securities of another person or (3) to acquire in any manner, directly or indirectly, over 20% of the equity securities or consolidated total assets of the Company and its subsidiaries, in each case, other than the Merger.

As used in the Merger Agreement, Superior Proposal means a bona fide, unsolicited, written Alternative Proposal (except that references to 20% in the definition of such term will be deemed to be references to 50%) made in writing and not solicited in violation of the no shop provision that the Board (acting through the Special Committee, if then in existence) determines in good faith, after consultation with outside legal counsel and financial advisors, (i) is

reasonably likely to be consummated in accordance with its terms, taking into account all legal, financial and regulatory aspects of the proposal and the person making the proposal (including any conditions relating to financing, regulatory approvals or other events or circumstances beyond the control of the party invoking the condition), (ii) for which financing, if a cash transaction (whether in whole or in part), is then fully committed, and (iii) if consummated, would result in a transaction more favorable to the holders of Common Stock in their sole capacity as such (other than Parent and Merger Sub) from a financial point of view (including the effect of any termination fee or provision relating to the reimbursement of expenses) than the transaction contemplated by the Merger Agreement (after taking into account any revisions to the terms of the transaction contemplated by the no shop provision and the time likely to be required to consummate such Alternative Proposal).

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Additionally, neither the Board nor any committee thereof may withdraw or modify in a manner adverse to Parent or Merger Sub, or publicly propose to withdraw or modify in a manner adverse to Parent or Merger Sub or fail to publicly reaffirm as promptly as practicable (but in any event within five business days after written receipt of any written request to do so from Parent), its recommendation (a Recommendation Change). Notwithstanding the foregoing, with respect to (aa) an event, fact, circumstance, development or occurrence that affects the business, assets or operations of the Company that is unknown to the Board or any committee thereof as of the date of the Merger Agreement and becomes known to the Board or any committee thereof (an Intervening Event) or (bb) an Alternative Proposal, the Board (acting through the Special Committee, if then in existence) may at any time prior to receipt of the required stockholder approvals, make a Recommendation Change and/or terminate the Merger Agreement if (and only if):

- in the case of an Alternative Proposal, the Alternative Proposal (that did not result from a breach of the no shop provision) is made to the Company by a third party, and such Alternative Proposal is not withdrawn, the Board (acting through the Special Committee, if then in existence) determines in good faith after consultation with its financial advisors and outside legal counsel that such Alternative Proposal constitutes a Superior Proposal and the Board (acting through the Special Committee, if then in existence) determines to terminate the Merger Agreement; and

- in the case of an Intervening Event, following consultation with outside legal counsel, the Board (acting through the Special Committee, if then in existence) determines that the failure to make a Recommendation Change could reasonably be expected to be inconsistent with the fiduciary duties of the Board (acting through the Special Committee, if then in existence) under applicable laws.

In either case, (x) the Company must provide Parent three business days prior written notice of its intention to take such action, which notice must include the information with respect to such Superior Proposal (if applicable) that is specified in the no shop provision or a description of such Intervening Event (if applicable) and must otherwise specify the basis for the Recommendation Change or proposed termination, (y) after providing such notice and prior to making such Recommendation Change in connection with an Intervening Event or a Superior Proposal, or taking any action to terminate the Merger Agreement with respect to a Superior Proposal, as applicable, the Company must negotiate in good faith with Parent during such three business day period (to the extent that Parent desires to negotiate) to make such revisions to the terms of the Merger Agreement as would permit the Board and the Special Committee not to effect a Recommendation Change in connection with an Intervening Event or a Superior Proposal or to take such action to terminate the Merger Agreement in response to a Superior Proposal, and (z) the Board and the Special Committee must have considered in good faith any changes to the Merger Agreement offered in writing by Parent and must have determined in good faith, after consultation with its outside legal counsel and financial advisors, that the event continues to constitute an Intervening Event or that the Superior Proposal would continue to constitute a Superior Proposal, in each case, if such changes offered in writing by Parent were to be given effect. However, neither the Board nor any committee thereof may effect a Recommendation Change in connection with an Intervening Event or a Superior Proposal or take any action to terminate the Merger Agreement with respect to a Superior Proposal prior to the time that is three business days after it has provided the required written notice; provided, further, that in the event that the Alternative Proposal is modified subsequently by the party making such Alternative Proposal, the Company must provide written notice of such modified Alternative Proposal and must again comply with the no shop provision.

See the section entitled *The Merger Agreement Non-Solicitation* beginning on page 63.

Termination (page 66)

The Merger Agreement may be terminated and abandoned at any time prior to the Effective Time, whether before or (subject to the terms of the Merger Agreement) after any approval of the matters presented in connection with the Merger by the stockholders of the Company:

by the mutual written consent of the Company and Parent;

by either the Company or Parent, if:

the Effective Time shall not have occurred on or before the one year anniversary of the date of the Merger Agreement (the End Date), and the party seeking to terminate the Merger Agreement shall not have breached its obligations under the Merger Agreement in any manner that shall have proximately caused the failure to consummate the Merger on or before such date;

an injunction, other legal restraint or order shall have been entered permanently restraining, enjoining or otherwise prohibiting the consummation of the Merger and such injunction, other legal restraint or order shall have become final and nonappealable; provided, that the party seeking to terminate the Merger Agreement

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shall have used its commercially reasonable efforts to remove such injunction, other legal restraint or order in accordance with the Merger Agreement; or

the special meeting (including any adjournments thereof) shall have concluded and the stockholder approvals contemplated by the Merger Agreement shall not have been obtained;

by the Company:

if there shall have been a breach of any of the covenants or agreements or failure to be true of any of the representations or warranties on the part of Parent, which breach or failure to be true, either individually or in the aggregate (A) would result in a failure of a closing condition of Parent and Merger Sub set forth in the Merger Agreement and (B) cannot be cured by the End Date; provided, that the Company shall have given Parent written notice, delivered at least 30 days prior to such termination, stating the Company s intention to terminate the Merger Agreement and the basis for such termination; provided, further, that the Company shall not have the right to terminate the Merger Agreement if the Company is then in material breach of any of its representations, warranties, covenants or agreements contained in the Merger Agreement; or

prior to obtaining the required stockholder approvals, in order to enter into a definitive agreement with respect to a Superior Proposal, but only if the Company has complied in all material respects with its obligations under the no shop provisions;

by Parent:

if there shall have been a breach of any of the covenants or agreements or failure to be true of any of the representations or warranties on the part of the Company which breach or failure to be true, either individually or in the aggregate (A) would result in a failure of a closing condition of the Company set forth in the Merger Agreement and (B) which is not cured within the earlier of (I) the End Date; and (II) 30 days following written notice to the Company; provided, that Parent shall have given the Company written notice, delivered at least 30 days prior to such termination, stating Parent s intention to terminate the Merger Agreement and the basis for such termination; provided, further, that Parent shall not have the right to terminate the Merger Agreement if Parent is then in material breach of any of its representations, warranties, covenants or agreements contained in the Merger Agreement;

prior to obtaining the required stockholder approvals, if the Board or the Special Committee withdraws or modifies, in a manner adverse to Parent or Merger Sub, or publicly proposes to withdraw or modify, in a manner adverse to Parent or Merger Sub, its recommendation, fails to use commercially reasonable efforts to obtain the required stockholder approvals in accordance with the Merger Agreement or approves or recommends, or publicly proposes to approve or recommend, any Alternative Proposal; or

prior to obtaining the required stockholder approvals, if the Company or any of its subsidiaries or representatives materially breaches its obligations under the no shop provision or its obligations under the Merger Agreement concerning filings and other actions related to this proxy statement or the Company gives Parent notification that it intends to make a Recommendation Change and/or terminate the Merger Agreement due to an Alternative Proposal or Intervening Event contemplated by the Merger Agreement.

In the event that the Court does not approve the Settlement, the parties to the Merger Agreement have agreed to proceed with the consummation of the Merger based on the Original Merger Consideration of $10.00 per share, without the $3.00 per share increase to the Merger Consideration contemplated by the Second Amendment, which would involve the solicitation of stockholder approval at such $10.00 price per share. The Second Amendment further allows for the extension of the End Date to provide reasonably sufficient time for stockholder approval.

Fees and Expenses (pages 47, 67)

If the Merger is not consummated, all costs and expenses incurred in connection with the Merger, the Merger Agreement and the transactions contemplated thereby shall be paid by the party incurring or required to incur such expenses. If the Merger is consummated, all costs and expenses incurred by Parent or Merger Sub in connection with the Merger, the Merger Agreement and the transactions contemplated thereby shall be paid by the Surviving Corporation and/or, to the extent applicable, reimbursed to Parent by the Surviving Corporation. See the section entitled *Special Factors Fees and Expenses* beginning on page 47 and the section entitled *The Merger Agreement Fees and Expenses* beginning on page 67.

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QUESTIONS AND ANSWERS ABOUT THE SPECIAL MEETING AND THE MERGER

The following questions and answers address briefly some questions you may have regarding the special meeting of stockholders, the Merger Agreement and the Merger. These questions and answers may not address all questions that may be important to you as a stockholder of the Company. Please refer to the more detailed information contained elsewhere in this proxy statement, the annexes to this proxy statement and the documents referred to in or incorporated by reference into this proxy statement.

Q: Why am I receiving this proxy statement?

A: On June 4, 2013, we entered into the Merger Agreement providing that Merger Sub will be merged with and into the Company, whereupon the separate corporate existence of Merger Sub will cease, and the Company will continue as the Surviving Corporation and a wholly owned subsidiary of Parent. Following the Effective Time, the Company would be privately held as a wholly owned subsidiary of Parent. As our stockholders must vote on the adoption of the Merger Agreement, and the Closing is subject to a non-waivable condition that the Merger Agreement be adopted by the affirmative vote of holders of a majority of outstanding shares of Common Stock not owned by Parent, Merger Sub, Mr. Gumbiner or their respective affiliates, you are receiving this proxy statement in connection with the solicitation of proxies by the Board in favor of the proposal to adopt the Merger Agreement and the other matters to be voted on at the special meeting (if any).

Q: What matters will be voted on at the special meeting?

A: You will be asked to consider and vote on the following proposals:

- to adopt the Merger Agreement;
- to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement; and
- to act upon other business that may properly come before the special meeting or any adjournment or postponement thereof by or at the direction of the Board.

Q: Where and when is the special meeting?

A: The special meeting will be held at 3710 Rawlins, Suite 1500, Dallas, Texas 75219 on April , 2014, at [ ], Central Time.

Q: Who can attend and vote at the special meeting?

A: All stockholders of record as of the close of business on the Record Date are entitled to receive notice of and to attend and vote at the special meeting, or any adjournment or postponement thereof. A complete list of stockholders entitled to vote at the special meeting will be available for examination by any stockholder at 3710 Rawlins, Suite 1500, Dallas, Texas 75219, during regular business hours for a period of no less than ten days before the special meeting, and at the special meeting. We are commencing our solicitation of proxies on March , 2014. We will

continue to solicit proxies until the date of the special meeting. If you wish to attend the special meeting and are a stockholder of record on the Record Date, please be prepared to provide proper identification, such as a driver s license. If you wish to attend the special meeting and your shares of Common Stock are held in street name by your broker, bank or other nominee, you will need to provide proof of ownership, such as a recent account statement or letter from your bank, broker or other nominee, along with proper identification. Street name holders who wish to vote at the special meeting will need to obtain a proxy executed in such holder s favor from the broker, bank or other nominee that holds their shares of Common Stock. Seating will be limited at the special meeting.

Q: What is a quorum?

A: In order for any matter to be considered at the special meeting, there must be a quorum present. The presence, in person or represented by proxy, of the holders of a majority of the shares of the Common Stock entitled to vote on such matters as of the Record Date will constitute a quorum. Shares of Common Stock represented by proxies reflecting abstentions and properly executed broker non-votes (if any) will be counted as present and entitled to vote for purposes of determining a quorum. If a quorum is not present, the stockholders entitled to vote at the meeting who are present or represented by proxy may adjourn the meeting until a quorum is present. However, given Parent s ownership of 65.7% of the issued and

outstanding shares of Common Stock, Parent s attendance at the special meeting, by itself, will constitute a quorum. See the section entitled *The Special Meeting Record Date and Quorum* on page 54.

Q: What will I receive in the Merger?

A: If the Settlement is approved and the Closing occurs, you will be entitled to receive $13.00 in cash, without interest, less a proportionate deduction for any incentive fee and attorney s fees that may be awarded by the Court in connection with the Stipulation of Settlement, filed on February 7, 2014, relating to the Sample Litigation, for each share of Common Stock you own, unless you properly exercise, and do not withdraw or lose, appraisal rights under Section 262. For example, if you own 100 shares of Common Stock, you will be entitled to receive $1,300 in cash in exchange for your shares of Common Stock, without interest, less a proportionate deduction for any incentive fee and attorney s fees that may be awarded by the Court. The plaintiff and plaintiff s attorneys in the Sample Litigation intend to petition the Court for a $15,000 incentive fee and attorney s fees and expenses not exceeding $310,000 which is equivalent to approximately $0.62 per share. Therefore, if the Settlement is approved, the Company expects that the Merger Consideration will be at least $12.38 per share and may be more if the Court does not approve the full amount requested by the plaintiff and the plaintiff s counsel. In the event that the Court does not approve the Settlement, the parties to the Merger Agreement have agreed to proceed with the consummation of the Merger based on the Original Merger Consideration of $10.00 per share, without the $3.00 per share increase to the Merger Consideration contemplated by the Second Amendment, which would involve the solicitation of stockholder approval at such $10.00 price per share. The Sample Litigation is more fully described under the section entitled *Special Factors Litigation.* You will not be entitled to receive shares in the Surviving Corporation or in Parent. Parent will be entitled to deduct and withhold from the Merger Consideration otherwise payable, any amounts that are required to be withheld or deducted under the Code, or any provision of U.S., state, local or foreign laws. To the extent that the amounts are withheld or deducted, those withheld or deducted amounts will be treated for all purposes as having been paid to the holder of shares of Common Stock in respect of which such deduction and withholding were made.

Q: Is the Merger expected to be taxable to me?

A: If you are a U.S. holder, the receipt of cash for your shares of Common Stock as part of the Merger will generally be a taxable transaction for U.S. federal income tax purposes. If you are a non-U.S. holder, the receipt of cash for your shares of Common Stock as part of the Merger will generally not be a taxable transaction for U.S. federal income tax purposes, unless you have certain connections to the United States. See the section entitled *Special Factors Material U.S. Federal Income Tax Consequences of the Merger* beginning on page 44. You should consult your own tax advisors regarding the particular tax consequences to you of the exchange of shares of Common Stock for cash pursuant to the Merger in light of your particular circumstances (including the application and effect of any state, local, foreign and other tax laws).

Q: What vote of our stockholders is required to approve the proposal to adopt the Merger Agreement?

A: Under Delaware law, stockholders holding at least a majority of the shares of Common Stock outstanding and entitled to vote at the close of business on the Record Date must vote **FOR** the proposal to adopt the Merger Agreement. In addition, the Merger Agreement provides that the Closing is subject to a non-waivable condition that the Merger Agreement be adopted by (i) the affirmative vote of the holders of a majority of the outstanding shares of our Common Stock entitled to vote on the adoption of the Merger Agreement, voting together as a single class, and (ii) the affirmative vote of the holders of a majority of the outstanding shares of Common Stock, voting together as a single class, excluding all shares of Common Stock owned by Parent, Merger Sub, Mr. Gumbiner or any of their respective affiliates (other than the Company and its subsidiaries), or by any director, officer or other employee of the Company or any of its subsidiaries (the Majority of the Minority Approval). A failure to vote your shares of Common

Stock or an abstention from voting or broker non-vote will have the same effect as a vote against the proposal to adopt the Merger Agreement. As of March 3, 2014 there were 1,525,166 shares of Common Stock issued and outstanding, such being the only class of capital stock and representing 1,525,166 votes in the aggregate to which such class is entitled. Of these total issued and outstanding shares of Common Stock, 523,591 are owned by holders other than Parent, Merger Sub, Mr. Gumbiner or their respective affiliates.

Q: What will happen if I abstain from voting or fail to vote on the proposal to adopt the Merger Agreement?

A: A failure to vote your shares of Common Stock or an abstention from voting will have the same effect as a vote **AGAINST** the proposal to adopt the Merger Agreement. Abstentions will be included in the calculation of the number of shares of Common Stock represented at the special meeting for purposes of determining whether a quorum has been achieved. See the section entitled *The Special Meeting Required Vote* on page 54.

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Q: What vote of our stockholders is required to approve other matters to be discussed at the special meeting?

The proposal to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement requires the affirmative vote of the holders of a majority of the shares of Common Stock present or represented by proxy and entitled to vote thereon. However, given Parent s ownership of 65.7% of the issued and outstanding shares of Common Stock, adjournment of the special meeting may be approved solely by the affirmative vote of Parent s shares.

Q: How does the Board recommend that I vote?

A: The Board (without Mr. Gumbiner s participation), acting on the unanimous recommendation of the Special Committee, unanimously recommends that our stockholders vote:

- **FOR** the proposal to adopt the Merger Agreement;
- **FOR** the proposal to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement.

You should read the section entitled *Special Factors Background of the Merger Reasons for the Merger; Fairness of the Merger; Recommendations of the Special Committee and the Board* beginning on page 23 for a discussion of the factors that the Special Committee and the Board (without Mr. Gumbiner s participation) considered in deciding to recommend the approval of the Merger Agreement and the section entitled *Special Factors Interests of the Company s Directors and Executive Officers in the Merger* beginning on page 43.

Q: How will the Company s directors and executive officers vote on the proposal to adopt the Merger Agreement?

A: Of the Company s directors and current executive officers, only Mr. Charles A. Crocco, Jr. (director) and Mr. Gumbiner, through Parent, own shares of Common Stock. Mr. Crocco has informed the Company that, as of the date of the filing of this proxy statement, he intends to vote in favor of the proposal to adopt the Merger Agreement. As of March 3, 2014, Mr. Crocco owned 9,996 shares of Common Stock entitled to vote at the special meeting.

Q: Am I entitled to exercise appraisal rights instead of receiving the Merger Consideration for my shares of Common Stock?

A: Pursuant to Section 262, stockholders who do not vote in favor of the Merger and who comply with the applicable requirements of Section 262 and do not withdraw or otherwise lose the right of appraisal are entitled to statutory appraisal rights under Delaware law in connection with the Merger. This means that if you comply precisely with the requirements of Section 262, you are entitled to seek appraisal of the fair value of your shares of Common Stock determined by the Court of Chancery of the State of Delaware and to receive payment based on that valuation instead of receiving the Merger Consideration. If you validly exercise (and do not withdraw or lose) appraisal rights, the ultimate amount you may be entitled receive in an appraisal proceeding may be more than, the same as or less than the amount you would have received under the Merger Agreement. To exercise your appraisal rights, (i) you must submit a written demand for appraisal to us before the vote is taken on the Merger Agreement, (ii) you must NOT vote in

favor of the proposal to adopt the Merger Agreement and (iii) you must otherwise comply precisely with the requirements of Section 262. Your failure to follow precisely the procedures specified under Delaware law could result in the loss of your appraisal rights. See the section entitled *Rights of Appraisal* beginning on page 77 and the text of the Delaware appraisal rights statute, Section 262, which is reproduced in its entirety as Annex C to this proxy statement. Assuming you have otherwise complied with the requirements of Section 262, your right to seek appraisal under Section 262 is not released under the Settlement, but if the Settlement is approved, you may not claim value related to or arising from the derivative claims that are released, settled, and dismissed with prejudice pursuant to the Settlement.

Q: What effects will the Merger have on the Company?

A: The Common Stock is currently registered under the Exchange Act, and is quoted on the NYSE MKT stock exchange (the NYSE MKT) under the symbol HWG. As a result of the Merger, the Company will cease to have publicly traded equity securities and will be wholly owned by Parent. Following the Closing, the registration of Common Stock and our reporting obligations under the Exchange Act with respect to such registration will be terminated upon application to the

SEC. In addition, upon the Closing, our Common Stock will no longer be listed on the NYSE MKT or any other stock exchange or quoted on any quotation system.

Q: When is the Merger expected to be completed?

A: The parties to the Merger Agreement are working to complete the Merger as quickly as possible. In order to complete the Merger, the Company must obtain the stockholder approvals described in this proxy statement and the other closing conditions under the Merger Agreement must be satisfied or waived. The Company currently expects the Closing to occur soon after the special meeting. The Company, however, can provide no assurance that the Closing will occur by any particular date, if at all. Because the Closing is subject to a number of conditions, the exact timing of the Merger cannot be determined at this time. For more information, see *The Merger Agreement When the Merger Becomes Effective* beginning on page 58.

Q: What happens if the Merger is not consummated?

A: If the proposal to adopt the Merger Agreement is not approved by the Company s stockholders, or if the Merger is not consummated for any other reason, the Company s stockholders will not receive any payment for their shares in connection with the Merger. Instead, the Company will remain a public company and shares of its Common Stock will continue to be listed and traded on the NYSE MKT. For more information, see the section entitled *The Merger Agreement Termination* beginning on page 66.

Q: What do I need to do now?

A: We urge you to read this proxy statement carefully, and in its entirety, including its annexes and the documents referred to in, or incorporated by reference into, this proxy statement, and to consider how the Merger affects you. If you are a stockholder of record, you can ensure that your shares are voted at the special meeting by submitting your proxy via:

mail, using the enclosed postage-paid envelope;

telephone, using the toll-free number listed on each proxy card; or

the Internet, at the Internet address provided on each proxy card.

If you hold your shares in street name through a broker, bank or other nominee, you should follow the directions provided by your broker, bank, or other nominee regarding how to instruct your broker, bank, or other nominee to vote your shares. Without those instructions, your shares will not be voted, which will have the same effect as voting against the proposal to adopt the Merger Agreement.

Q: Should I send in my stock certificates or other evidence of ownership now?

A: No. After the Merger is completed, you will be sent a letter of transmittal with detailed written instructions for exchanging your shares of Common Stock for the Merger Consideration. If your shares of Common Stock are held in street name by your broker, bank or other nominee, you may receive instructions from your broker, bank or other nominee as to what action, if any, you need to take to effect the surrender of your street name shares in exchange for

the Merger Consideration. **Do not send in your certificates now.**

Q: What happens if I sell my shares of Common Stock after the Record Date but before the date of the special meeting?

A: The record date for the special meeting is earlier than the date of the special meeting and the expected date on which the Closing will occur. If you transfer your shares of Common Stock after the Record Date but before the date of the special meeting, you will retain your right to vote at the special meeting (provided such shares remain outstanding on the date of the special meeting), but you will not have the right to receive the Merger Consideration to be received by the Company s stockholders in the Merger. In order to receive the Merger Consideration, you must hold your shares of Common Stock through the Closing.

Q: Can I revoke my proxy?

A: Yes. You can revoke your proxy at any time before the vote is taken at the special meeting. If you are a stockholder of record, you may revoke your proxy by notifying the Company s Corporate Secretary in writing at The Hallwood Group

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Incorporated, Attn: Corporate Secretary, 3710 Rawlins, Suite 1500, Dallas, Texas 75219, or by submitting a new proxy by telephone, the Internet or mail, in each case, dated after the date of the proxy being revoked. In addition, you may revoke your proxy by attending the special meeting and voting in person, although simply attending the special meeting will not cause your proxy to be revoked. If you hold your shares in street name and you have instructed a broker, bank or other nominee to vote your shares, the options described above for revoking your proxy do not apply, and instead you must follow the instructions received from your broker, bank or other nominee to revoke your proxy or submit new voting instructions.

Q: What does it mean if I get more than one proxy card or voting instruction card?

A: If your shares are registered differently or are held in more than one account, you will receive more than one proxy or voting instruction card. Please complete and return all of the proxy cards or voting instruction cards you receive (or submit each of your proxies by telephone or the Internet, if available to you) to ensure that all of your shares are voted.

Q: What is householding and how does it affect me?

A: The SEC permits companies to send a single set of proxy materials to any household at which two or more stockholders reside, unless contrary instructions have been received, but only if the applicable company provides advance notice and follows certain procedures. In such cases, each stockholder continues to receive a separate notice of the meeting and proxy card. Certain brokerage firms may have instituted householding for beneficial owners of Common Stock held through brokerage firms. If your family has multiple accounts holding Common Stock, you may have already received householding notification from your broker. Please contact your broker directly if you have any questions or require additional copies of this proxy statement. The broker will arrange for delivery of a separate copy of this proxy statement promptly upon your written or oral request. You may decide at any time to revoke your decision to household, and thereby receive multiple copies.

Q: Who can help answer my other questions?

A: If you have more questions about the special meeting, or require assistance in submitting your proxy or voting your shares or need additional copies of the proxy statement or the enclosed proxy card, please contact Georgeson Inc., which is acting as the Company s proxy solicitation agent:

Call Toll-Free 1-866-391-7007

Email: hallwood@georgeson.com

If your broker, bank or other nominee holds your shares, you should also call your broker, bank or other nominee for additional information.

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SPECIAL FACTORS

BACKGROUND OF THE MERGER

Background of the Merger

The Board of Directors of the Company (the Board) and management, regularly and in the ordinary course of business, evaluate potential strategic alternatives available to the Company in an effort to enhance stockholder value. On June 13, 2012, at Mr. Gumbiner s request, Hunton & Williams LLP (Hunton & Williams) advised the independent members of the Board that Mr. Gumbiner believed it would be appropriate for Parent to consider the status and structure of Parent s ownership of Hallwood Group and had requested that those independent members of the Board consent to Hunton & Williams representation of Parent in that connection. The independent directors provided that consent on behalf of the Company and the Board on June 21, 2012. However, during the months of July and August of 2012, Mr. Gumbiner advised the independent members of the Board that he had not determined whether, on what basis or when he might make any proposal concerning the Company.

At the meeting of the Board held on September 4, 2012, management of the Company discussed with the independent members of the Board whether it would be appropriate for the Board to consider a transaction to take the Company private, but in late October, the independent directors determined that they did not believe they were able to consider such a transaction in the abstract. After management of the Company advised Mr. Gumbiner of that determination, on about November 1, 2012, Mr. Gumbiner informed management of the Company, and on November 6, 2012, advised Mr. Crocco by telephone that Parent intended to propose to acquire all of the outstanding shares of Common Stock that were not already beneficially owned by Parent, at a cash purchase price of $10.00 per share. In determining the proposed purchase price, Parent did not engage any third party advisors, obtain any valuations from third parties or conduct any formal valuation of the Company. Parent determined the proposed purchase price based on Mr. Gumbiner s general knowledge of and familiarity with the Company and its business and his understanding of all available information regarding the Company, without particularly focusing on any specific aspects of the business or any specific information. The price Parent proposed was not based on any calculation of book value, market value, going concern value, liquidation value, comparable companies or comparable transactions, but on Mr. Gumbiner s personal assessment of what he was willing for Parent to pay and his personal judgment regarding a price that would be acceptable to the Special Committee and the stockholders of the Company. Mr. Gumbiner understood that the proposed price constituted a premium over the market price of the Common Stock at that time, and believed that this was appropriate because the Special Committee and the stockholders would be unlikely to accept a price that did not include a premium to the then current market price. In arriving at the price, Parent took into account the factors described in *Special Factors The Parent Filing Persons Purposes And Reasons For The Merger* and *The Parent Filing Persons Position As To The Fairness Of The Merger*.

Later on November 6, 2012, Mr. Gumbiner sent a letter (the Proposal Letter) to the rest of Board setting forth the proposal from Parent to acquire all of the outstanding shares of Common Stock that were not already beneficially owned by Parent at a cash purchase price of $10.00 per share (the Proposed Transaction). The Proposal Letter specified that the Proposed Transaction would be in the form of a merger of the Company with a new acquisition vehicle that Parent would form. The Proposal Letter also specified that the Proposed Transaction would be governed by a merger agreement providing for a non-waivable condition requiring the approval of a majority of the shares of the Company that are not directly or indirectly owned by Parent, and that it was expected that the Board would establish a special committee of independent directors to consider the Proposed Transaction on behalf of the Company s public stockholders and to make a recommendation to the full Board. In addition, the Proposal Letter stated that, in its capacity as a stockholder of the Company, Parent was interested only in acquiring the shares of the Company that it did not currently own, and that in such capacity Parent had no interest in a disposition or sale of its

interest in the Company, nor was it Parent s intention to vote in favor of any alternative sale, merger or similar transaction involving the Company. As such, without the approval of Parent as the Company s controlling stockholder, no transaction other than the Proposed Transaction would be possible.

On November 7, 2012, in response to the Proposal Letter, the Board formed a special committee (the Special Committee) of independent directors for the purposes of negotiating the Proposed Transaction on an arm s length basis against Parent, consisting of Charles A. Crocco, Jr., Amy H. Feldman and Michael R. Powers, all of the Company s independent directors. The Special Committee was empowered, among other things, to consider whether the Proposed Transaction was in the best interests of the Company and the holders of the Common Stock, consider and review potential alternative transactions, and, in its own and full discretion, reject the Proposed Transaction if the Special Committee determined it was not fair to or otherwise not in the best interests of the Company and the holders of the Common Stock, in addition to considering other matters deemed appropriate by the Special Committee. The Board empowered the Special Committee to, among other things, retain its own independent legal and financial advisors to assist in its review of the Proposed Transaction. The Board also resolved to refrain from taking any action in relation to the Proposed Transaction, including, without limitation, its negotiation, rejection or approval, without first having obtained a recommendation from the Special Committee that the Board take such action. The Board established the compensation for each member of the Special Committee as $1,000 per meeting of the Special Committee attended and $125 per

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hour (or a proportionate amount thereof for each hourly fraction) for other time expended on Special Committee matters. The Special Committee retained Wick Phillips Gould & Martin, LLP (Wick Phillips) on November 8, 2012 as its independent legal counsel.

On November 9, 2012, the Company issued a press release announcing the Company s receipt of the Proposal Letter and the Board s formation of the Special Committee, and filed a copy with the SEC as an exhibit to a Current Report on Form 8-K on the same day.

On November 14, 2012, Hallwood Energy I Creditors Trust (HEI Creditors Trust), successor-in-interest to Hallwood Energy, L.P., the plaintiff in the case originally styled as *Hallwood Energy, L.P. v. The Hallwood Group Incorporated* pending in the Bankruptcy Court of the Northern District of Texas (the Bankruptcy Court), a description of which can be found under *Special Factors Litigation* , filed a motion requesting that the Bankruptcy Court direct the Company to comply with the Bankruptcy Court s prior order issued on May 28, 2010. That order required the Company to notify the Bankruptcy Court of any intention to sell assets out of the ordinary course of business, pay a dividend, distribution or return of capital to its stockholders or transfer in any manner any assets to its majority stockholder or its affiliates outside the ordinary course of business. In reference to such order, the November 14, 2012 motion sought to enjoin the Company from participating in the Proposed Transaction.

On December 3, 2012, the Special Committee held a telephonic meeting, at which representatives of Wick Phillips were also in attendance, during which it discussed, among other things, the independence of the members of the Special Committee and the need for engaging an independent financial advisor to the Special Committee to assist in the negotiation and evaluation of the Proposed Transaction. Based upon Wick Phillips advice regarding the required Delaware law independence standard, Mr. Crocco confirmed his independence and the Special Committee determined Mr. Crocco to be independent for purposes of serving on the Special Committee. The Special Committee also noted during its meeting the Company s recent engagement of K&L Gates LLP (K&L Gates) as counsel to the Company.

On December 12, 2012, Wick Phillips interviewed each of Ms. Feldman and Mr. Powers. During such interviews, Wick Phillips discussed with each of Ms. Feldman and Mr. Powers, among other things, any interest that they or their respective families may have in the Proposed Transaction, their relationship with Mr. Gumbiner, the percentage that their compensation as directors of the Company represented out of their respective families total assets and any other factors or relationships that could adversely affect their ability to consider the merits of the Proposed Transaction in a neutral, non-biased manner. Following their respective interviews and after receiving advice from Wick Phillips, each of Ms. Feldman and Mr. Powers confirmed their independence from Parent for the purposes of serving on the Special Committee.

Each member of the Special Committee was determined to be independent for purposes of the Proposed Transaction. Each member of the Special Committee was determined to have the requisite level of independence from Parent and its ultimate owner, Mr. Gumbiner, because it was determined that no Special Committee member has a relationship with Parent or Mr. Gumbiner that would affect his or her ability to independently negotiate the Proposed Transaction on behalf of the Company s minority and unaffiliated stockholders. In the Special Committee meeting on December 3, 2012, Mr. Crocco was able to confirm that he was independent because he has no relationship, whether financial or personal, with Parent or its ultimate owner, Mr. Gumbiner, other than as a director of the Company and his minor stockholding in the Company (described on page 43). However, Mr. Powers and Ms. Feldman have had, and continue to have a social relationship with Mr. Gumbiner. Ms. Feldman s husband had previously received an indirect referral fee for a real estate transaction involving Mr. Gumbiner (although that fee was an insignificant component of Ms. Feldman s family income). For these reasons the Special Committee requested that Wick Phillips conduct a further analysis into the relationships of Mr. Powers and Ms. Feldman to verify they each satisfied the independence standard under Delaware law. As noted above, on December 12, 2012, Wick Phillips interviewed Mr. Powers and

Ms. Feldman. Each explained their prior and current relationship with Mr. Gumbiner and affirmatively stated that such relationship would not affect their ability to independently negotiate the Proposed Transaction on behalf of the Company s minority and unaffiliated stockholders. From these interviews, and the discussions in the December 3, 2012, meeting, Wick Phillips concluded that each member of the Special Committee satisfied the requisite level of independence to negotiate the Proposed Transaction on behalf of the Company s minority and unaffiliated stockholders. The Special Committee relied upon such conclusion.

Each member of the Special Committee was also determined to be disinterested because they have no financial interest or other material interest in the Proposed Transaction, other than their compensation as directors and Mr. Crocco s minor stockholding in the Company as described on page 43.

During the week of December 19, 2012, Mr. Crocco, on behalf of the Special Committee, interviewed five investment banking candidates to act as independent financial advisor to the Special Committee in connection with the Proposed Transaction.

On January 7, 2013, the Special Committee held a telephonic meeting at which a representative of Wick Phillips was also in attendance, during which it discussed the results of Mr. Crocco s interviews with Southwest Securities and the four other investment banks, and, after consideration, selected Southwest Securities as its independent financial advisor in connection with the Proposed Transaction. The criteria for the Special Committee s selection of Southwest Securities over the other four investment banks were the experience of Southwest Securities as a large, sophisticated investment bank, its quality presentation to Mr. Crocco, its preparation for such presentation and resulting knowledge about the Company and its competitive fee bid. On January 10, 2013, the Company executed an engagement letter with Southwest Securities as financial advisor to the Special Committee.

On January 10, 2013, after a hearing on HEI Creditors Trust s November 14, 2012 motion which was held on January 7, 2013, the Bankruptcy Court entered an order (the Notice Order) requiring the Company to notify the Bankruptcy Court and HEI Creditors Trust after entering into a material, definitive agreement to consummate any transaction similar to that described in the Proposal Letter and the related Form 8-K filed by the Company. Pursuant to the Notice Order, upon the signing of any such agreement, the Company was required to provide at least 35 days prior notice of the earliest anticipated closing date of the Proposed Transaction so that HEI Creditors Trust could request a hearing as to whether the Proposed Transaction is prohibited by the Notice Order. The Company s required notice was to be in the form of a copy of a Current Report on Form 8-K reporting the entry into a material, definitive agreement as filed with the SEC.

On January 23, 2013, Mr. Crocco, Southwest Securities and Wick Phillips met telephonically to discuss business and financial due diligence being performed by Southwest Securities with respect to the Company.

On January 29, 2013, William L. Guzzetti and Richard Kelley, the respective President and Chief Operating Officer and Chief Financial Officer of the Company, met with Southwest Securities at the Company s offices to provide Southwest Securities with a historical overview of the Company. Among other items discussed, the Company s management explained to Southwest Securities that the Company was unable, and it was not the Company s practice, to prepare cash flow projections beyond one year, as a result of the Company s reliance on orders from the U.S. military as its predominant source of revenue and the uncertainty as to when during the year such orders would be placed.

During the week of February 11, 2013, as part of its due diligence review, Southwest Securities conducted on-site visits to the facilities of the Company and updated Wick Phillips as to its progress. Southwest Securities informed Wick Phillips that, although it was not customary for bankers to conduct an analysis for the purposes of preparing a fairness opinion without the benefit of cash flow projections from the target company s management, Southwest Securities would consider other factors in performing its analysis, such as a comparable company analysis, selected precedent transaction analysis, and premiums paid analysis as more fully described in *Summary of Southwest Securities Analyses.*

On March 11, 2013, the Special Committee held a telephonic meeting, at which representatives of Wick Phillips and Southwest Securities were also in attendance, for a discussion led by Southwest Securities, regarding the financial analysis performed by Southwest Securities in connection with the Proposed Transaction and the fairness of the proposal contained in the Proposal Letter to the Company s minority and unaffiliated stockholders. Southwest Securities reported to the Special Committee that, as part of such analysis, Southwest Securities performed (i) a market analysis of companies comparable to the Company, (ii) an analysis of precedent mergers and acquisitions transactions that Southwest Securities deemed similar to the Proposed Transaction and (iii) an analysis of the premiums paid in connection with transactions similar to the Proposed Transaction. Southwest Securities and the Special Committee also discussed the fact that, due to the uncertainty of the Company s prospects as a result of its business material reliance on U.S. military activity, the Company s management had not been able to provide five-year

financial projections or estimates of future performance beyond 2013, and that Southwest Securities was thus unable to conduct a discounted cash flow analysis. The Special Committee then asked Southwest Securities for its view with respect to the valuation of the Company s property, plant and equipment on its balance sheet. Southwest Securities explained that it did not perform an independent evaluation, physical inspection or appraisal of any of the assets or liabilities (contingent or otherwise) of the Company, and had not been furnished with any such valuations or appraisals. After deliberation, the Special Committee decided to look further into obtaining a valuation of the Rhode Island facilities of Kenyon Industries, Inc., a subsidiary of the Company, for the purposes of considering the possibility of a liquidation of such parcel of real estate.

On March 18, 2013, the Special Committee held a telephonic meeting, at which representatives of Wick Phillips were also in attendance, to discuss, among other things, the Special Committee s duties with respect to the Proposed Transaction, the Special Committee s progress as to the evaluation of Parent s proposal contained in the Proposal Letter and the Special Committee s preferred strategy in negotiating with Parent for the benefit of the Company s minority and unaffiliated stockholders.

On March 25, 2013, the Special Committee held a telephonic meeting, at which representatives of Wick Phillips and, for a portion of such meeting, Southwest Securities, were also in attendance. The Special Committee discussed the results of an informal estimate of the Company s Rhode Island site s value that was obtained by Ms. Feldman with the help of a real estate broker (which amounted to $2 million), the Company s debt levels (which exceed $2 million), and a concern about potential environmental issues at the Rhode Island site. The Special Committee concluded it was unlikely that further exploration of the real estate liquidation value of such property would indicate a value in excess of the Company s current debt and, therefore, decided not to further pursue such valuation. After Southwest Securities joined the meeting, a discussion ensued regarding the Company s continued liquidity issues and the probability that the audit opinion from the Company s independent registered public accounting firm, Deloitte & Touche LLP (Deloitte), to be included in Company s upcoming Annual Report on Form 10-K for the fiscal year ended December 31, 2012, might contain a going concern explanatory paragraph. A going concern explanatory paragraph included in the unqualified opinion from a company s independent registered public accounting firm references the readers of the company s financial statements to a company s disclosure regarding the current financial position and the company s analysis, based upon current financial resources, as to whether the company can meet its obligations over the next year in order to continue as a going concern. The Special Committee discussed with its advisors its concern that, as a result of such liquidity issues, the Company s minority and unaffiliated stockholders could be harmed by a drop in the Company s stock price followed by a reduction or possible withdrawal of Parent s bid to consummate the Proposed Transaction. The Special Committee requested that Wick Phillips and Southwest Securities contact Hunton & Williams to discuss and negotiate the terms of the Proposed Transaction on the basis of the comments discussed during the meeting. In particular, because the Special Committee was concerned about losing the $10.00 per share offer in light of the Company s liquidity issues and preliminary report from Southwest Securities, it instructed Wick Phillips to inquire whether Parent would consider increasing its offered price, rather than aggressively demand a higher price.

On March 25, 2013, as instructed by the Special Committee, Wick Phillips and Southwest Securities held a telephonic meeting with Hunton & Williams to begin negotiating the terms of the Proposed Transaction and inquired whether Parent would consider increasing the price per share that it was prepared to offer.

On March 26, 2013, Hunton & Williams replied telephonically to Wick Phillips that in order for Parent to consider a higher price, the Special Committee should provide Parent with information that supported a value for the Common Stock greater than the price of $10.00 per share.

On March 28, 2013, the Special Committee held a telephonic meeting, at which representatives of Wick Phillips and Southwest Securities were also in attendance, for the primary purpose of a presentation by Southwest Securities of an analysis report (a copy of which is attached as Exhibit (c)(2) to Amendment No. 1 to the Schedule 13E-3 filed in conjunction herewith), which had previously been provided to the Special Committee, presenting Southwest Securities findings with respect to the financial terms of the Proposed Transaction and its fairness to the Company s minority and unaffiliated stockholders and to determine the Special Committee s response to Parent. With the assistance of the presentation materials comprising its report, Southwest Securities explained its preliminary conclusion that the Merger Consideration of $10.00 per share originally offered by Parent was a fair price from a financial point of view. The Special Committee then discussed the possible reasons for Parent s offer and proposed Merger Consideration as set forth in the Proposal Letter. On the basis of the Company s lack of liquidity, market and economic considerations and other factors, the Special Committee concluded that it could not present sufficient rationale to Parent supporting a higher price than that offered by Parent. Because of its inability to obtain support for a per share price higher than $10.00 per share, and its concern that the Company s minority and unaffiliated stockholders would be harmed by a withdrawal of Parent s proposed $10.00 offer as discussed in the March 25, 2013 meeting, the Special Committee decided not to ask for an increased purchase price. Following such decision, the Special Committee instructed Wick Phillips to contact Hunton & Williams to request a draft merger agreement reflecting the terms set forth in the

Proposal Letter.

On April 1, 2013, the Company filed its Form 10-K for the year ended December 31, 2012. The Form 10-K disclosed several factors negatively impacting the Company s financial situation, including the Company s dependence on Brookwood for cash, the Company s lack of cash to pay its operating costs or service its existing debt and an audit report from Deloitte, which included an explanatory paragraph related to its status as a going concern resulting from the uncertainty of the payment of dividends from Brookwood to fund the Company s ongoing operations and obligations.

On April 2, 2013, the closing price of the Common Stock dropped to $7.90 per share from its closing price of $8.61 per share on March 28, 2013, the trading day prior to the filing of the Company s Form 10-K.

On April 8, 2013, Hunton & Williams delivered a draft Merger Agreement to the Special Committee.

On April 11, 2013, the Company received a letter from NYSE MKT LLC (the Exchange), indicating that the Company was not in compliance with certain NYSE MKT continued listing standards. The Exchange determined the Company s financial condition had become impaired based upon its review of the Company s Form 10-K for the fiscal year ended December 31, 2012. As a result of the Exchange s review and determination, the Company was not in compliance with one of the Exchange s continued listing standards, and therefore became subject to the procedures and requirements of Section 1009 of the NYSE MKT Company Guide (Company Guide). Specifically, the Company was not in compliance with Section 1003(a)(iv) of the Company Guide in that it had sustained losses which were so substantial in relation to its overall operations or its then-existing financial resources or financial condition had become so impaired that it appeared questionable, in the opinion of the Exchange, as to whether the Company would be able to continue operations and/or meet its obligations as they mature. The letter stated that, in order to maintain the Company s listing with the Exchange, the Company was required to submit a plan of compliance by May 13, 2013 addressing how it intended to regain compliance with Section 1003(a)(iv) by July 15, 2013. If the Company did not submit a plan, or if the plan was not accepted by the Exchange, the Company would be subject to delisting proceedings. Furthermore, if the plan was accepted but the Company was not in compliance with the continued listing standards of the Company Guide by July 15, 2013, or if the Company did not make progress consistent with the plan, the Exchange staff would initiate delisting proceedings in accordance with Section 1010 and Part 12 of the Company Guide.

On April 15, 2013, the Company issued a press release announcing receipt of the April 11, 2013 notice from the Exchange of potential delisting. On April 16, 2013, the Company filed a copy of such press release as an exhibit to a Current Report on Form 8-K.

On April 16, 2013, the Special Committee held a telephonic meeting, at which representatives of Wick Phillips were also in attendance, primarily for the purposes of discussing comments and questions from the Special Committee and Wick Phillips pertaining to the draft Merger Agreement. The Special Committee asked Wick Phillips to revise the draft Merger Agreement accordingly and to deliver the revised version to Hunton & Williams.

On April 19, 2013, the Special Committee, through its counsel, returned a revised draft of the Merger Agreement to Parent, through its counsel. As part of its comments, the Special Committee requested, among other things, additional materiality qualifiers to representations and warranties; a reduced scope of several representations and warranties; a representation by Parent that it has sufficient internal funds to consummate the Proposed Transaction without reliance on funds or assets of the Company, as well as an indication as to the source of such funds; the removal of a covenant of the Company to cooperate with Parent in connection with Parent s efforts to obtain financing for purposes of consummating the Proposed Transaction; the increased ability for the Board to consider alternative proposals without breaching the no shop provision and change its recommendation to the Company s stockholders that they adopt the Merger Agreement; a change to the standard for the Company s efforts with respect to certain pre-closing covenants from reasonable best efforts to commercially reasonable efforts ; certain additional exceptions to occurrences which constitute a Company Material Adverse Effect under the Merger Agreement; the right for the Company to terminate the Merger Agreement if it has satisfied its obligations and waived any unsatisfied obligations of Parent thereunder but Parent fails to proceed with the Proposed Transaction; and the removal of the lack of occurrence of a Company Material Adverse Effect as a condition to Parent s obligation to effect the Proposed Transaction.

On April 22, 2103, Mr. Gumbiner requested that the Special Committee consent to Parent s retention of Potter Anderson & Corroon LLP (Potter Anderson) as its Delaware counsel in connection with the Merger, and waive on the Company s behalf any conflicts of interests faced by Potter Anderson, in light of the fact that Potter Anderson had in the past also represented the Company in certain matters. The Special Committee considered this request and provided its consent, and waiver on the Company s behalf of any conflict of interest, on April 30, 2013.

On April 23, 2013, the Special Committee held a telephonic meeting, at which representatives of Wick Phillips were also in attendance, to discuss, among other matters, the April 11, 2013 letter from the Exchange informing the Company of its potential delisting unless certain measures were put in place. The Special Committee discussed its concern about the ability of the Company to maintain its listing if the Proposed Transaction was not announced and consummated and the potential harm that the failure to maintain such listing could cause to the Company s minority and unaffiliated stockholders.

On April 30, 2013, Hunton & Williams, on behalf of Parent, communicated orally to Wick Phillips Parent s comments to the revised draft of the Merger Agreement that had been circulated by the Special Committee, through its counsel, on April 19, 2013. As part of such comments, Parent generally accepted most of the Special Committee s requested changes, but insisted on keeping the lack of a Company Material Adverse Effect as a condition to Parent s obligation to effect the Proposed Transaction and rejected the ability of the Company to terminate the Merger Agreement if Parent fails to close (while leaving the Company other possibilities for terminating the Merger Agreement in certain other circumstances). Also, in exchange for reducing certain representations and warranties regarding certain environmental matters, Parent added an additional condition precedent to its

obligation to effect the Proposed Transaction that the Company did not suffer environmental liabilities in excess of a certain threshold after the signing of the Merger Agreement.

On May 3, 2013, the Special Committee held a telephonic meeting, at which representatives of Wick Phillips were also in attendance, to discuss, among other things, Parent s comments to the draft Merger Agreement communicated orally to Wick Phillips on April 30, 2013.

On May 4, 2013, Hunton & Williams delivered to Wick Phillips a revised version of the Merger Agreement containing Parent s comments which had previously been communicated orally on April 30, 2013 as described above.

During the week of May 6, 2013, discussions between Wick Phillips and the Special Committee occurred to finalize the then-current draft of the Merger Agreement. The Special Committee considered the fact that Parent had accepted most of the Special Committee s material changes to the Merger Agreement contained in its April 19, 2013 draft (including, among others, the changes making the representations and warranties more favorable to the Company and reinforcing Parent s commitment to finance the Proposed Transaction with internal funds). The Special Committee determined that the significant concessions made by Parent in accepting most of the Special Committee s material transaction points, combined with the relatively few substantial counterproposals included by Parent in its May 4, 2013 draft of the Merger Agreement, had resulted in a balanced draft of the Merger Agreement which the Special Committee had negotiated to the best of its ability in the interest of the Company s minority and unaffiliated stockholders.

On May 9, 2013, representatives of Southwest Securities met with the Company s management team at the Company s Dallas, Texas office to provide Southwest Securities an opportunity to update its due diligence review of the Company.

On May 10, 2013, the Special Committee held a telephonic meeting, at which representatives of Wick Phillips were also in attendance, to discuss, among other items, the status of negotiations of the Merger Agreement and various factors impacting the general timing of the contemplated signing of the Merger Agreement.

On May 13, 2013, the Company submitted a plan of compliance with the Exchange in response to the Exchange s request set forth in its April 11, 2013 letter to the Company. Additionally and as part of the Company plan of compliance, on May 13, 2013, the promissory note associated with the loan to the Company by Hallwood Family (BVI) L.P., an affiliate of Parent (HFL Loan), was amended, pursuant to a Second Amendment to Promissory Note, to convert it to a revolving credit facility to provide additional liquidity to the Company. The maturity date of the promissory note continues to be June 30, 2015. As of March 31, 2013, the outstanding balance of the HFL Loan was $9,047,000, and such amendment resulted in $953,000 of credit availability as of May 13, 2013. Subject to the terms and conditions of the HFL Loan, upon written request, the Company may borrow and receive advances of amounts requested by the Company (including amounts previously repaid) not to exceed either of: (a) the amount in each calendar quarter equal to the amount budgeted by the Company to fund general and administrative costs for that calendar quarter; or (b) an amount that would result in the aggregate principal amount of the HFL Loan to exceed $10,000,000.

During the week of May 27, 2013, K&L Gates communicated to Wick Phillips its comments to the draft Merger Agreement, which comments were primarily aimed at ensuring that certain recent events concerning the Company and its business were adequately disclosed as exceptions to the Company s representations and warranties set forth in the Merger Agreement.

On May 29, 2013, Hunton & Williams delivered to Wick Phillips a final draft of the Merger Agreement containing the agreed upon terms, including the changes requested by K&L Gates on May 27, 2013 and the price per share comprising the original Merger Consideration.

On May 30, 2013, representatives of Southwest Securities met with the Company s management team telephonically to provide Southwest Securities an opportunity to update its due diligence review of the Company.

The closing price for the Company s Common Stock was $8.05 per share on June 3, 2013 and June 4, 2013. On June 4, 2013, the Special Committee held a telephonic meeting with all of its advisors to review the final terms of the Merger Agreement and to consider an oral report by Southwest Securities detailing the contents of and analysis underlying its draft fairness opinion with respect to the Proposed Transaction and the fairness of the offered price per share to the Company s minority and unaffiliated stockholders, which draft had previously been provided to the Special Committee. The contents of and analysis underlying Southwest Securities opinion are more fully described in *Opinion of Southwest Securities*. Southwest Securities subsequently delivered to the Special Committee a signed version of its fairness opinion. After receiving Southwest Securities report, the Special Committee performed a final review of the Merger Agreement and received from Wick Phillips a final reminder of the fiduciary obligations of the Special Committee. The Special Committee then discussed the reasons for its decision not to insist that the Merger Agreement contain a provision allowing the Company to actively solicit competing offers from other potential

bidders. In doing so, the Special Committee considered the fact that, although the Company had announced the Potential Transaction to the public in November 2012, the Company had not since that time received any indication of interest from other bidders besides Parent, and that the Proposal Letter made it clear that Parent was only interested in acquiring the shares it did not currently own, had no interest in a disposition of its own interest, and had no intention to vote in favor of any transaction other than the Proposed Transaction. Given those considerations, the Special Committee ultimately concluded that the inclusion in the Merger Agreement of a go-shop provision, permitting the Company to seek a superior bid, the consummation of which would in any event have required the approval of Parent, would have been futile. The Special Committee also determined that, in negotiating the Proposed Transaction, it had reached an appropriate balance between giving the Proposal Letter due consideration and vigorously negotiating the Proposed Transaction, while remaining wary of the risk of jeopardizing the only available transaction that would allow the minority and unaffiliated stockholders to receive a premium over the market value of their shares. The Special Committee also noted during its discussion that it had considered the possibility of liquidating the real estate owned by the Company in Rhode Island, but had concluded that such a transaction was unlikely to yield a value as favorable to the Company s minority and unaffiliated stockholders as the per share price offered by Parent. Following the Special Committee s deliberation regarding the reasons for the Proposed Transaction and the fairness of the Proposed Transaction, it reiterated its conclusion that its members were independent and that it had analyzed the Proposed Transaction in the best interest of the Company s minority and unaffiliated stockholders. Then, taking into account the relevant facts and circumstances, the Special Committee unanimously determined that the Proposed Transaction was substantively and procedurally fair to the Company s minority and unaffiliated stockholders, and to recommend that the Board approve the Proposed Transaction and the entry into and execution of the Merger Agreement (and any other document deemed necessary or advisable in connection with the Proposed Transaction) and to recommend that the Board recommend the same to the Company s stockholders.

On June 4, 2013, immediately following the meeting of the Special Committee, the Board (consisting of Mr. Crocco, Ms. Feldman and Mr. Powers, with Mr. Gumbiner not participating) held a telephonic meeting to consider the Proposed Transaction and the Merger Agreement. During such meeting, the Board (consisting of Mr. Crocco, Ms. Feldman and Mr. Powers, with Mr. Gumbiner not participating), upon the recommendation of the Special Committee, agreed with the Special Committee that the Proposed Transaction, as contemplated by the Merger Agreement, was advisable and in the best interests of the Company and its minority and unaffiliated stockholders, and was substantively and procedurally fair to the Company s minority and unaffiliated stockholders, and the Board approved the Merger Agreement and recommended the Merger Agreement to the Company s stockholders for their approval and adoption.

On June 4, 2013, following the Board meeting, the Merger Agreement in the form submitted to the Board (consisting of Mr. Crocco, Ms. Feldman and Mr. Powers, with Mr. Gumbiner not participating) was executed by the parties thereto.

On June 5, 2013, the Company issued a press release and filed with the SEC a Current Report on Form 8-K announcing that it had entered into the Merger Agreement.

On June 5, 2013, as required by the January 10, 2013 Notice Order, the Company provided notice to HEI Creditors Trust and the Bankruptcy Court of the filing on June 5, 2013 of the Company s Current Report on Form 8-K announcing its entry into the Merger Agreement.

On June 11, 2013, HEI Creditors Trust, FEI Shale L.P. and Hall Phoenix/Inwood Ltd. filed in the Bankruptcy Court an objection to the Company s June 5, 2013 notice of intent to proceed with the Proposed Transaction. The plaintiffs motion argues, among other things, that the Proposed Transaction would be in violation of the Bankruptcy Court s May 28, 2010 order and requests that the Bankruptcy Court enjoin the Company from consummating the Proposed

Transaction. This litigation was dismissed on November 22, 2013.

On July 1, 2013, the Special Committee held a telephonic meeting, at which representatives of Wick Phillips were also in attendance, to consider, among other items, a postponement by the parties to the Merger Agreement of the performance of their respective obligations to file with the SEC a proxy statement and Schedule 13E-3 prior to October 31, 2013. The Special Committee determined that the process of preparing the proxy solicitation and the Schedule 13E-3 would require significant use of Company resources, and that preparing such filings before October 31, 2013 would not be commercially reasonable in light of the then-pending litigation against the Company, which litigation has since been dismissed. Accordingly, the Special Committee was concerned about the timing of the filing of the Preliminary Proxy Statement. After deliberating and receiving advice from its counsel, the Special Committee concluded that the postponement of such filings was in the best interest of the Company and its stockholders.

On July 8, 2013, the Company issued a press release announcing the receipt of a letter from the Exchange dated July 5, 2013 informing the Company that it had resolved the continued listing deficiency referenced in the Exchange s letter dated April 11, 2013. On July 9, 2013, the Company filed a copy of such press release as an exhibit to a Current Report on Form 8-K.

On July 11, 2013, the parties to the Merger Agreement entered into an Amendment to Agreement and Plan of Merger stating that no party shall have any obligation to file a Schedule 13E-3, prior to October 31, 2013 (the Amendment).

On July 12, 2013, the Company filed with the SEC a Current Report on Form 8-K announcing that it had entered into the Amendment.

On August 23, 2013, a complaint was filed in the Court of Chancery of the State of Delaware captioned Sample v. Gumbiner et al., Civil Action No. 8833-VCN. The action named as defendants the directors of the Company, and also named as defendants Parent and Merger Sub. The Company was also named as a defendant or, in the alternative, as a nominal defendant. Among other things, the plaintiff alleged that all defendants other than Merger Sub breached fiduciary duties to the minority and unaffiliated stockholders in connection with the proposed Merger as a consequence of an allegedly unfair merger process and an allegedly unfair merger price. The complaint also alleged that Merger Sub aided and abetted these claimed breaches of fiduciary duty. The defendants denied, and continue to deny, any and all alleged wrongdoing. The complaint is described in more detail on page 47.

In December 2013 and January 2014, the parties to the Sample Litigation discussed and negotiated the terms on which the Sample Litigation might be settled, subject to Court approval. Ultimately, Parent offered to settle the Sample Litigation by adding an additional $3.00 per share to the purchase price to be paid in the Merger, with a condition that the Merger Agreement be amended to provide that Parent could terminate the Merger Agreement if such settlement were rejected by the Court or other court of appropriate jurisdiction.

On January 23, 2014, Potter Anderson provided a draft of a proposed settlement stipulation.

On January 24, 2014, Hunton & Williams provided a draft of a proposed amendment to the Merger Agreement.

On January 24, 2014, the Special Committee held a meeting in which Wick Phillips reported the proposed terms of the settlement. The Special Committee reserved making a decision on the settlement while the terms were being negotiated with the plaintiff in the Sample Litigation.

On January 28, 2014, the Special Committee met again to discuss the terms of the settlement proposed by Parent. The Special Committee was concerned about accepting Parent s request to have the right to terminate the Merger Agreement if the Settlement were rejected by the Court or other court having such authority. The Special Committee considered the following options: (i) rejecting the settlement and requiring the Merger to proceed at the $10.00 per share purchase price, (ii) accepting Parent s proposed terms, or (iii) negotiating for additional protection of the Merger while obtaining the additional $3.00 per share for the Company s minority and unaffiliated stockholders. Without approving the settlement, the Special Committee instructed Wick Phillips to request a change to the proposed amendment to the Merger Agreement that would preserve the Merger at the original purchase price of $10.00 per share if the settlement were rejected by the Court.

On January 28, 2014, Wick Phillips contacted Hunton & Williams to request a modification to the proposed amendment to the Merger Agreement that would require Parent to close the Merger at $10.00 per share if the settlement were ultimately rejected by the Court.

On January 29, 2014, Hunton & Williams provided a draft amendment to the Merger Agreement that provided for an additional $3.00 per share to the purchase price in the Merger, a condition to closing that the settlement to the Sample Litigation be finally approved by the Court, and a provision for further amendment to the Merger Agreement to reduce the purchase price back to the original purchase price of $10.00 per share if the settlement were rejected by the Court. The draft amendment further provided for the re-solicitation of stockholder approval of the Merger at the original

$10.00 purchase price if the settlement were rejected.

On February 3, 2014, the Special Committee met to discuss the proposed amendment to the Merger Agreement and a proposed settlement stipulation that would be filed with the Court. A draft of each had been previously provided to the Special Committee for review. The Special Committee discussed both the risks and benefits of entering into the proposed amendment. On one hand, an obvious and significant benefit included an additional $3.00 per share in purchase price (less a proportionate deduction for any incentive fee and attorney s fees awarded by the Court) for the Company s minority and unaffiliated stockholders. On the other hand, the completion of the Merger could be put at risk by the amount of time it would take to amend the Merger Agreement and solicit stockholder approval again at the original price of $10.00 per share in the event that the Merger Agreement had to be further amended following a rejection of the settlement agreement by the Court. In general, the longer a merger transaction goes without closing, the greater the risk of an event occurring that could permit a party to refuse to close. For example, a default

under the Brookwood credit facility is one of the events identified in the Merger Agreement that would allow Parent not to close the Merger. The risk of such event occurring is increased by the amount of time that elapses between the signing of the Merger Agreement and the closing of the Merger. The Special Committee believed that the benefit of obtaining the increased purchase price in an amendment to the Merger Agreement was greater than the risk of the transaction failing in the time required to address the events required if the settlement were rejected. The Special Committee approved the proposed amendment to the Merger Agreement and the proposed settlement stipulation. The Special Committee further authorized its counsel and the officers of the Company to complete negotiation of such amendment and stipulation, with such other terms, documents and notices as such counsel and officers deemed appropriate in furtherance of such approved terms, and to execute and file such documents with the appropriate courts, the SEC and other authorities.

On February 7, 2014, the Company entered into a proposed Stipulation of Settlement in the Sample Litigation, subject to approval by the Court, and entered into the Second Amendment formalizing the terms outlined above, which had been previously approved by the Special Committee. The Company filed a Form 8-K announcing the Second Amendment.

REASONS FOR THE MERGER; FAIRNESS OF THE MERGER; RECOMMENDATIONS OF THE SPECIAL

COMMITTEE AND THE BOARD

The Company s Board of Directors

As discussed in greater detail below, the Board believes that the Merger Agreement and the merger contemplated thereby (the Merger), upon the terms and conditions set forth in the Merger Agreement, are advisable and in the best interests of the Company and its minority and unaffiliated stockholders. The Board has determined that the Merger is substantively and procedurally fair to the Company s minority and unaffiliated stockholders. The recommendation of the Board is based, in part, upon the unanimous recommendation of the Special Committee.

The Board consists of four directors. Anthony J. Gumbiner, who is affiliated with Parent and will remain as an executive officer and director of the Company, did not participate in the deliberations concerning or voting on the Merger Agreement or the above recommendations. The three remaining, independent directors (Charles A. Crocco, Jr., Amy Feldman and Michael Powers, who also constitute the independent Special Committee), voted in favor of the above recommendations.

The Special Committee

In November 2012, in response to the Proposal Letter from Parent, the Board formed a Special Committee of independent non-employee directors to consider on behalf of the Board the Proposed Transaction. The Special Committee is comprised of Charles A. Crocco, Jr. (chairman), Amy H. Feldman and Michael R. Powers, three independent directors.

As discussed in greater detail below, the Special Committee believes that the Merger Agreement and the Merger, upon the terms set forth in the Merger Agreement, including without limitation, the price of $10.00 per share of Common Stock originally agreed to be paid to the Company s minority and unaffiliated stockholders, or if the Settlement is approved, $13.00 per share (less a proportionate deduction for any incentive fee and attorney s fees that may be awarded by the Court in connection with the Stipulation of Settlement, filed on February 7, 2014, relating to the Sample Litigation, as further described under the subheading entitled *Special Factors Litigation*), are advisable, in

the best interest of, and substantively and procedurally fair to, such minority and unaffiliated stockholders.

Recommendation of the Special Committee

The Special Committee, by unanimous vote at a meeting held on June 4, 2013:

- determined that it was advisable and in the best interests of the Company and the Company s minority and unaffiliated stockholders to consummate the Merger, enter into and execute the Merger Agreement and enter into and/or execute any agreement or document deemed necessary or advisable in connection with the Merger; and

- recommended that the Board approve the Merger, the Merger Agreement and any agreement or document deemed necessary or advisable in connection with the Merger, and that the Board recommend the same to all of the Company s stockholders for their approval.

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The Special Committee considered the following material factors in approving the Merger Agreement and making its determination and recommendation, which factors support the Special Committee s belief that the Merger Agreement and the Merger, upon the terms set forth in the Merger Agreement, are substantively and procedurally fair to the Company s minority and unaffiliated stockholders:

- the cash consideration to be paid to the Company s minority and unaffiliated stockholders upon consummation of the Merger;

- the current and historical market prices of the Common Stock, including, without limitation, the fact that the price of $10.00 per share originally agreed to be paid to the Company s minority and unaffiliated stockholders represented a premium of 78.3% over the $5.61 closing price of the Common Stock on November 8, 2012, the last trading day prior to the Company s public announcement of the Proposal Letter, and a premium of 24.2% over the $8.05 closing price of the Common Stock on June 4, 2013, the date of the Merger Agreement;

- the financial analyses and valuation factors reviewed by Southwest Securities with the Special Committee; these factors are set forth in more detail under the subheadings *Historical Stock Trading Analysis* , *Comparable Company Analysis* , *Selected Precedent Transactions Analysis* , and *Premiums Paid Analysis* , under *Opinion of Southwest Securities* ;

- the opinion of Southwest Securities delivered to the Special Committee on June 4, 2013 as to the fairness, as of June 4, 2013, from a financial point of view, of the original Merger Consideration of $10.00 in cash per share to be received by the holders of Common Stock (other than the shares held by Parent, Merger Sub and their respective affiliates) in the Merger, and based upon and subject to the procedures followed, assumptions made, qualifications and limitations on the review undertaken and other matters considered by Southwest Securities in preparing its opinion. A more detailed description of the opinion of Southwest Securities is set forth below under *Opinion of Southwest Securities* ;

- the conclusion by the Special Committee, after reviewing information relating to the Company and consulting its advisors, and, given the absence of an alternative bidder following the announcement of the Proposed Transaction in November 2012, that it was unlikely that either Parent or another bidder would be willing to pay more than $10.00 per share of Common Stock;

- the fact that Parent has stated it has no intention of selling its interest in the Company in the foreseeable future and that it would not vote in favor of any alternative sale, merger or similar transaction involving the Company, rendering futile the pursuit by the Special Committee of any such alternative sale, merger or similar transaction;

- the Special Committee s understanding of the Company s business, historical and current financial performance, competitive and operating environment, operations, management strength and future prospects,

including the Company s dependence on sales to the U.S. military and the decline in such sales in recent years;

the fact that the consideration to be paid to the Company s minority and unaffiliated stockholders would be all cash, which provides liquidity and certainty to the Company s minority and unaffiliated stockholders in light of the Company s historically low trading volume;

the high costs of operating as a public company;

the Special Committee s understanding of Parent s ability to obtain financing from internal sources to fully fund the payment of the original Merger Consideration and the related fees and expenses without further leveraging the Company or its assets;

the fact that the Special Committee considered the Company s liquidation value and determined that the value to the Company s minority and unaffiliated stockholders of such a liquidation was unlikely to equal or exceed the original Merger Consideration being offered by Parent;

the fact that the Merger Agreement includes a non-waivable condition requiring the approval by holders of at least a majority of the outstanding shares of Common Stock and by holders of a majority of the outstanding shares of Common Stock, excluding all shares of Common Stock owned by Parent, Merger Sub, Mr. Gumbiner or any of their respective affiliates or by any director, officer or employee of the Company or any of its subsidiaries;

the fact that the Special Committee had retained Southwest Securities as its financial advisor and Wick Phillips as its legal counsel, both of whom are unaffiliated with the Company, Parent or their respective affiliates, to assist and advise the Special Committee, solely with respect to the Company s minority and unaffiliated stockholders interests, in negotiations of the Merger Agreement with Parent;

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- the potential risks and costs to the Company and its minority and unaffiliated stockholders if the Merger does not close, including the Company s current financial situation; and

- the Company has not received any other firm offer from any other person during the two years prior to the execution of the Merger Agreement for the sale of the Company.

In considering the Proposed Transaction, the Special Committee also considered certain risks and potentially negative factors, including the following:

- the fact that the Merger Agreement does not permit the Company to solicit third-party bids or to enter into discussions or negotiations regarding, or to accept, approve or recommend, any unsolicited third-party bids except subject to specific terms and conditions;

- the fact that, upon consummation of the Merger, the Company s minority and unaffiliated stockholders will cease to be stockholders of the Company and thus will be unable to participate in any future appreciation in the value of the Company s stock;

- the fact that the Company s Common Stock, prior to the Proposed Transaction, has exceeded the $10.00 per share Merger Consideration originally offered by Parent on some occasions since the execution of the Merger Agreement;

- the fact that one of the four analyses of Southwest Securities contained per share prices that exceeded the Merger Consideration originally offered by Parent; and

- the fact that the current market price of the Common Stock, $12.35 on March 3, 2014, may not reflect the value of the Common Stock, given the lack of trading volume in the Common Stock, the position held by the principal stockholder and the paucity of coverage by outside analysts.

The Special Committee did not establish, and did not specifically consider, a pre-Merger public company going concern value of Common Stock for the purposes of determining the per share Merger Consideration or the fairness of the per share Merger Consideration to the minority and unaffiliated stockholders of the Company. However, to the extent the pre-Merger going concern value was reflected in the pre-announcement per share price of Common Stock, the original per share Merger Consideration of $10.00 represented a premium to the going concern value of the Company. In addition, the Special Committee did not consider net book value of Common Stock because it believes that net book value, which is an accounting concept, does not reflect, or have any meaningful impact on, either the public trading prices of Common Stock or the Company s value as a going concern. The Special Committee did not consider liquidation value in determining the fairness of the Merger to the minority and unaffiliated stockholders of the Company because of its belief that liquidation sales generally result in proceeds substantially less than sales of a going concern, because of the impracticability of determining a liquidation value given the significant execution risk involved in any breakup, because it considered the Company to be a viable, going concern and because the Company will continue to operate its business following the Merger.

The Special Committee determined it was unnecessary to establish or specifically consider the going concern value of the Company (or the value of its business as operated rather than the value of its assets sold in a liquidation) in light of the other information considered by the Special Committee in assessing the initial $10.00 per share offer price, as described in this proxy statement. In addition, Southwest Securities reported to the Special Committee that certain approaches in its analysis resulted in estimates of value that were either negative or approximately zero. Southwest Securities noted that stock prices cannot be negative and considered any negative results to imply speculative or essentially no going concern value. One indication of going concern value is the company s pre-announcement per share price of its common stock. Additionally, multiplying adjusted EBITDA (earnings before reduction for interest, taxes, depreciation and amortization, and after removing certain extraordinary income and expense items) of a company by a certain multiple is a typical manner of determining the going concern value of a company on an enterprise value basis. Another manner of going concern valuation is to calculate a company s expected cash flow over a long period of time and apply a discount to provide for the time value of that projected cash flow. At the time Southwest Securities presented its March 28, 2013 report to the Special Committee, the Company was expected to have a $900,000 negative EBITDA in 2013. Also, the Company was unable to determine a projected cash flow beyond then end of 2013 due to dependence of its only operating business, Brookwood, on military purchasing.

Instead of specifically determining the Company s single going concern value, the Special Committee examined the deemed enterprise value of the Company that was implied by the Parent s $10.00 per share bid as compared to the deemed enterprise value reflected in the purchase price of other comparable public companies and similar transactions. Enterprise value of a company is its public market value, plus the amount of its indebtedness, minus the amount of its cash. The Southwest Securities report of March 28, 2013 indicated that Parent was implicitly treating the Company as having a $29.2 million enterprise value by offering $10.00 per share, which was 24.6 times (a multiple of 24.6) the Company s 2012 adjusted EBITDA. Furthermore, at the time of such report, the Company was expected to have $900,000 negative EBITDA in 2013. Such report also contained an analysis of 12 transactions similar to the Proposed Transaction. The purchase prices in these example transactions implied an average enterprise valuation of these companies of 7.0 times their EBITDA, as compared to the 24.6 times EBITDA valuation

reflected in the price offered by Parent. For these reasons, and based on the other information and circumstances described in this proxy statement, the Special Committee did not believe that it needed to determine a single actual going concern value of the Company to conclude that the $10.00 per share purchase price was fair to the Company s minority and unaffiliated stockholders.

Because the Special Committee concluded that the purchase price of $10.00 per share was fair to the Company s minority and unaffiliated stockholders, it concluded that an increase in purchase price to $13.00 per share, without interest, less a proportionate deduction for any incentive fee and attorney s fees that may be awarded by the Court in connection with the Stipulation of Settlement, filed on February 7, 2014, relating to the Sample Litigation, would make the Proposed Transaction no less fair to the Company s minority and unaffiliated stockholders. The Sample Litigation is more fully described under the subheading entitled *Special Factors Litigation.*

The foregoing discussion is not intended to be exhaustive, but summarizes certain factors considered by the Special Committee in making its determination and recommendation to the Board. In view of the wide variety of factors considered by the Special Committee and the complexity of these matters, the Special Committee did not find it practicable to quantify or otherwise assign relative weights to the foregoing factors and instead made its determination based on all factors and considerations, taken as a whole. In addition, each of the members of the Special Committee may have assigned different weights to various factors. On balance, the Special Committee determined that the positive factors discussed above outweighed any negative factors.

Although the market trading price of the Company s Common Stock at some points in the twelve months prior to the execution of the Merger Agreement had exceeded the proposed $10.00 per share purchase price for the Proposed Transaction, the Special Committee did not consider such higher price as significant to determining the fairness of the price in the Proposed Transaction. The Special Committee recognized from the March 28, 2013 report of Southwest Securities that the proposed $10.00 per share purchase price was at a 15.7% premium over the 120 day trading average for such Common Stock immediately prior to the announcement of the proposal by Parent of the proposed $10.00 per share purchase price. Such report also indicated that the price of such Common Stock had not traded above $10.00 since the third quarter of 2012 and the trading price demonstrated steady trend of decline beginning in March 2010. Considering this history, the other information presented by Southwest Securities, and the Special Committee s knowledge about the performance of the Company, the Special Committee believed that the prior trades of the Company s Common Stock in excess of such $10.00 per share price did not reflect the value of such Common Stock at the time the Special Committee approved the Proposed Transaction. The market trading price of the Company s Common Stock has not exceeded $13.00 per share since February 2012.

Although the Premiums Paid Analysis of Southwest Securities described on page 32 indicated some ranges of values for the Common Stock that exceeded $10.00 per share, the Special Committee did not view such excess as a basis for requiring a higher per share Merger Consideration. Such test was used to demonstrate the price of $10.00 per share fell within a range that was fair to the minority and unaffiliated stockholders and not as a basis for supporting a higher value. The sampling of companies used in such analysis was based only on the size of such companies and not on their business, historical and current financial performance, competitive and operating environment, and, therefore, the Board and the Special Committee did not believe that this analysis was itself determinative of the value of the Company.

The Special Committee believes that the process it followed in making its determination and recommendation with respect to the Merger Agreement was fair and proper because, among other things:

the Special Committee consists solely of independent directors, as no such director has a material financial or other interest in the Merger, nor does any such director have any other significant interest or relationship that would influence such director s decision;

the Special Committee retained and was advised by experienced and independent legal counsel;

the Special Committee retained and was advised by an experienced and independent financial advisor, which rendered an opinion as to the fairness, from a financial point of view, of the original Merger Consideration of $10.00 in cash per share to be received by the Company s minority and unaffiliated stockholders in the Merger;

the Special Committee, with the assistance of its independent advisors, diligently negotiated the terms of the Merger Agreement with Parent; and

the Special Committee acted diligently in discharging its responsibilities, meeting on eleven separate occasions prior to execution of the Merger Agreement, to review all information relevant to the Proposed Transaction and carefully consider matters related to its mandate.

Recommendation of the Board

At a meeting on June 4, 2013, following the recommendation of the Special Committee, the Board (consisting of Mr. Crocco, Ms. Feldman and Mr. Powers, with Mr. Gumbiner not participating):

- approved the Merger Agreement; and

- recommended the Merger Agreement to the Company s stockholders for their approval and adoption.

In voting on the above items, the Board reviewed a significant amount of information and considered each of the factors recited above with respect to the Special Committee s deliberations, as well as the fact that the Merger Agreement was approved and recommended by the Special Committee after a full and deliberate process. In view of the wide variety of factors considered by the Board and the complexity of these matters, the Board did not find it practicable to quantify or otherwise assign relative weights to the factors it considered in making its decision. In addition, individual members of the Board may have assigned different weights to various factors. The Board members voting on the Merger Agreement unanimously approved the Merger Agreement and the Merger, and found the Proposed Transaction to be substantively and procedurally fair to the minority and unaffiliated stockholders, based upon the totality of the information presented to and considered by them. The Board expressly adopted the analysis and recommendations of the Special Committee and Southwest Securities with respect to the Proposed Transaction.

The Board (consisting of Mr. Crocco, Ms. Feldman and Mr. Powers, without Mr. Gumbiner s participation) unanimously recommends that you vote FOR the proposal to adopt the Merger Agreement and FOR the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement.

OPINION OF SOUTHWEST SECURITIES

Southwest Securities was retained to act as financial advisor to the Special Committee in connection with the transactions described in this Proxy Statement. In connection with this engagement, the Special Committee requested Southwest Securities to evaluate the fairness, from a financial point of view, to the holders of Common Stock (other than shares of Common Stock owned by Parent, HFL Merger Corporation, a Delaware corporation (Merger Sub), and their respective affiliates and other than shares as to which any appraisal rights are properly exercised) of the Merger Consideration payable per share of Common Stock pursuant to the Merger Agreement. On March 28, 2013, at a meeting of the Special Committee, Southwest Securities expressed orally to the Special Committee that it was prepared to opine that the Merger Consideration originally offered by Parent was fair from a financial point of view. On June 4, 2013, Southwest Securities provided its oral report to the Special Committee, which confirmed, with no substantial changes, its March 28, 2013 oral statement and was then confirmed by delivery of its written opinion dated as of June 4, 2013, to the effect that, as of that date and based on and subject to the matters described in its opinion, the original Merger Consideration payable pursuant to the Merger Agreement was fair, from a financial point of view, to the holders of Common Stock (other than shares of Common Stock owned by Parent, Merger Sub and their respective affiliates and other than shares as to which any appraisal rights are properly exercised).

The full text of Southwest Securities written opinion, dated as of June 4, 2013, which describes the assumptions made, procedures followed, matters considered and limitations on the review undertaken, is attached to this Proxy Statement as Annex B. You are urged to read the opinion carefully and in its entirety. Southwest Securities opinion was directed to the Special Committee in connection with its evaluation of the original

Merger Consideration from a financial point of view and does not address any other aspects or implications of the Merger. Southwest Securities opinion is not intended to be and does not constitute a recommendation to any stockholder as to any action that should be taken with respect to the proposed Merger. Southwest Securities opinion does not address the relative merits of the Merger as compared to any alternative business strategies that might exist for the Company or the underlying business decision of the Company to effect the Merger. The following is a summary of Southwest Securities opinion and the methodology that Southwest Securities used to render its opinion.

Southwest Securities has consented to the use of its opinion in this proxy statement. Pursuant to the engagement letter between Southwest Securities and the Company, Southwest Securities opinion was furnished solely for the use and benefit of the Special Committee (solely in its capacity as such) in connection with its consideration of the Merger and was not intended to, and did not, confer any rights or remedies upon any other person. Any defenses by Southwest Securities with respect to a claim by any such person, including a shareholder of the Company, would be subject to resolution under applicable law and would need to be resolved by a court of competent jurisdiction. In the view of the SEC, the availability

of any such defenses under applicable law will have no effect on the rights and responsibilities of the Special Committee or board of directors of the Company under applicable Delaware law, or on the rights and responsibilities of the Special Committee or board of directors of the Company or Southwest Securities under applicable U.S. federal securities laws. The Opinion was not intended to be used, and may not be used, for any other purpose, without the express, prior written consent of Southwest Securities. This opinion should not be construed as creating any fiduciary duty on the part of Southwest Securities to any party. This opinion is not intended to be, and does not constitute, a recommendation to the Special Committee, any security holder or any other person or entity as to how to act or vote with respect to any matter relating to the Merger.

The opinion was necessarily based on financial, economic, market and other conditions as in effect on, and information available to Southwest Securities as of, the date of the opinion. Southwest Securities did not undertake to update, reaffirm, revise or withdraw its opinion or otherwise comment upon any events occurring or coming to its attention after the date of the opinion and does not have any obligation to update, revise or reaffirm this opinion.

In the course of performing its review and analysis for rendering this opinion, Southwest Securities, among other things:

(i) reviewed a draft of the Merger Agreement dated June 4, 2013;

(ii) reviewed and analyzed certain publicly available financial and other data with respect to the Company and certain other relevant historical operating data relating to the Company made available to Southwest Securities from published sources and from the internal records of the Company;

(iii) conducted discussions with members of the senior management of the Company with respect to the business, operations, prospects and financial condition and outlook of the Company;

(iv) visited certain facilities and the business offices of the Company;

(v) reviewed current and historical market prices and trading activity of the Common Stock of the Company;

(vi) compared certain financial information for the Company with similar information for certain other companies, the securities of which are publicly traded;

(vii) reviewed the financial terms, to the extent publicly available, of selected precedent transactions which Southwest Securities deemed generally comparable to the Company and the Merger; and

(viii) conducted such other financial studies, analyses and investigations and considered such other information as Southwest Securities deemed appropriate.

In rendering its opinion, Southwest Securities relied upon and assumed, without independent verification, the accuracy and completeness of all data, material and other information furnished or otherwise made available to it, discussed with it or reviewed by it, or that was publicly available, and did not assume any responsibility for or with respect to such data, material, or other information. Southwest Securities was not requested to, and did not perform an independent evaluation, physical inspection or appraisal of any of the assets or liabilities (contingent or otherwise) of the Company, and was not furnished with any such valuations or appraisals. Southwest Securities did not undertake any independent analysis of any potential or actual litigation, regulatory action, possible unasserted claims or other contingent liabilities, to which the Company is or may be a party or is or may be subject, or of any governmental investigation of any possible unasserted claims or other contingent liabilities to which the Company is or may be a party or is or may be subject. Southwest Securities was not provided any financial projections or estimates of future performance by management of the Company beyond the year ended December 31, 2013, and was advised by management that none exist or could be meaningfully prepared, due to the uncertainty created by the Company s significant reliance on one source of revenue.

In its analysis of the Company, Southwest Securities reviewed projections for the Company on a consolidated basis covering the year ending 2013 that were periodically updated during the term of its due diligence. The report Southwest Securities presented to the Special Committee on March 28, 2013, attached as Exhibit (c)(2) to Amendment No. 1 to Schedule 13E-3 filed in conjunction herewith, contained projections that reflected a loss for the Company in 2013. Brookwood, the Company s only operating subsidiary, updates its projections periodically for the Company s board of directors. Brookwood made such an update on May 7, 2013, to show a slight increase in projected income for 2013, which projections are described herein on page 41 without consolidation with the projected cash flows of the Company as its parent. Such revised projections were also reviewed by Southwest Securities prior to the delivery of its opinion.

In relying on the financial analyses and forecasts provided, Southwest Securities assumed that they were reasonably prepared on a basis reflecting the best currently available estimates and judgments of the management of the Company as to the future financial performance of the Company. Southwest Securities relied on the assurances of management of the Company that they were

unaware of any facts that would make such business prospects and financial outlook incomplete or misleading. Southwest Securities also assumed that the Merger Agreement conformed in all material respects to the latest available drafts it reviewed; that the Merger will be consummated in a timely manner and in accordance with the terms set forth in the Merger Agreement without waiver, modification, or amendment of any material term, condition or agreement; and that all governmental, regulatory, and other consents and approvals necessary for the consummation of the Merger will be obtained without any material adverse effect on the Company or on the contemplated benefits of the Merger. Southwest Securities relied upon and assumed, without independent verification, that there had been no change in the business, assets, liabilities, financial condition, results of operations, cash flows or prospects of the Company since the dates of the most recent financial statements and other information, financial or otherwise, provided to it, in each case that would be material to the analysis for its opinion.

The opinion addressed solely the fairness of the financial terms of the original Merger Consideration and did not address any other terms or agreement relating to the Merger or any other matters pertaining to the Company. Southwest Securities was not authorized to, and did not:

(i) solicit other potential parties with respect to the Merger or any alternatives to the Merger or any related transaction with the Company;

(ii) negotiate the terms of the Merger or any related transaction; or

(iii) advise the Special Committee or any other party or entity with respect to alternatives to the Merger or any related transaction.

Southwest Securities did not consider, and expressed no opinion with respect to, (i) the price at which shares of the Common Stock may trade following announcement or consummation of the Merger; (ii) the estimated value of the Company s Rhode Island real estate; and (iii) the value of any potential claims the Company may have against Mr. Gumbiner and other employees and advisors of the Company resulting from the entry of judgments by the Bankruptcy Court against the Company totaling approximately $24 million.

Southwest Securities acted as financial advisor to the Special Committee in connection with the Merger and received a fee for its services in the aggregate amount of $150,000. A portion of the fee was paid at the commencement of the engagement, and the remainder was paid in accordance with the terms of the engagement letter, including $75,000 which was paid upon the delivery of an oral summary by Southwest Securities of its fairness opinion. No portion of the fee was contingent upon consummation of the Merger or the conclusions which Southwest Securities reached in its opinion. In addition, the Company agreed to reimburse Southwest Securities for its expenses and indemnify Southwest Securities for certain liabilities that may arise out of the engagement. In the ordinary course of business, Southwest Securities may, for its own account and the accounts of its customers, actively trade the securities of the Company and, accordingly, may hold a long or short position in such securities. During the last two years, Southwest Securities has not provided investment banking or any other services to the Company for which it received compensation from the Company.

Southwest Securities opinion does not constitute legal, regulatory, accounting, insurance, tax or other similar professional advice, and does not address or express an opinion regarding:

(i) the underlying business decision of the Special Committee of the Company or the Company s security holders to proceed with or effect the Merger;

(ii) the fairness of any portion or aspect of the Merger not expressly addressed in this opinion;

(iii) the fairness of any portion or aspect of the Merger to the creditors or other constituencies of the Company other than those set forth in the opinion;

(iv) the relative merits of the Merger as compared to any alternative business strategies that might exist for the Company or the effect of any other transaction in which the Company might engage;

(v) the tax or legal consequences of the Merger to either the Company or its security holders;

(vi) how any security holder should act or vote, as the case may be, with respect to the Merger;

(vii) the solvency, creditworthiness or fair value of the Company or any other participant in the Merger under any applicable laws relating to bankruptcy, insolvency or similar matters; or

(viii) the fairness of the amount or nature of the compensation to any of the Company s officers, directors, or employees relative to the compensation to the other stockholders of the Company.

Summary of Southwest Securities Analyses

In preparing its opinion, Southwest Securities performed a variety of financial and comparative analyses, including those described below. This summary is not a complete description of Southwest Securities opinion of the financial and comparative analyses performed and factors considered in connection with its opinion. The preparation of a fairness opinion is a complex process involving various determinations as to the most appropriate and relevant quantitative and qualitative methods of financial analysis and the applications of those methods to the particular circumstances and, therefore, is not necessarily susceptible to partial analysis or summary description. Southwest Securities believes that its analyses must be considered as a whole. Considering any portion of Southwest Securities analyses or the factors considered by Southwest Securities, without considering all analyses and factors, could create a misleading or incomplete view of the process underlying the conclusion expressed in Southwest Securities opinion. In addition, Southwest Securities did not attribute any particular weight to any analysis, but instead made qualitative judgments about the significance and relevance of each such analysis so that the range of valuations resulting from any particular analysis described below should not be taken to be Southwest Securities view of the Company s actual value. Accordingly, the conclusions reached by Southwest Securities are based on all analyses and factors taken as a whole and also on the application of Southwest Securities own experience and judgment.

In performing the analyses, Southwest Securities took into consideration factors related to industry performance, general business, economic and regulatory conditions and other matters, many of which are beyond the Company s and Southwest Securities control. The analyses performed by Southwest Securities are not necessarily indicative of actual values or actual future results, which may be significantly more or less favorable than suggested by such analyses. In addition, analyses relating to the per share value of the Common Stock do not purport to be appraisals or to reflect the prices at which the Common Stock may actually be sold. The analyses performed were prepared solely as part of Southwest Securities analysis of the fairness, from a financial point of view, of the proposed Merger Consideration originally offered by Parent to be received by holders of Common Stock pursuant to the Merger Agreement, and were provided to the Special Committee in connection with the delivery of Southwest Securities opinion. As described in the foregoing analysis, certain approaches resulted in estimates of value that were either negative or approximately zero and therefore, Southwest Securities noted that stock prices cannot be negative and considers any negative results to imply speculative or essentially no value.

The following is a summary of the material financial and comparative analyses reviewed by Southwest Securities with the Special Committee in connection with Southwest Securities delivery of its opinion. **The financial analyses summarized below include information presented in tabular format. In order to fully understand Southwest Securities financial analyses, the tables must be read together with the text of each summary. The tables alone do not constitute a complete description of the financial analyses. Considering the data described below without considering the full narrative description of the financial analyses, including the methodologies and assumptions underlying the analyses, could create a misleading or incomplete view of Southwest Securities financial analyses**.

Historical Stock Trading Analysis. Southwest Securities analyzed the $10.00 cash per share of Common Stock to be paid to the holders of shares of Common Stock pursuant to the Merger Agreement in relation to the closing price of shares of Common Stock on November 8, 2012, the closing prices of shares of Common Stock for the 52-week period ended March 26, 2013, and the Common Stock s 30-trading day average, 60-trading day average, 90-trading day average and 120-trading day average closing prices prior to November 8, 2012 the last trading day prior to the date on which the offer was announced. This analysis was undertaken to assist the Special Committee in understanding the Merger Consideration originally offered by Parent compared to recent historical market prices of the Common Stock.

This analysis indicated that the $10.00 cash per share of Common Stock to be paid to the holders of the Company s shares of Common Stock pursuant to the Merger Agreement represented:

- a premium of 78.3% based on the closing stock price of $5.61 per share of Common Stock on November 8, 2012;
- a premium of 49.8% based on the average closing price of $6.68 per share of Common Stock during the 30-day period ended November 8, 2012;
- a premium of 27.5% based on the average closing price of $7.85 per share of Common Stock during the 60-day period ended November 8, 2012;
- a premium of 17.4% based on the average closing price of $8.52 per share of Common Stock during the 90-day period ended November 8, 2012; and
- a premium of 15.7% based on the average closing price of $8.64 per share of Common Stock during the 120-day period ended November 8, 2012.

Southwest Securities also presented a stock price histogram for the 12-month period ended March 26, 2013, illustrating that 87.9% of the trading activity in the Common Stock occurred at prices of $10.00 per share or below.

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Comparable Company Analysis. Southwest Securities reviewed and analyzed certain financial information, public market valuation multiples and market trading data relating to 12 selected comparable publicly-traded textile and specialty apparel manufacturers. Southwest Securities then compared such information to the corresponding information for the Company. No company used in this analysis is identical to the Company. The selected group of comparable companies was as follows:

Cintas Corporation

ComWest Enterprise Corp.

Culp Inc.

Delta Apparel Inc.

Formosa Taffeta Co., Ltd.

G&K Services Inc.

Kurabo Industries Ltd.

Lakeland Industries Inc.

S. Kumars Nationwide Ltd.

Superior Uniform Group Inc.

Unifi Inc.

UniFirst Corp.

Although none of the selected textile and specialty apparel manufacturers is directly comparable to the Company, the companies included were chosen because they are publicly-traded companies in the textile and specialty apparel manufacturers industries with operations and/or business drivers that for the purposes of this analysis may be considered similar to the operations and business drivers of the Company. Criteria for selecting comparable companies included similar lines of business, markets of operation, customers and other business and financial considerations (*e.g.*, business drivers, business risk and financial performance).

In the analysis, Southwest Securities reviewed, among other things, enterprise values of the selected publicly-traded companies, calculated as equity values based on closing stock prices as of March 26, 2013, plus debt, minority interest and preferred stock, less cash, as a multiple of actual and estimated EBITDA for the calendar years 2012 and 2013 (unless otherwise noted). Southwest Securities utilized EBITDA because the metric is commonly used when evaluating companies in the textile and specialty apparel manufacturers industries. The estimated financial data of the selected publicly-traded companies were based on publicly available research analysts estimates, public filings and other publicly available information. Based on the comparable company metrics analyzed and its professional judgment, Southwest Securities selected a multiple range of 3.3x to 10.7x for calendar year 2012 EBITDA and 3.1x to 8.8x for calendar year 2013 estimated EBITDA. Southwest Securities then applied the calculated multiples for the comparable companies to the Company s EBITDA. Financial data of the Company were based on actual results for calendar year 2012 and based on management s forecast estimate for the calendar year 2013 (adjusted to add-back to EBITDA the costs associated with the Hallwood Energy and Nextec litigation which were deemed to be unusual in nature). The analysis yielded only negative amounts and therefore, Southwest Securities noted that stock prices cannot be negative and considers any negative results to imply speculative or essentially no value.

Southwest Securities selected the companies reviewed in this analysis because, among other things, such companies operate similar businesses to the Company. However, no selected company is identical to the Company. Accordingly, Southwest Securities believed that purely quantitative analyses are not, in isolation, determinative in the context of the Merger and that qualitative judgments concerning differences between the business, financial and operating characteristics and prospects of the Company and the selected companies that could affect the public trading values of each also are relevant.

Selected Precedent Transactions Analysis. Using publicly available information, Southwest Securities examined financial information relating to the following six majority stake acquisition transactions of various transaction sizes, announced over the last seven years involving textile and specialty apparel manufacturers. These transactions were selected generally because they involve target companies with similar industry focus and business drivers to the Company. The closing dates and transactions were as follows:

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Acquirer	Target	Date Closed
Qualium Investissement	Kermel S.A.	07/27/12
Lear Corp.	Guilford Performance Textiles, Inc.	05/31/12
Bangladesh Export Import Company Ltd.	Bextex Limited	07/31/11
Gilde Buy Out Partners	Gamma Holding NV	02/22/11
The Blackstone Group	Polymer Group, Inc.	01/28/11
International Textile Group, Inc.	Global Safety Textiles GmbH	04/01/07

Southwest Securities reviewed transaction values, calculated as the enterprise value implied for the target company based on the consideration payable in the selected transaction, as a multiple of the target company s latest 12 months revenues and EBITDA. Financial data of the selected transactions were based on publicly available information at the time of announcement of the transaction. This analysis indicated the following multiple ranges:

Enterprise Value/	
LTM	EBITDA
Low	5.9x
Mean	6.6x
Median	6.4x
High	8.2x

Based on the selected precedent transaction metrics analyzed and its professional judgment, Southwest Securities selected a multiple range of 5.9x to 8.2x for EBITDA. Southwest Securities then applied the calculated multiples for the precedent transactions to the Company s EBITDA. Financial data of the Company were based on actual results for calendar year 2012 and based on management s March 28, 2013 forecast estimate for the calendar year 2013 (adjusted to add-back to EBITDA the costs associated with the Hallwood Energy and Nextec litigation which were deemed to be unusual in nature). The analysis yielded only negative amounts and therefore, Southwest Securities noted that stock prices cannot be negative and considers any negative results to imply speculative or essentially no value.

No company, business or transaction used in this analysis is identical to the Company or the Merger. In addition, an evaluation of the results of this analysis is not entirely mathematical. This analysis involves considerations and judgments concerning differences in financial and operating characteristics and other factors that could affect the acquisition or other values of the companies, business segments or transactions to which the Company and the Merger were compared.

Discounted Cash Flow Analysis. Management did not prepare or make available to Southwest Securities financial forecasts beyond 2013 and therefore, a discounted cash flow analysis could not be performed.

Premiums Paid Analysis. Using publicly available information, Southwest Securities analyzed the premiums offered in (i) 41 selected publicly-traded minority buy-in merger and acquisition transactions of all sizes since January 1, 2008 and (ii) 20 selected publicly-traded minority buy-in merger and acquisition transactions for less than $50 million since January 1, 2008. For each of these transactions, Southwest Securities calculated the premium represented by the offer price over the target company s closing share price one day, one week, 30-days and 60-days prior to the transaction s announcement. This analysis indicated the following premiums for those time periods prior to announcement:

Publicly-Traded Minority Buy-In M&A Transactions All Sizes

	Hallwood Group Historical (1)	$10.00	Buy-In Premium Low (2)	Mean (3)	Median	High (4)	Implied Hallwood Group Price Per Share Mean (3)	Median
1-Day Spot Premium	$ 5.61	78.3%	9.9%	30.8%	28.3%	62.5%	$ 7.34	$ 7.20
1-Week Spot Premium	6.15	62.6%	8.0%	31.9%	28.6%	63.0%	8.11	7.91
30-Day Spot Premium	8.00	25.0%	10.3%	33.4%	36.4%	70.9%	10.67	10.91
60-Day Spot Premium	9.74	2.7%	2.1%	27.9%	30.3%	60.5%	12.46	12.69

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Publicly-Traded Minority Buy-In M&A Transactions Less than $50 million

	Hallwood Group		Buy-In Premium				Implied Hallwood Group Price Per Share	
	Historical (1)	$10.00	Low (2)	Mean (3)	Median	High (4)	Mean (3)	Median
1-Day Spot Premium	$ 5.61	78.3%	0.8%	22.5%	17.6%	74.0%	$ 6.87	$ 6.59
1-Week Spot Premium	6.15	62.6%	(0.2%)	20.5%	14.5%	67.9%	7.41	7.04
30-Day Spot Premium	8.00	25.0%	0.1%	28.0%	22.8%	72.7%	10.24	9.82
60-Day Spot Premium	9.74	2.7%	(7.3%)	25.3%	11.9%	91.7%	12.20	10.90

Source: Capital IQ

(1) Closing price on trading days prior to the date on which the offer was announced.
(2) First quartile.
(3) Based on interquartile data set.
(4) Third quartile.

Based on the foregoing, this analysis indicated the following implied equity value reference ranges based on median minority buy-in premiums for the Company, as compared to the Merger Consideration of $10.00 originally offered by Parent:

Minority Buy-in M&A Transactions All Sizes

Implied Per Share Equity

Value Reference Range

$7.20 $12.69

Minority Buy-in M&A Transactions Less Than $50 million

Implied Per Share Equity

Value Reference Range

$6.59 $10.90

The above information was presented to the Special Committee on March 28, 2013.

General. The Merger Consideration was determined through negotiations between the Company and Parent, and was approved by the Special Committee. Southwest Securities opinion was one of many factors taken into consideration by the Special Committee in making its determination to approve the Merger and should not be considered determinative of the views of the Special Committee, the Board or management with respect to the Merger or the Merger Consideration. Southwest Securities was selected by the Special Committee based on Southwest Securities qualifications, expertise and reputation. Southwest Securities is a nationally recognized investment banking and advisory firm. Southwest Securities, as part of its investment banking business, is regularly engaged in the valuation of businesses and securities in connection with mergers and acquisitions, negotiated underwritings, competitive

biddings, secondary distributions of listed and unlisted securities, private placements, financial restructurings and other financial services. In the ordinary course of business, Southwest Securities may, for its own account and the accounts of its customers, actively trade the securities of the Company and, accordingly, may hold a long or short position in such securities. During the last two years, Southwest Securities has not provided investment banking services to the Company, Parent, or their respective affiliates for which it received compensation.

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THE PARENT FILING PERSONS PURPOSES AND REASONS FOR THE MERGER

Each of the Parent Filing Persons (as defined below) may be deemed to be affiliates of the Company and, therefore, under the SEC rules governing going-private transactions, are required to express their purpose and reasons for the Merger. The Parent Filing Persons are making the statements included in this section solely for the purpose of complying with the requirements of Rule 13e-3 and related rules under the Exchange Act.

Mr. Gumbiner, his wife Marie Magdeleine Gumbiner and Gert Lessing are the directors of Parent. Messrs. Gumbiner and Lessing are the executive directors of Parent and the sole directors and executive officers of Merger Sub. Mr. Gumbiner and Mrs. Gumbiner are the directors and executive officers of Hallwood Family Investments Ltd. (HFI). Mrs. Gumbiner, in her role as a director of Parent, and Mr. Lessing, in his roles as a director of Parent and a director and officer of Merger Sub, each delegated the determination of issues related to the Merger, and the negotiation of the Merger Agreement to Mr. Gumbiner. Parent, Merger Sub, HFI, Mr. Gumbiner, and Mrs. Gumbiner are referred to collectively in this discussion as the Parent Filing Persons. For the Parent Filing Persons, the purpose of the Merger is to enable Parent to acquire sole ownership of the Company, in a transaction in which the minority and unaffiliated stockholders of the Company will be cashed out for the Merger Consideration, so Parent will bear the rewards and risks of the ownership of the Company after shares of Common Stock cease to be publicly held and traded. Parent attempted to negotiate the terms of a transaction that would be most favorable to itself, and not to stockholders of the Company and, accordingly, did not negotiate the Merger Agreement with the goal of obtaining terms that were fair to such stockholders. Parent decided to pursue the Merger because it believes that the Company can be operated more effectively as a privately-owned company because it will not be subject to the obligations, constraints and costs associated with having publicly traded securities. In addition, the success of the Company depends primarily on the success of its Brookwood subsidiary. Brookwood s success in turn depends in large part on sales to the customers from whom it derives its military business, which have been increasingly volatile and difficult to predict. The Parent Filing Persons believe that a business subject to this type of volatility is more appropriately operated as a private company because the public markets tend to focus on consistency and growth. For these reasons, the Parent Filing Persons believe that private ownership is in the best interests of the business and the organization and that the Merger is in the best interests of the Company s stockholders.

THE PARENT FILING PERSONS   POSITION AS TO THE FAIRNESS OF THE MERGER

Under the SEC rules governing   going-private   transactions, each of the Parent Filing Persons may be deemed to be affiliates of the Company and, therefore, required to express their beliefs as to the substantive and procedural fairness of the Merger to the minority and unaffiliated stockholders of the Company. The Parent Filing Persons are making the statements included in this section solely for the purpose of complying with the requirements of Rule 13e-3 and related rules under the Exchange Act. The Parent Filing Persons   views as to the fairness of the Merger should not be construed as a recommendation to any stockholder as to how that stockholder should vote on the proposal to adopt the Merger Agreement.

Given Mr. Gumbiner s participation in the transactions contemplated by the Merger Agreement, Mr. Gumbiner did not vote or otherwise participate in the deliberations of the Special Committee or the Board when the Special Committee voted to recommend, or the Board voted to approve, the adoption of the Merger Agreement and did not receive advice from the Company s or the Special Committee s legal counsel or Financial Advisor.

As described in the   *Special Factors Interests of the Company s Directors and Executive Officers in the Merger* section beginning on page 43, the Parent Filing Persons have interests in the Merger different from those of the minority and unaffiliated stockholders of the Company by virtue of Parent s and Mr. Gumbiner s holdings of Common Stock and Mr. Gumbiner s expectation of a continuing leadership role in the Surviving Corporation. None of the Parent Filing Persons participated in the deliberations of the Special Committee or the Board regarding, or received advice from the Special Committee s legal or financial advisors as to, the fairness of the Merger. Nevertheless, the Parent Filing Persons took into account the fact that the Board determined, by the unanimous vote of all members of the Board (with Mr. Gumbiner not participating), based on the unanimous recommendation of the Special Committee, that the Merger is fair to, and in the best interests of, the Company and its minority and unaffiliated stockholders on the basis of the factors and considerations described in the   *Special Factors Background of the Merger Reasons for the Merger; Fairness of the Merger; Recommendations of the Special Committee and the Board*   section beginning on page 23. In addition, the Parent Filing Persons believe that the Merger is fair to the minority and unaffiliated stockholders of the Company on the basis of the additional factors and considerations described below in this section. In this section, we refer to the   Board   to mean the Board of Directors other than Mr. Gumbiner (who did not participate as a Board member in discussions relating to the Merger).

The Parent Filing Persons have not engaged a financial advisor to perform any valuation or other analysis for the purpose of assessing the fairness of the Merger to the minority and unaffiliated stockholders of the Company. Based on the Parent Filing Persons   knowledge and analysis of available information regarding the Company, the Parent Filing Persons believe that the Merger is substantively fair to the minority and unaffiliated stockholders of the Company. In particular, the Parent Filing Persons considered the following factors:

- other than their receipt of Board and Special Committee fees (which are not contingent upon the consummation of the Merger or the Special Committee s or the Board s recommendation or approval of the Merger) and their interests described in the   *Special Factors Interests of the Company s Directors and Executive Officers in the Merger*   section beginning on page 43, no member of the Special Committee has a financial interest in the Merger that is different from, or in addition to, the interests of the minority and unaffiliated stockholders generally, although the Merger Agreement does include customary provisions for indemnity and the continuation of liability insurance for the Company s officers and directors;

the Board (consisting of Mr. Crocco, Ms. Feldman and Mr. Powers, without Mr. Gumbiner s participation) determined, based on the unanimous recommendation of the Special Committee (consisting of Mr. Crocco, Ms. Feldman, and Mr. Powers), that the Merger is fair to, and in the best interests of, the Company and its minority and unaffiliated stockholders;

the $10.00 per share of Common Stock originally agreed to be paid to the holders of the Company s shares of Common Stock pursuant to the Merger Agreement represented a 78.3% premium over the closing price of the Common Stock on November 8, 2012, the last trading day prior to the date on which the offer was announced; a premium of 49.8% over the average closing price of $6.68 per share of Common Stock during the 30-day period ended November 8, 2012; a premium of 27.5% over the average closing price of $7.85 per share of Common Stock during the 60-day period ended November 8, 2012; a premium of 17.4% over the average closing price of $8.52 per share of Common Stock during the 90-day period ended November 8, 2012; and a premium of 15.7% over the average closing price of $8.64 per share of Common Stock during the 120-day period ended November 8, 2012. Accordingly, the increased Merger Consideration of $13.00 per share, without interest, less a proportionate deduction for any incentive fee and attorney s fees that may be awarded by the Court to the plaintiff and the plaintiff s counsel in the Sample Litigation, will, if approved, represent at least a 120% premium over the closing price of our Common Stock on November 8, 2012; a premium of at least 85% over the average closing price of $6.68 per share of Common Stock during the 60-day period ended November 8, 2012; a premium of at least 57% over the average closing price of

$7.85 per share of Common Stock during the 60-day period ended November 8, 2012; a premium of at least 45% over the average closing price of $8.52 per share of Common Stock during the 90-day period ended November 8, 2012; and a premium of at least 43% over the average closing price of $8.64 per share of Common Stock during the 120-day period ended November 8, 2012 if the Court approves an incentive fee and attorney s fees totaling $325,000, which is equivalent to approximately $0.62 per share, that the plaintiff and the plaintiff s counsel have requested and, therefore, the Merger Consideration is $12.38 per share;

the Merger will provide consideration to the minority and unaffiliated stockholders of the Company entirely in cash, allowing the minority and unaffiliated stockholders of the Company to realize immediately a certain and fair value for their shares of Common Stock and eliminating any uncertainty in valuing the consideration to be received by those stockholders;

the Parent Filing Persons understanding of the Company s business, historical and current financial performance, competitive and operating environment, operations, management strength and future prospects, including Brookwood s dependence on military sales and the decline in those sales in recent years;

the high costs of operating as a public company;

the fact that there are no unusual requirements or conditions to the Merger, and the ability of Parent to fund fully the payment of the Merger Consideration and the related fees and expenses from internal sources; and

that the Merger Agreement allows the Board to withdraw or change its recommendation of the Merger Agreement, and to terminate the Merger Agreement, under certain circumstances.

While the Parent Filing Persons were aware of a variety of risks and other potentially negative factors concerning the Merger, the Parent Filing Persons did not specifically take such factors into account in determining the per share Merger Consideration or the fairness of the per share Merger Consideration to the minority and unaffiliated stockholders of the Company, and such factors did not directly influence the Parent Filing Persons determination that the Merger is substantively fair to the minority and unaffiliated stockholders. Further, the Parent Filing Persons took into account that at certain points over the year prior to the signing of the Merger Agreement, the Company s stock price exceeded the per share Merger Consideration. However, the Parent Filing Persons determination that the Merger was fair to the minority and unaffiliated stockholders of the Company was based on all factors and considerations, taken as a whole.

The Parent Filing Persons did not attempt to calculate, and did not consider, a pre-Merger public company going concern value for the Company for purposes of determining the fairness of the Merger Consideration to the minority and unaffiliated stockholders of the Company because they believe that any such calculated value is speculative and unreliable and that the pre-announcement per share price of Common Stock, which is described above, is a much more reliable indication of the Company s pre-Merger value. In addition, the Parent Filing Persons did not consider net book value of Common Stock because they believe that net book value, which is an accounting concept, does not reflect, or have any meaningful impact on, either the market trading prices of Common Stock or the Company s value as a going concern. The Parent Filing Persons did not consider liquidation value in determining the fairness of the Merger to the minority and unaffiliated stockholders of the Company because of their belief that liquidation sales generally result in proceeds substantially less than sales of a going concern, because of the impracticability of

determining a liquidation value given the significant execution risk involved in any breakup, because they considered the Company to be a viable, going concern and because the Company will continue to operate its business following the Merger. The Parent Filing Persons are not aware of any firm offers made by any unaffiliated person during the two years prior to the execution of the Merger Agreement for the merger or consolidation of the Company with or into another company, or vice versa, the sale or transfer of all or any substantial part of the Company s assets or a purchase of the Company s securities that would enable the holder to exercise control of the Company in determining the fairness of the Merger to the minority and unaffiliated stockholders Company and, therefore, did not take any such offers into account in determining the fairness of the Merger.

The Parent Filing Persons believe that the Merger is procedurally fair to the minority and unaffiliated stockholders of the Company based primarily upon the following:

other than their receipt of Board of Directors and Special Committee fees (which are not contingent upon the consummation of the Merger or the Special Committee s or the Board s recommendation or approval of the Merger) and their interests described in the *Special Factors Interests of the Company s Directors and Executive Officers in the Merger* section beginning on page 43, the Special Committee, consisting solely of directors who are not officers or employees of the Company and who are not affiliated with Parent or Mr. Gumbiner, and who have no financial interest in the Merger that is different from, or in addition to, the interests of the minority and unaffiliated stockholders generally, was given exclusive authority to, among other things, review, evaluate and negotiate the terms of the proposed Merger, to decide not to engage in the Merger and to consider alternatives to the Merger;

- the Special Committee retained its own independent legal and financial advisors;
- the Special Committee and its advisors had all information they believed was necessary to represent the interests of the minority and unaffiliated stockholders effectively;
- the per share Merger Consideration, and the other terms and conditions of the Merger Agreement, resulted from arm s-length negotiations between Parent and its advisors, on the one hand, and the Special Committee and its advisors, on the other hand;
- the Special Committee was deliberate in its process, taking approximately seven months to analyze and evaluate Mr. Gumbiner s initial proposal and to negotiate with Mr. Gumbiner the terms of the proposed Merger;
- the Special Committee received an opinion, dated June 4, 2013, of its financial advisor as to the fairness, from a financial point of view and as of such date, to holders of Common Stock (other than holders of Excluded Shares) of the $10.00 per share Merger Consideration originally agreed to be received by those holders;
- the Merger was approved by the unanimous vote of the Board (consisting of Mr. Crocco, Ms. Feldman and Mr. Powers, without Mr. Gumbiner s participation), based on the unanimous recommendation of the Special Committee (consisting of Mr. Crocco, Ms. Feldman and Mr. Powers);
- the Merger is subject to the non-waivable Majority of the Minority Approval condition; and
- the Company s ability to terminate the Merger Agreement if the Majority of the Minority Approval is not obtained, with each party generally bearing its own expenses in such circumstances as described in the *The Merger Agreement Fees and Expenses* section beginning on page 67.

While Mr. Gumbiner is an officer and director of the Company, because of his participation in the transaction as described in the *Special Factors Interests of the Company s Directors and Executive Officers in the Merger* section beginning on page 43, he did not serve on the Special Committee, nor did he participate in, or vote in connection with, the Special Committee s evaluation or recommendation of the Merger Agreement and the Merger or the Board s evaluation or approval of the Merger Agreement and the Merger. For these reasons, the Parent Filing Persons do not believe that Mr. Gumbiner s interests in the Merger influenced the decision of the Special Committee or the Board with respect to the Merger Agreement or the Merger. Parent has stated, including in its initial proposal letter for the Merger, that the failure of the Special Committee to recommend, or the minority and unaffiliated stockholders to approve, the Merger would not adversely affect Parent s or Mr. Gumbiner s future relationship with the Company.

The foregoing discussion of the information and factors considered and given weight by the Parent Filing Persons in connection with the fairness of the Merger Agreement and the Merger is not intended to be exhaustive but is believed to include all material factors considered by them. The Parent Filing Persons did not find it practicable to, and did not, quantify or otherwise attach relative weights to the foregoing factors in reaching their position as to the fairness of the

Merger Agreement and the Merger. Rather, the Parent Filing Persons made the fairness determinations after considering all of the foregoing as a whole. The Parent Filing Persons believe these factors provide a reasonable basis upon which to form their belief that the Merger is fair to the minority and unaffiliated stockholders of the Company. This belief should not, however, be construed as a recommendation to any Company stockholder to approve the Merger or adopt the Merger Agreement. The Parent Filing Persons do not make any recommendation as to how stockholders of the Company should vote their shares of Common Stock relating to the Merger.

DEREGISTRATION OF THE COMPANY S COMMON STOCK

Following and as a consequence of the Merger, the Company will become a privately held company and a wholly owned subsidiary of Parent. Shares of our Common Stock will no longer be listed on any stock exchange or quotation system, including the NYSE MKT or publicly traded and will be deregistered under the Exchange Act.

MARKET PRICE OF THE COMPANY S COMMON STOCK

Shares of Common Stock are traded on the NYSE MKT under the ticker symbol HWG . The closing price of our Common Stock on the NYSE MKT on June 4, 2013, the last trading day prior to our public announcement of the Merger Agreement on June 5, 2013, was $8.05 per share. On March 3, 2014, the closing price of our Common Stock on the NYSE MKT was $12.35 per share. The Company has not paid any cash dividends on its Common Stock since 2008. You are encouraged to obtain current market quotations for our Common Stock.

CERTAIN EFFECTS OF THE MERGER

If the Merger Agreement is adopted by the requisite votes of the Company s stockholders and all other conditions to the Closing are either satisfied or waived, Merger Sub will merge with and into the Company, with the Company continuing as the Surviving Corporation and as a wholly owned subsidiary of Parent. At the Effective Time, each share of Common Stock outstanding immediately prior to the Effective Time (other than Excluded Shares and any Dissenting Shares) will be converted into the right to receive the Merger Consideration, and all such shares will be automatically cancelled upon the conversion thereof and will cease to exist, and each holder of (x) a certificate that immediately prior to the Effective Time represented such share or (y) uncertificated shares represented by book-entry that immediately prior to the Effective Time represented such shares will cease to have any rights with respect thereto, other than the right to receive the Merger Consideration, without interest, upon surrender of such certificate or book-entry share in accordance with the Merger Agreement.

A primary benefit of the Merger to our stockholders (other than holders of Excluded Shares) will be, if the Settlement is approved, the right of such stockholders to receive a cash payment of $13.00, without interest, less a proportionate deduction for any incentive fee and attorney s fees that may be awarded by the Court in connection with the Stipulation of Settlement, filed on February 7, 2014, relating to the Sample Litigation, for each share of Common Stock held by such stockholders, as described above. The plaintiff and plaintiff s attorneys in the Sample Litigation have requested an incentive fee and attorney s fees totaling $325,000, which is equivalent to approximately $0.62 per share. Therefore, the Company expects that the Merger Consideration will be at least $12.38 per share and may be more if the Court does not approve the full amount requested by the plaintiff and the plaintiff s counsel. If the Court approves the full amount requested, the Merger Consideration will represent at least a premium of approximately 53.7% above the closing price of the Common Stock on June 4, 2013, the last trading day prior to our public announcement of the Merger Agreement and a premium of at least approximately 120% above the closing price of the Common Stock on November 8, 2012, the last trading day prior to the date on which Parent s proposal of a transaction was announced. Additionally, such stockholders will avoid the risk after the Merger of any possible decrease in our future earnings, growth or value.

The primary detriments of the Merger to our stockholders (other than holders of Excluded Shares) include the lack of interest of such stockholders in any potential future earnings, growth or value realized by the Company after the Merger. The minority and unaffiliated stockholders will be required to surrender their shares in exchange for a cash price determined by the filing persons and such stockholders will not have the right as a result of the merger to liquidate their shares at a time and price of their choosing. Additionally, the receipt of cash in exchange for shares of Common Stock pursuant to the Merger generally will be a taxable transaction for U.S. federal income tax purposes to our stockholders who are U.S. holders. See *Special Factors Material U.S. Federal Income Tax Consequences of the Merger* beginning on page 44.

PROJECTED FINANCIAL INFORMATION

The Company does not as a matter of course make public projections as to future sales, earnings, or other results. However, the management of the Company prepared the projected financial information for Brookwood and the Company as of March 12, 2013 and May 7, 2013, set forth below and both were made available to the Board, the Special Committee, the Company s financial advisors, and the Special Committee s advisors in connection with their respective consideration of strategic alternatives available to the Company. This information was also made available to Mr. Gumbiner in the normal course of business in his capacity as a member of management and the Board. In addition, the management of the Company prepared the projected financial information for Brookwood and the Company as of November 7, 2012 described below, which was made available to the Board, including Mr. Gumbiner, in the normal course of business. The accompanying projected financial information was not prepared with a view

toward public disclosure or with a view toward complying with the guidelines established by the American Institute of Certified Public Accountants with respect to projected financial information, but, in the view of the Company s management, was prepared on a reasonable basis, and at the time it was prepared reflected the best estimates and judgments then available, and presented, to the best of management s knowledge and belief, the expected course of action and the expected future financial performance of the Company. However, this information is not fact and should not be relied upon as being necessarily indicative of future results, and readers of this proxy statement are cautioned not to place undue reliance on the prospective financial information.

Neither the Company s independent auditors, nor any other independent accountants, have compiled, examined, or performed any procedures with respect to the projected financial information contained herein, nor have they expressed any opinion or any other form of assurance on such information or its achievability, and assume no responsibility for, and disclaim any association with, the prospective financial information.

The projected financial information is being included in this proxy statement not to influence your decision whether to vote for or against the proposal to adopt the Merger Agreement, but because these financial forecasts were made available to the Board, the Special Committee, the Company s financial advisors, or the Special Committee s advisors. The inclusion of this information should not be regarded as an indication that the Company, the Board, the Special Committee, the Special Committee s advisors, the Company s financial advisors or any other recipient of this information considered, or now considers, such financial forecasts to be a reliable prediction of future results. No person has made or makes any representation to any stockholder regarding the information included in these financial forecasts.

Although presented with numerical specificity, the projected financial information is based upon a variety of estimates and numerous assumptions made by the Company s management with respect to, among other matters, industry performance, general business, economic, market and financial conditions and other matters, including the factors described under *Cautionary Statement Concerning Forward-Looking Information* beginning on page 51, many of which are difficult to predict, are subject to significant economic and competitive uncertainties, and are beyond the Company s control. As a result, there can be no assurance that the estimates and assumptions made in preparing the projected financial information will prove accurate, that the projected results will be realized or that actual results will not be significantly higher or lower than projected.

The financial projections for Brookwood are dependent on Brookwood s having adequate liquidity to purchase greige goods and other raw materials and to maintain levels of inventory to support both ongoing programs and opportunistic sales.

The projected financial information was prepared as of the date indicated, and thus does not take into account any circumstances or events occurring after the date it was prepared, and, except as may be required in order to comply with applicable securities laws, neither the Company nor its management intends to update, or otherwise revise, the projected financial information, or the specific portions presented, to reflect circumstances existing after the date when they were made or to reflect the occurrence of future events, even in the event that any or all of the assumptions are shown to be in error. In addition, the projected financial information assumes that the Company will remain a publicly traded company.

For the foregoing reasons, as well as the bases and assumptions on which the projected financial information was compiled, the inclusion of specific portions of the projected financial information in this proxy statement should not be regarded as an indication that the Company considers such projected financial information to be an accurate prediction of future events, and the projections should not be relied on as such an indication. No one has made any representation to any stockholder of the Company or anyone else regarding the information included in the projected financial information discussed below.

On March 12, 2013, management presented the 2013 projected financial information for Brookwood and the Company summarized below to the Board.

BROOKWOOD FINANCIAL PROJECTIONS

CONSOLIDATED STATEMENT OF EARNINGS

MARCH 12, 2013

			2013 FORECAST MARCH 12, 2013				
			Q1	Q2	Q3	Q4	Year
	2011	2012	Forecast	Forecast	Forecast	Forecast	Forecast
Sales	**139,499**	**130,524**	**30,855**	**32,175**	**31,075**	**33,480**	**127,615**
Cost of sales	**115,865**	**112,193**	**27,340**	**28,196**	**26,953**	**28,964**	**111,453**
Gross profit	**23,634**	**18,332**	**3,545**	**3,979**	**4,122**	**4,516**	**16,162**
	16.94%	**14.04%**	**11.48%**	**12.37%**	**13.99%**	**13.49%**	**13.32%**
Operating expenses	**17,999**	**18,824**	**3,945**	**3,945**	**3,945**	**3,945**	**15,778**
Operating Profit (EBIT)	**5,635**	**(493)**	**(400)**	**35**	**177**	**572**	**384**
	4.04%	**-0.38%**	**-1.29%**	**0.11%**	**0.57%**	**1.71%**	**0.30%**
Interest (income) / expense	**78**	**166**	**47**	**57**	**57**	**66**	**228**
Profit before income taxes	**5,557**	**(659)**	**(447)**	**(22)**	**119**	**505**	**156**

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	2011	2012	Q1 Forecast	Q2 Forecast	Q3 Forecast	Q4 Forecast	Year Forecast
			2013 FORECAST MARCH 12, 2013				
	3.98%	-0.50%	-1.45%	-0.07%	0.38%	1.51%	0.12%
Income taxes	2,183	(250)	(161)	(8)	43	182	56
Net income	3,374	(408)	(286)	(14)	76	323	100

BROOKWOOD CONSOLIDATED BALANCE SHEET

MARCH 12, 2013

Amounts in $000	2013 Q1 Actual	Q2 Forecast	Q3 Forecast	Q4 Forecast
Cash	202	223	205	237
Marketable Securities				
Accounts receivable (net)	19,149	19,949	19,267	20,758
Inventory (net)	25,076	25,258	26,057	26,567
Prepaid expenses	1,199	1,199	1,199	1,199
Other current assets	1,201	1,201	1,201	1,201
Total Current Assets	46,827	46,830	47,939	49,962
Fixed assets (net)	20,079	20,089	20,132	20,160
Other assets	146	146	146	146
Total Assets	67,052	67,065	68,217	70,268
Notes payable current				
Accounts payable	9,629	9,218	9,906	10,096
Accrued expenses	3,934	3,872	4,210	4,548
Taxes payable	1,183	1,183	1,183	1,183
Total Current Liab.	14,746	14,273	15,299	15,827
Notes payable - Rev long term	5,030	5,530	5,580	6,780
Capital stock	17,942	17,942	17,942	17,942
Retained earnings	29,334	29,320	29,396	29,720
Total Liab. & S/E	67,052	67,065	68,217	70,268

THE COMPANY CASH FLOW PROJECTIONS

MARCH 12, 2013

Amounts in $000	**2013 Forecast**
CASH FLOWS FROM OPERATING EXPENSES	
Net Income	100
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation	2,308
Changes in assets and liabilities	
(Increase) / decrease in accounts receivable - net	(1,011)
(Increase) / decrease in inventories - net	(1,501)
(Increase) / decrease in prepaid expenses	
(Increase) / decrease in other current assets	
(Increase) / decrease in other assets	
Increase / (decrease) in accounts payable	1,550
Increase / (decrease) in accrued expenses	339
Increase / (decrease) in taxes payable	
Net cash provided by operating activities	1,785

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Amounts in $000	2013 Forecast
CASH FLOWS FROM INVESTING ACTIVITIES:	
Addition of CT facility	
Additions to property, plant & equipment	(2,394)
Disposals of property, plant & equipment	
Short Term Investment, Purchases & Redemptions	
Net cash used for investing activities	(2,394)
CASH FLOWS FROM FINANCING ACTIVITIES:	
Increase / (decrease) in notes payable - Long Term	1,450
Increase / (decrease) in notes payable - Short Term	
Dividends paid to parent	(650)
Net cash provided by financing activities	800
NET INCREASE (DECREASE) IN CASH	190
CASH, BEGINNING OF PERIOD	

The financial projections as of March 12, 2013 presented in this proxy statement are set forth in the form in which they were presented by the Company to Southwest Securities: separately for Brookwood, as an operating subsidiary, and the Company, as a parent holding company. Projections are typically presented to the Company s Board of Directors in this manner. Additionally, management of the Company provided Southwest Securities with further financial information in order to reflect the forecasted results for the consolidated Company, including certain anticipated holding company expenses that included an estimated $4 million for holding company selling, general and administrative expenses and $525,000 for holding company interest expense. The report of Southwest Securities dated March 28, 2013, which is attached to the Form 13E-3 as Exhibit 99.2, presented such projections on a consolidated basis.

On May 7, 2013, management presented the 2013 projected financial information for Brookwood and the Company summarized below to the Board.

BROOKWOOD FINANCIAL PROJECTIONS

CONSOLIDATED STATEMENT OF EARNINGS

MAY 7, 2013

			2013 FORECAST MAY 7, 2013				
	Actual 2011	Actual 2012	Q1 Actual	Q2 Forecast	Q3 Forecast	Q4 Forecast	Year Forecast
Sales	**139,499**	**130,524**	**31,283**	**33,875**	**31,075**	**33,480**	**129,713**
Cost of sales	**115,865**	**112,193**	**27,459**	**29,279**	**26,728**	**28,964**	**112,430**
Gross profit	**23,634**	**18,332**	**3,824**	**4,597**	**4,347**	**4,516**	**17,283**
	16.94%	**14.04%**	**12.22%**	**13.57%**	**13.99%**	**13.49%**	**13.32%**
Operating expenses	**17,999**	**18,824**	**3,730**	**4,021**	**4,021**	**4,021**	**15,792**

Operating Profit (EBIT)	**5,635**	**(493)**	**94**	**576**	**326**	**496**	**1,491**
	4.04%	**-0.38%**	**0.30%**	**1.70%**	**1.05%**	**1.48%**	**1.15%**
Interest (income) / expense	**78**	**166**	**62**	**60**	**53**	**62**	**237**
Profit before income taxes	**5,557**	**(659)**	**32**	**515**	**273**	**433**	**1,254**
	3.98%	**-0.50%**	**0.10%**	**1.52%**	**0.88%**	**1.29%**	**0.97%**
Income taxes	**2,183**	**(239)**	**12**	**186**	**98**	**156**	**452**
Net income	**3,374**	**(419)**	**20**	**330**	**175**	**277**	**802**

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BROOKWOOD CONSOLIDATED BALANCE SHEET

MAY 7, 2013

	2013			
	Q1	Q2	Q3	Q4
Amounts in $000	Actual	Forecast	Forecast	Forecast
Cash	32	200	219	239
Marketable Securities				
Accounts receivable (net)	21,654	22,358	20,510	22,097
Inventory (net)	23,325	23,788	25,778	26,028
Prepaid expenses	886	886	886	886
Other current assets	1,206	1,206	1,206	1,206
Total Current Assets	47,103	48,437	48,598	50,456
Fixed assets (net)	19,631	19,754	19,912	20,077
Other assets	136	136	136	136
Total Assets	66,870	68,327	68,646	70,669
Notes payable current	2,675	5,975	4,925	6,225
Accounts payable	11,789	10,229	11,084	11,192
Accrued expenses	3,897	3,535	3,873	4,211
Taxes payable	1,387	1,387	1,387	1,387
Total Current Liab.	19,748	21,126	21,269	23,015
Notes payable Revolver				
Capital stock	17,942	17,942	17,942	17,942
Retained earnings	29,180	29,260	29,435	29,712
Total Liab. & S/E	66,870	68,327	68,646	70,669

THE COMPANY CASH FLOW PROJECTIONS

MAY 7, 2013

	2013
Amounts in $000	Forecast
Brookwood Related	
Dividends (Ordinary & Special)	950
Tax Sharing Payments	345
Corporate Operating Expenses	

G&A Expenses, Net of Interest	(4,057)
Net Operating Cash Flow	(2,762)
HFL Loan (Principal & interest)	(4,725)
Federal Income (Taxes) Refunds	4,569
State Taxes	(60)
Net Other Items	(216)
Net Change in Cash	**(2,978)**
Plus Beginning Cash	**141**
Equals Ending Cash	**(2,837)**

Management of Brookwood also prepared projected 2013 financial information for Brookwood as of November 7, 2012, which was presented to the Board, including Mr. Gumbiner, in the normal course of business.

In the November 2012 information, management projected that Brookwood would have sales, operating profit and net income of $126,700,000, $4,646,000, and $2,797,000, respectively, for 2013.

Additionally, management of the Company prepared projected cash flow information for the Company as of March 12, 2013, which was presented to the Board, including Mr. Gumbiner, in the normal course of business. In such information, management projected that the Company would have operating expenses of approximately $4,240,000, principal and interest payments on the loan from Hallwood Family, L.P. of $4,892,000, would receive an estimated refund of 2010 federal income taxes of $4,569,000,

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and have negative cash flow of $(3,113,000) during 2013, all before consideration of any potential Brookwood dividends or additional proceeds from the HFL Loan in the second half of 2013.

The foregoing projections were based on a number of assumptions concerning the future sales, cost of sales, capital expenditures, including assumptions that: Brookwood s consumer and industrial sales would increase during the periods presented, but that military sales would continue to decline; gross margins would decline during 2012 but increase in 2013; there would be no significant increases in energy, environmental or legal costs; operating expenses would be impacted by the continuing costs of the Nextec litigation; that inventory would continue to require higher than traditional dollar levels due to price increases of raw materials, a trend to more expensive greige, and lower margins; and that capital expenditures would increase during 2013.

FINANCING THE MERGER

Parent will satisfy the funding required for the Merger of a maximum aggregate amount of approximately $6,806,683 from the working capital and personal funds of Parent and HFI, its affiliate. HFI has liquid funds available substantially in excess of $10 million, and prior to the Closing of the Merger will contribute to Parent the amount necessary to fund the Merger. As such, the consummation of the Merger is not subject to a financing contingency.

INTERESTS OF THE COMPANY S DIRECTORS AND EXECUTIVE OFFICERS IN THE MERGER

As of June 4, 2013, Hallwood Trust and Mr. Gumbiner, a director and executive officer of the Company, beneficially owned, through Parent, 1,001,575 shares of Common Stock, in the aggregate, or approximately 65.7% of the total number of outstanding shares of Common Stock. Common Stock beneficially owned by Hallwood Trust and Mr. Gumbiner will be cancelled in the Merger without consideration, and the outstanding shares of Merger Sub will be converted into, and constitute the only outstanding shares, of the Surviving Corporation, with the result that Parent will be the sole stockholder of the Surviving Corporation after the Effective Time.

Charles A. Crocco, Jr., a director of the Company and Chairman of the Special Committee, owned 9,996 shares of Common Stock, or approximately 0.7% of the total number of outstanding shares of Common Stock, as of March 3, 2014.

The members of the Special Committee evaluated and negotiated the Merger Agreement and evaluated whether the Merger is advisable and in the best interests of the Company s minority and unaffiliated stockholders. Mr. Gumbiner did not participate in the deliberations of the Special Committee regarding the Merger Agreement and the transactions contemplated thereby, including the Merger. The members of the Special Committee were aware of these differing interests and considered them, among other matters, in evaluating and negotiating the Merger Agreement and the transactions contemplated thereby, including the Merger, and in recommending to the stockholders that the Merger Agreement be adopted. See the section entitled *Special Factors Background of the Merger* beginning on page 15 for a further discussion of these matters. You should take these interests into account in deciding whether to vote **FOR** the proposal to adopt the Merger Agreement.

EFFECTIVE TIME OF MERGER

The Merger will become effective when the Company files a certificate of merger with the Secretary of State of the State of Delaware or at such later date or time as Parent and the Company agree in writing and specify in the certificate of merger in accordance with the DGCL (which we refer to herein as the Effective Time).

The Closing will take place on a date which will be no later than the fifth business day after the satisfaction or waiver (to the extent permitted by applicable law and the terms of the Merger Agreement) of the closing conditions stated in the Merger Agreement (other than those conditions that by their nature are to be satisfied at the Closing, but subject to the satisfaction or waiver of such conditions) or at such other time and date as the Company and Parent may agree in writing.

The Company currently expects the Closing to occur soon after the special meeting. The Company, however, can provide no assurance that the Closing will occur by any particular date, if at all. Because the Closing is subject to a number of conditions, the exact timing of the Closing cannot be determined at this time.

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MERGER CONSIDERATION

As a consequence of the Merger, each share of our Common Stock (other than Excluded Shares and any Dissenting Shares) shall be converted automatically into, and shall thereafter represent the right to receive, the Merger Consideration. All shares (other than Excluded Shares and any Dissenting Shares) shall, upon conversion thereof, cease to be outstanding and shall automatically be cancelled and shall cease to exist, and each holder of (x) a certificate that immediately prior to the Effective Time represented such share or (y) uncertificated shares represented by book-entry that immediately prior to the Effective Time represented such shares shall cease to have any rights with respect thereto, except the right to receive the Merger Consideration, without interest, upon surrender of such certificate or book-entry share in accordance with Section 2.2(b) of the Merger Agreement. For more information, see the section entitled *Special Factors Litigation*.

MATERIAL U.S. FEDERAL INCOME TAX CONSEQUENCES OF THE MERGER

The following is a general discussion of the material U.S. federal income tax consequences of the Merger to holders of our Common Stock whose shares are exchanged for cash pursuant to the Merger. This discussion is based on the provisions of the Code, applicable U.S. Treasury regulations, judicial opinions and administrative rulings and published positions of the Internal Revenue Service, each as in effect as of the date hereof. These authorities are subject to change, possibly on a retroactive basis, and any such change could affect the accuracy of the statements and conclusions set forth in this discussion. This discussion does not address any tax considerations under state, local or foreign laws or U.S. federal laws other than those pertaining to the U.S. federal income tax. This discussion is not binding on the Internal Revenue Service or the courts and, therefore, could be subject to challenge, which could be sustained. No ruling is intended to be sought from the Internal Revenue Service with respect to the Merger.

For purposes of this discussion, the term U.S. holder means a beneficial owner of Common Stock that is:

- a citizen or individual resident of the United States;
- a corporation, or other entity taxable as a corporation for U.S. federal income tax purposes, created or organized in or under the laws of the United States, any state thereof or the District of Columbia;
- a trust if (i) a court within the United States is able to exercise primary supervision over the trust s administration and one or more U.S. persons are authorized to control all substantial decisions of the trust or (ii) such trust has a valid election in effect under applicable U.S. Treasury regulations to be treated as a U.S. person; or
- an estate the income of which is subject to U.S. federal income tax regardless of its source.

For purposes of this discussion, a non-U.S. holder is a beneficial owner of shares of Common Stock, other than a partnership or other entity taxable as a partnership for U.S. federal income tax purposes, that is not a U.S. holder.

This discussion applies only to beneficial owners of shares of Common Stock who hold such shares as a capital asset within the meaning of Section 1221 of the Code (generally, property held for investment). Further, this discussion does not purport to consider all aspects of U.S. federal income taxation that may be relevant to a holder in light of its

particular circumstances, or that may apply to a holder that is subject to special treatment under the U.S. federal income tax laws (including, for example, insurance companies, controlled foreign corporations, passive foreign investment companies, dealers or brokers in securities or foreign currencies, traders in securities who elect the mark-to-market method of accounting, holders liable for the alternative minimum tax, U.S. holders that have a functional currency other than the U.S. dollar, tax-exempt organizations, banks and certain other financial institutions, mutual funds, certain expatriates, partnerships or other pass-through entities or investors in partnerships or such other entities, holders who hold shares of Common Stock as part of a hedge, straddle, constructive sale or conversion transaction, holders who will hold, directly or indirectly, an equity interest in the Surviving Corporation, and holders who acquired their shares of Common Stock through the exercise of employee stock options or other compensation arrangements).

If a partnership (including any entity or arrangement treated as a partnership for U.S. federal income tax purposes) holds shares of Common Stock, the tax treatment of a partner in such partnership will generally depend on the status of the partners and the activities of the partnership. If you are a partner of a partnership holding shares of Common Stock, you should consult your tax advisor.

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Holders of Common Stock should consult their own tax advisors as to the specific tax consequences to them of the Merger, including the applicability and effect of the alternative minimum tax, and any state, local, foreign or other tax laws.

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Consequences to U.S. Holders

The receipt of cash by U.S. holders in exchange for shares of Common Stock pursuant to the Merger will be a taxable transaction for U.S. federal income tax purposes. In general, for U.S. federal income tax purposes, a U.S. holder who receives cash in exchange for all of such holder s shares of Common Stock as part of the Merger will recognize capital gain or loss in an amount equal to the difference, if any, between (1) the amount of cash received and (2) the U.S. holder s adjusted tax basis in such shares.

If a U.S. holder s holding period in the shares of Common Stock surrendered in the Merger is greater than one year as of the date of the Merger, the gain or loss generally will be long-term capital gain or loss. Long-term capital gains of certain non-corporate holders, including individuals, are generally subject to U.S. federal income tax at preferential rates. The deductibility of capital losses is subject to limitations. If a U.S. holder acquired different blocks of Common Stock at different times or different prices, such U.S. holder must determine its adjusted tax basis and holding period separately with respect to each block of Common Stock.

In addition to regular U.S. federal income tax, a U.S. holder that is an individual, estate or trust and whose income exceeds certain thresholds is subject to a 3.8% Medicare tax on all or a portion of such U.S. holder s net investment income, which may include all or a portion of such U.S. holder s gain from the disposition of shares of Common Stock. U.S. holders that are individuals, estates or trusts should consult their tax advisors regarding the applicability of the Medicare tax to gain from the disposition of shares of Common Stock.

Consequences to Non-U.S. Holders

A non-U.S. holder whose shares of Common Stock are converted into the right to receive cash in the Merger generally will not be subject to U.S. federal income taxation unless:

- gain resulting from the Merger is effectively connected with the non-U.S. holder s conduct of a U.S. trade or business (and, if required by an applicable income tax treaty, is attributable to a United States permanent establishment of the non-U.S. holder);

- the non-U.S. holder is an individual who is present in the United States for 183 days or more in the individual s taxable year in which the Merger occurs and certain other conditions are satisfied; or

- the Company is or has been a U.S. real property holding corporation (USRPHC) as defined in Section 897 of the Code at any time within the five-year period preceding the Merger, the non-U.S. holder owned more than five percent of our Common Stock at any time within that five-year period, and certain other conditions are satisfied. We believe that, as of the effective date of the Merger, we will not have been a USRPHC at any time within the five-year period ending on the date thereof.

Any gain recognized by a non-U.S. holder described in the first bullet above generally will be subject to U.S. federal income tax on a net income basis at regular graduated U.S. federal income tax rates in the same manner as if such holder were a U.S. person as defined under the Code. A non-U.S. holder that is a corporation may also be subject to an additional branch profits tax at a rate of 30% (or such lower rate as may be specified by an applicable income tax treaty) on after-tax profits effectively connected with a U.S. trade or business to the extent that such after-tax profits are not reinvested and maintained in the U.S. business.

Gain described in the second bullet above generally will be subject to U.S. federal income tax at a flat 30% rate, but may be offset by certain U.S. source capital losses, if any, of the non-U.S. holder.

Information Reporting and Backup Withholding

Payments made to holders in exchange for shares of Common Stock pursuant to the Merger may be subject, under certain circumstances, to information reporting and backup withholding (currently at a rate of 28%). To avoid backup withholding, a U.S. holder that does not otherwise establish an exemption should complete and return Internal Revenue Service Form W-9, certifying that such U.S. holder is a U.S. person, the taxpayer identification number provided is correct and such U.S. holder is not subject to backup withholding. In general, a non-U.S. holder will not be subject to U.S. federal backup withholding and information reporting with respect to cash payments to the non-U.S. holder pursuant to the Merger if the non-U.S. holder has provided an IRS Form W-8BEN (or an IRS Form W-8ECI if the non-U.S. holder s gain is effectively connected with the conduct of a U.S. trade or business).

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Backup withholding is not an additional tax. Any amounts withheld under the backup withholding rules may be refunded or credited against a holder s U.S. federal income tax liability, if any, provided that such holder furnishes the required information to the Internal Revenue Service in a timely manner.

This summary of certain material U.S. federal income tax consequences is for general information only and is not tax advice. Holders of Common Stock should consult their tax advisors as to the specific tax consequences to them of the Merger, including the applicability and effect of the alternative minimum tax and the effect of any federal, state, local, foreign or other tax laws.

REGULATORY APPROVALS

The Company does not believe that the filing of notification and report forms under the Hart-Scott-Rodino Act will be necessary to complete the Merger. However, at any time before or after the Merger, the U.S. Department of Justice, the Federal Trade Commission, a state attorney general or a foreign competition authority could take action under the antitrust laws as it deems necessary or desirable in the public interest, including seeking to enjoin the Merger or seeking divestiture of substantial assets of the Company or Merger Sub or their subsidiaries. Private parties may also bring legal actions under the antitrust laws under certain circumstances. Notwithstanding that no such filings are required, there can be no assurance that a challenge to the Merger on antitrust grounds will not be made or, if a challenge is made, of the result of such challenge.

FEES AND EXPENSES

If the Merger is not consummated, all costs and expenses incurred in connection with the Merger, the Merger Agreement and the transactions contemplated thereby shall be paid by the party incurring or required to incur such expenses. If the Merger is consummated, all costs and expenses incurred by Parent or Merger Sub in connection with the Merger, the Merger Agreement and the transactions contemplated thereby shall be paid by the Surviving Corporation and/or, to the extent applicable, reimbursed to Parent by the Surviving Corporation. Costs incurred or to be incurred in connection with the Merger are estimated as follows:

	Amount to be Paid
Financial advisory fee and expenses	$ 152,000.00
Legal, accounting and other professional fees	605,000.00
SEC filing fees	674.39
Proxy solicitation, printing and mailing costs	70,000.00
Paying agent fees	18,000.00
Special committee fees	185,000.00
Miscellaneous	10,000.00
Total	$ 1,040,876.69

The Company will pay all costs listed above, excluding the paying agent fees, which will be paid by Parent. The expenses detailed above will not reduce the Merger Consideration to be received by our minority and unaffiliated stockholders.

LITIGATION

From time to time, the Company, its subsidiaries, certain of its affiliates and others have been named as defendants in lawsuits relating to various transactions in which the Company or its affiliated entities participated. Although the Company does not believe that the results of any of these matters are likely to have a material adverse effect on its financial position, results of operations or cash flows, except as described below, it is possible that any of the matters could result in material liability. Hallwood Group has spent significant amounts in professional fees and other associated costs in connection with these matters, and it expenses professional fees and other costs associated with litigation matters as incurred.

Nextec Applications, Inc.

In July 2007, Nextec Applications, Inc. filed *Nextec Applications, Inc. v. Brookwood Companies Incorporated and The Hallwood Group Incorporated* in the United States District Court for the Southern District of New York (SDNY No. CV 07-6901) claiming

that Brookwood infringed five United States patents pertaining to internally-coated webs. In October 2007, the Company was dismissed from the lawsuit. Nextec later added additional patents to the lawsuit. After a number of motions, only two patents remained in the action and were being asserted against the process and machine for making defendants Agility Storm-Tec X-Treme and Eclipse Storm-Tec X-Treme fabrics, which constitute two levels of the Military s Extended Cold Weather Clothing System. Nextec was seeking a permanent injunction as well as damages in an amount to be determined at trial. After a five week trial that ended on June 1, 2012, the Court ruled from the bench that, while Nextec s patents were valid, Brookwood had not infringed any of the patents in the lawsuit. On July 20, 2012, Nextec filed a motion requesting that the Court either correct/amend its finding of non-infringement or grant a new trial, which the Court subsequently denied. The Court s Order and Final Judgment was issued June 21, 2012. Nextec filed a notice of appeal and Brookwood a notice of cross-appeal. The United States Court of Appeals for the Federal Circuit heard oral argument on November 6, 2013. On November 18, 2013, the United States Court of Appeals for the Federal Circuit summarily affirmed the Southern District of New York s ruling that Brookwood did not infringe any of the patents belonging to Nextec. Nextec has not appealed the decision and the deadline for filing an appeal has expired. Separately, and prior to trial, Brookwood filed requests for reexamination by the United States Patent and Trademark Office of the remaining patent claims at issue in the litigation. The United States Patent and Trademark Office granted the reexamination requests and issued first office actions rejecting all the reexamined patent claims as unpatentable over the prior art of record. With respect to one of the patents, the Patent Office has since received Nextec s responsive arguments and subsequently issued a reexamination certificate. With respect to the second patent, the Patent Office has since received Nextec s responsive arguments and has issued a final rejection to that patent. Nextec has appealed this rejection.

Stockholders Lawsuit

On August 23, 2013, a complaint was filed in the Delaware Court of Chancery (the Court) captioned Sample v. Gumbiner et al., Civil Action No. 8833-VCN. The action named as defendants the directors of the Company, and also named as defendants Parent and Merger Sub. The Company is also named as a defendant, or in the alternative, as a nominal defendant.

In part, the action purported to be a class action of the Company s stockholders brought by a single individual stockholder challenging the Merger. The plaintiff alleges that all defendants other than Merger Sub breached fiduciary duties to those stockholders in connection with the proposed Merger as a consequence of an allegedly unfair merger process and an allegedly unfair merger price. The complaint also alleges that Merger Sub aided and abetted these claimed breaches of fiduciary duty.

In part, the action also purported to be a derivative action brought on behalf of the Company against Mr. Gumbiner and Charles A. Crocco, Jr., based on various matters relating to the investment by the Company in Hallwood Energy in 2008, various related transactions engaged in by the Company or employees, executives, or advisors to the Company, a dividend declared by the Company in 2008, and Hallwood Energy s Chapter 11 bankruptcy court proceeding. The complaint alleges that Mr. Gumbiner and Mr. Crocco engaged in wrongful conduct and/or breached fiduciary duties with respect to these matters and should be held liable to the Company. The complaint further alleged that the $10.00 per share offered in the Merger was unfair and did not reflect the true value of the Company and all of its assets, including potential claims against Mr. Gumbiner, other Company executives and advisors.

The plaintiff sought an order from the court (i) certifying the action as a class action, (ii) finding that the defendants other than Merger Sub breached fiduciary duties to the plaintiff and the class, and that Merger Sub aided and abetted those breaches, (iii) finding that those breaches have proximately caused the plaintiff and the class damage in an amount subject to proof at trial, (iv) awarding the plaintiff and the class any damages that are proven at trial, (v) alternatively, finding that the action is properly brought as a derivative action and that demand on the Board is

excused as to the claims asserted, (vi) alternatively, awarding the company such damages as are proven at trial with respect to the derivative action, (vii) awarding the plaintiff its costs and expenses in connection with this action, including expert and attorney s fees, and (viii) awarding such further and other relief as the court deems just and appropriate.

On February 7, 2014, the plaintiff and the defendants in the Sample Litigation (together, the Parties) entered into the Stipulation, by and through their respective attorneys, whereby the Parties agreed that, in order to resolve the Sample Litigation, the parties to the Merger Agreement would, among other actions, amend the Merger Agreement to increase the Merger Consideration by $3.00 per share, from $10.00 per share to $13.00 per share, less a proportionate deduction for any incentive fee and attorneys fees that may be awarded by the Court to the plaintiff and the plaintiff s counsel in accordance with the Stipulation. The plaintiff and plaintiff s attorneys in the Sample Litigation intend to petition the Court for a $15,000 incentive fee and attorney s fees and expenses not exceeding $310,000, which is equivalent to approximately $0.62 per share. Therefore, the Company expects that the Merger Consideration will be at least $12.38 per share and may be more if the Court does not approve the full amount requested by the plaintiff and the plaintiff s counsel. The plaintiff is further seeking an award of attorney s fees based on the Company s supplemental disclosures, but an award by the Court of attorney s fees based on supplemental disclosures would not affect the Merger Consideration. The defendants specifically deny that they have engaged in any wrongdoing, deny

that they committed any violation of law, deny that they breached any fiduciary duties, and deny liability of any kind to the plaintiff, the Company, or its stockholders. The increased Merger Consideration will be paid if the settlement set forth in the Stipulation (the Settlement) is approved by the Court and the Merger is consummated pursuant to the terms of the Merger Agreement as amended by the Second Amendment.

If the Settlement is approved by the Court, all known and unknown claims against the defendants relating to the Sample Litigation, the Merger, the Settlement, and investments in securities issued by the Company between November 6, 2012 and the date of the Merger will be released, including derivative claims. If the Court does not approve the Settlement, the Settlement and any actions to be taken with respect to the Settlement will be of no further force or effect and will be null and void, provided, however, that any amendment to the Merger Agreement entered into by the parties thereto shall remain in effect. In the event that the Court does not approve the Settlement, the parties to the Merger Agreement have agreed to proceed with the consummation of the Merger based on the original Merger Consideration of $10.00 per share, without the $3.00 per share increase to the Merger Consideration contemplated by the Second Amendment, which would involve the resolicitation of stockholder approval at such price.

On February 11, 2014, the Court entered a Scheduling Order (the Scheduling Order), a form of which was earlier provided to the Court as an attachment to the Stipulation. The Scheduling Order set a public hearing for March 25, 2014, at 10:00 a.m. at which the Court will consider the fairness and adequacy of the Settlement and the applications of the plaintiff and his counsel for an incentive fee and attorney s fees awards. The Scheduling Order also provided that a Notice of Pendency of Class and Derivative Action, Proposed Settlement of Class and Derivative Action, Settlement Hearing, and Right to Appear (the Notice) would be mailed to all persons or entities that were record holders of the Company s Common Stock at any time between and including November 6, 2012 through and including February 11, 2014, the date of entry of the Scheduling Order. The Notice requested brokerage firms, banks and/or other persons or entities who held shares of the Company s Common Stock for the benefit of others to immediately send copies of the Notice to all of their respective beneficial owners. As set forth in the Notice, to the extent that stockholders or members of the class object to (among other things) the Settlement and/or the incentive fee or fee applications, they may file objection papers with the Court at least 10 days prior to the March 25, 2014 hearing date and appear at the hearing so that the Court may consider their objections. Accordingly, as more fully described in the Notice, if you are or were a record or beneficial holder of the Company s Common Stock at any time after and including November 6, 2012, and you wish to be heard and/or to object to the (i) Settlement, (ii) class action determination, (iii) adequacy of representation by the plaintiff and his counsel, (iv) dismissal of the Settled Claims (as defined in the Stipulation), (v) judgments to be entered with respect thereto, and/or (vi) any incentive fee or fee applications, you may file papers with the Court and, if you wish, appear and be heard at the March 25, 2014 hearing. To obtain a copy of the Notice, contact:

Class Action Settlement Administrator:

Kurtzman Carson Consultants

75 Rowland Way, Suite 250

Novato, CA 94945

Attn: Jannette MacDonald

Environmental Contingencies

A number of jurisdictions in which the Company or its subsidiaries operate have adopted laws and regulations relating to environmental matters. Such laws and regulations may require the Company to secure governmental permits and approvals and undertake measures to comply therewith. Compliance with the requirements imposed may be time-consuming and costly. While environmental considerations, by themselves, have not significantly affected the Company s or its subsidiaries business to date, it is possible that such considerations may have a significant and adverse impact in the future. The Company and its subsidiaries actively monitor their environmental compliance and while certain matters currently exist, management is not aware of any compliance issues which will significantly impact the financial position, results of operations or cash flows of the Company or its subsidiaries.

The Company s Brookwood subsidiary is subject to a number of environmental laws, regulations, licenses and permits and has ongoing discussions with environmental regulatory authorities, including the U.S. Environmental Protection Agency, the Rhode Island Department of Health, the Rhode Island Department of Environmental Management and the Connecticut Department of Energy and Environmental Protection on a number of matters, including compliance with safe drinking water rules and wastewater discharge and treatment regulations, the control of chemicals used in the companies coating operations that are classified as air pollutants, the presence of groundwater and soil contaminants at the companies facilities, the removal of underground storage tanks, and hazardous waste management.

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From time to time Brookwood and its subsidiaries have paid fines or penalties for alleged failure to comply with certain environmental requirements, which did not exceed $100,000 in the aggregate during the three years ended December 31, 2012. In addition, Brookwood and its subsidiaries have entered into various settlements and agreements with the regulatory authorities requiring the companies to perform certain tests, undertake certain studies, and install remedial facilities. Brookwood and its subsidiaries incurred capital expenditures to comply with environmental regulations of approximately $572,000 in the year ended December 31, 2012 and $80,000 during the nine months ended September 30, 2013. In addition, Brookwood and its subsidiaries regularly incur expenses associated with various studies and tests to monitor and maintain compliance with diverse environmental requirements.

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CAUTIONARY STATEMENT CONCERNING FORWARD-LOOKING INFORMATION

This proxy statement (including the documents incorporated by reference herein, the annexes hereto and the exhibits filed herewith) includes forward-looking statements that reflect our current views as to future events and financial performance with respect to our operations, the expected completion and timing of the Merger and other information relating to the Merger. All forward-looking statements included in this document are based on information available to the Company on the date hereof. These statements are identifiable because they do not relate strictly to historical or current facts. There are forward-looking statements throughout this proxy statement. Forward-looking statements generally can be identified by the use of forward-looking terminology, such as may, will, would, expect, intend, estimate, should, anticipate , doubt or believe. All statements other than statements of historical information prov herein are forward-looking and may contain information about financial results, economic conditions, trends, and known uncertainties. All forward-looking statements are based on current expectations regarding important risk factors. Many of these risks and uncertainties are beyond the Company s ability to control, and, in many cases, the Company cannot predict all of the risks and uncertainties that could cause actual results to differ materially from those expressed in the forward-looking statements. Actual results could differ materially from those expressed in the forward-looking statements, and readers should not regard those statements as a representation by the Company or any other person that the results expressed in the statements will be achieved. Important risk factors that could cause results or events to differ from current expectations are described in the Company s Annual Report on Form 10-K for the year ended December 31, 2012 under Item 1A Risk Factors . These factors are not intended to be an all-encompassing list of risks and uncertainties that may affect the operations, performance, development and results of the Company s business. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. In addition to other factors and matters contained in or incorporated by reference in this proxy statement, we believe the following factors could cause actual results to differ materially from those discussed in the forward-looking statements:

- the occurrence of any event, change or other circumstance that could give rise to the termination of the Merger Agreement;
- the inability to complete the proposed Merger due to the failure to obtain the required stockholder approvals for the Merger or the failure to satisfy any other conditions to the Closing, including that a governmental entity may prohibit, delay or refuse to grant approval for the Closing;
- the failure of the Merger to close for any other reason;
- risks related to disruption of management s attention from the Company s ongoing business operations due to the Merger;
- the outcome of any legal proceedings, including the Sample Litigation, regulatory proceedings or enforcement matters that have been or may be instituted against the Company and others relating to the Merger Agreement;

- the risk that the Court will not approve the Settlement;
- the risk that the pendency of the Merger disrupts current plans and operations and the potential difficulties in employee retention as a result of the pendency of the Merger;
- the effect of the announcement of the proposed Merger on the Company s relationships with its customers, suppliers, operating results and business generally; and
- the amount of the costs, fees, expenses and charges related to the Merger;

and additional factors that could cause actual results to differ materially from those expressed in the forward-looking statements, which are discussed in reports we have filed with the SEC, including our most recent filings on Forms 10-Q and 10-K. For more information, see the section entitled *Where You Can Find Additional Information* on page 83.

Forward-looking statements speak only as of the date of this proxy statement or the date of the applicable document incorporated by reference in this document. All subsequent written and oral forward-looking statements concerning the Merger or other matters addressed in this proxy statement and attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. Except to the extent required by applicable law or regulation, we do not undertake any obligation to update forward-looking statements to reflect events or circumstances after the date of this proxy statement or to reflect the occurrence of unanticipated events.

THE PARTIES TO THE MERGER

THE COMPANY

The Company is a Delaware corporation. Founded in September 1981, the Company operates its principal business in the textile products industry through its wholly owned subsidiary, Brookwood. Brookwood is an integrated textile firm that develops and produces innovative fabrics and related products through specialized finishing, treating and coating processes.

Additional information about the Company is contained in reports we have filed with the SEC, including our most recent filings on Forms 10-Q and 10-K, which are incorporated by reference into this proxy statement. See the section entitled *Where You Can Find Additional Information* on page 83.

PARENT AND MERGER SUB

Parent is a corporation organized under the laws of the British Virgin Islands. Merger Sub is a Delaware corporation and a wholly owned subsidiary of Parent. Merger Sub was formed solely for the purpose of entering into the Merger Agreement and consummating the transactions contemplated thereby, including the Merger, and has not carried on any business activities to date, except activities incidental to its formation and activities undertaken in connection with the Merger Agreement and the transaction contemplated thereby, including the Merger. Parent owns 1,001,575 shares, or 65.7% of the outstanding shares, of our Common Stock. Parent and Merger Sub are private companies. All outstanding ownership interests of Parent are owned by Hallwood Trust, the trustee of which is a company controlled by Mr. Gumbiner and members of his family.

See Annex D, which is incorporated herein by reference, for additional information regarding the Parent Filing Persons.

THE SPECIAL MEETING

We are furnishing this proxy statement to the Company s stockholders as part of the solicitation of proxies by the Board for use at the special meeting.

DATE, TIME AND PLACE

The special meeting of stockholders will be held at 3710 Rawlins, Suite 1500, Dallas, Texas 75219, on April , 2014 at [ ], Central Time, or at any adjournment or postponement thereof.

PURPOSE OF THE SPECIAL MEETING

The special meeting is being held for the following purposes:

- to consider and vote on a proposal to adopt the Merger Agreement;
- to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement; and
- to act upon other business as may properly come before the special meeting or any adjournment or postponement thereof by or at the direction of the Board.

A copy of the Merger Agreement is attached to this proxy statement as Annex A. This proxy statement and the enclosed form of proxy are first being mailed to our stockholders on or about [ ], 2014.

RECOMMENDATIONS OF THE BOARD AND THE SPECIAL COMMITTEE

The Special Committee (consisting of Mr. Crocco, Ms. Feldman and Mr. Powers), with the assistance of its independent legal and financial advisors, unanimously determined that the transactions contemplated by the Merger Agreement, including the Merger, are fair to, and in the best interests of, the Company s stockholders and unanimously recommended that the Board approve and declare advisable the Merger Agreement and the transactions contemplated thereby, including the Merger, and that the Company s stockholders vote for the adoption of the Merger Agreement.

Based in part on the unanimous recommendation of the Special Committee, and with the assistance of its independent legal and financial advisors, on June 4, 2013, the Board (consisting of Mr. Crocco, Ms. Feldman and Mr. Powers, and excluding Mr. Gumbiner, who did not participate due to his interest in the Merger) unanimously (i) determined that the transactions contemplated by the Merger Agreement, including the Merger, are advisable and in the best interests of the Company s stockholders and are substantively and procedurally fair to the Company s minority and unaffiliated stockholders, (ii) approved and declared advisable the execution, delivery and performance of the Merger Agreement and the consummation of the transactions contemplated thereby, including the Merger, and (iii) resolved to recommend that the Company s stockholders vote for the adoption of the Merger Agreement.

Accordingly, the Board (consisting of Mr. Crocco, Ms. Feldman and Mr. Powers, without Mr. Gumbiner s participation), acting upon the unanimous recommendation of the Special Committee (consisting of

Mr. Crocco, Ms. Feldman and Mr. Powers), unanimously recommends that the stockholders of the Company vote FOR the proposal to adopt the Merger Agreement.

The Board (consisting of Mr. Crocco, Ms. Feldman and Mr. Powers, without Mr. Gumbiner s participation) unanimously recommends that the stockholders of the Company vote FOR the proposal to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement.

RECORD DATE AND QUORUM

The holders of record of Common Stock as of the close of business on March , 2014, the Record Date, are entitled to receive notice of and to vote at the special meeting. On the Record Date, 1,525,166 shares of Common Stock were issued and outstanding and held by approximately 436 holders of record. Of these total issued and outstanding shares of Common Stock, 523,591 are owned by holders other than Parent, Merger Sub, Mr. Gumbiner or their respective affiliates.

No matter may be considered at the special meeting unless a quorum is present. For any matter to be considered, the presence, in person or represented by proxy, of the holders of a majority of the shares of Common Stock entitled to vote as of the Record Date will constitute a quorum. Shares of Common Stock represented by proxies reflecting abstentions and properly executed broker non-votes will be counted as present and entitled to vote for purposes of determining a quorum. A broker non-vote occurs when a bank, broker or other nominee does not vote on a particular matter because such bank, broker or other nominee does not have the discretionary voting power with respect to that proposal and has not received voting instructions from the beneficial owner. Banks, brokers and other nominees will not have discretionary voting power with respect to the proposal to adopt the Merger Agreement. If a quorum is not present, the stockholders who are present or represented by proxy may adjourn the meeting until a quorum is present. However, given Parent s ownership of 65.7% of the issued and outstanding shares of Common Stock, Parent s attendance at the special meeting will, by itself, constitute a quorum.

REQUIRED VOTE

Each share of Common Stock outstanding as of the Record Date is entitled to one vote at the special meeting.

Proposal to Adopt the Merger Agreement

For the Company to consummate the Merger, under Delaware law, stockholders holding at least a majority of the shares of Common Stock outstanding at the close of business on the Record Date must vote **FOR** the proposal to adopt the Merger Agreement. In addition, the Closing is subject to a non-waivable condition that the Merger Agreement be adopted by (i) the affirmative vote of the holders of a majority of the outstanding shares of Common Stock entitled to vote on the adoption of the Merger Agreement, voting together as a single class, and (ii) the affirmative vote of the holders of a majority of the outstanding shares of Common Stock, voting together as a single class, excluding all shares of Common Stock owned by Parent, Merger Sub, Mr. Gumbiner or any of their respective affiliates (other than the Company and its subsidiaries), or by any director, officer or other employee of the Company or any of its subsidiaries.

Proposal to Approve the Adjournment of the Special Meeting, if Necessary or Appropriate, to Solicit Additional Proxies

Approval of the proposal to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement requires the affirmative vote of holders of a majority of the shares of Common Stock present and entitled to vote thereon. However, given Parent s ownership of 65.7% of the issued and outstanding shares of Common Stock, adjournment of the special meeting may be approved solely by the affirmative vote of Parent s shares.

Of the Company s directors and current executive officers, only Mr. Charles A. Crocco, Jr. (director) and Mr. Gumbiner, through Parent, own shares of Common Stock. Mr. Crocco has informed the Company that, as of the date of the filing of this proxy statement, he intends to vote in favor of the proposal to adopt the Merger Agreement.

As of March 3, 2014, Mr. Crocco owned 9,996 shares of Common Stock entitled to vote at the special meeting.

VOTING; PROXIES; REVOCATION

Attendance

All holders of shares of Common Stock as of the close of business on the Record Date, including stockholders of record and beneficial owners of Common Stock registered in the street name of a bank, broker or other nominee, are invited to attend the special meeting. If you wish to attend the special meeting and are a stockholder of record, please be prepared to provide proper identification, such as a driver s license. If you hold your shares in street name, you will need to provide proof of ownership, such as a recent account statement or letter from your bank, broker or other nominee, along with proper identification.

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Voting in Person

Stockholders of record will be able to vote in person at the special meeting. If you are not a stockholder of record, but instead hold your shares in street name through a bank, broker or other nominee, you must provide a proxy executed in your favor from your bank, broker or other nominee in order to be able to vote in person at the special meeting.

Providing Voting Instructions by Proxy

To ensure that your shares are represented at the special meeting, we recommend that you provide voting instructions promptly by proxy, even if you plan to attend the special meeting in person.

If you are a stockholder of record, you may provide voting instructions by proxy by completing, signing, dating and returning the enclosed proxy card. You may alternatively follow the instructions on the enclosed proxy card for Internet or telephone submissions. If you sign, date and return your proxy card without indicating how you wish to vote, your proxy will be voted **FOR** the proposal to adopt the Merger Agreement and **FOR** the proposal to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement and in accordance with the recommendation of the Board on any other matters properly brought before the stockholders at the special meeting for a vote. If you fail to return your proxy card, the effect will be that your shares will not be counted for purposes of determining whether a quorum is present at the special meeting (unless you are a record holder as of the Record Date and attend the special meeting in person) and will have the same effect as a vote **AGAINST** the proposal to adopt the Merger Agreement. Failure to return your proxy card will not affect the vote regarding the proposal to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement.

If your shares are held by a bank, broker or other nominee on your behalf in street name, your bank, broker or other nominee will send you instructions as to how to provide voting instructions for your shares by proxy. Many banks and brokerage firms have a process for their customers to provide voting instructions by telephone or via the Internet, in addition to providing voting instructions by proxy card.

In accordance with the rules of the NYSE MKT, banks, brokers and other nominees who hold shares of Common Stock in street name for their customers do not have discretionary authority to vote the shares with respect to the approval of the Merger Agreement. Accordingly, if banks, brokers or other nominees do not receive specific voting instructions from the beneficial owner of such shares they may not vote such shares with respect to the approval of the Merger Agreement. Under such circumstance, a broker non-vote would arise. Broker non-votes, if any, will be counted for purposes of determining whether a quorum is present at the special meeting, but will have the same effect as a vote AGAINST the proposal to adopt the Merger Agreement. Broker non-votes, if any, will not affect the vote regarding the proposal to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement. For shares of Common Stock held in street name, only shares of Common Stock affirmatively voted **FOR** the proposal to adopt the Merger Agreement will be counted as favorable vote(s) for such proposal(s).

REVOCATION OF PROXIES

Your proxy is revocable. If you are a stockholder of record, you may revoke your proxy at any time before the vote is taken at the special meeting by:

- submitting a new proxy with a later date, by using the telephone or Internet proxy submission procedures described in the proxy card, or by completing, signing, dating and returning a new proxy card by mail to the Company;

- attending the special meeting and voting in person; or

- sending written notice of revocation to the Corporate Secretary of the Company at The Hallwood Group Incorporated, Attn: Corporate Secretary, 3710 Rawlins, Suite 1500, Dallas, Texas 75219.

Attending the special meeting in person without taking one of the actions described above will not in itself revoke a previously submitted proxy. Please note that if you want to revoke your proxy by mailing a new proxy card to the Company or by sending a written notice of revocation to the Company, you should ensure that you send your new proxy card or written notice of revocation in sufficient time for it to be received by the Company before the day of the special meeting.

If you hold your shares in street name through a bank, broker or other nominee, you will need to follow the instructions provided to you by your bank, broker or other nominee in order to revoke your proxy or submit new voting instructions.

ABSTENTIONS

Abstentions will be included in the calculation of the number of shares of Common Stock represented at the special meeting for purposes of determining whether a quorum has been achieved. Abstaining from voting will have the same effect as a vote **AGAINST** the proposal to adopt the Merger Agreement and **AGAINST** the proposal to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the Merger Agreement.

APPRAISAL RIGHTS

Pursuant to Section 262, stockholders who do not vote in favor of the Merger and who comply precisely with the applicable requirements of Section 262 and do not withdraw or otherwise lose the rights to appraisal are entitled to statutory appraisal rights under Delaware law in connection with the Merger. This means that if you comply precisely with the requirements of Section 262, you are entitled to seek appraisal of the fair value of your shares of Common Stock determined by the Court of Chancery of the State of Delaware and to receive payment based on that valuation instead of receiving the Merger Consideration. If you validly exercise (and do not withdraw or lose) appraisal rights, the ultimate amount you may be entitled receive in an appraisal proceeding may be more than, the same as or less than the amount you would have received under the Merger Agreement. To exercise your appraisal rights, (i) you must submit a written demand for appraisal to us before the vote is taken on the Merger Agreement, (ii) you must NOT vote in favor of the proposal to adopt the Merger Agreement and (iii) you must otherwise comply precisely with the requirements of Section 262. Your failure to follow exactly the procedures specified under Delaware law could result in the loss of your appraisal rights. See the section entitled *Rights of Appraisal* beginning on page 77 and the text of the Delaware appraisal rights statute, Section 262, which is reproduced in its entirety as Annex C to this proxy statement. Assuming you have otherwise complied with the requirements of Section 262, your right to seek appraisal under Section 262 is not released under the Settlement, but if the Settlement is approved, you may not claim value related to or arising from the derivative claims that are released, settled, and dismissed with prejudice pursuant to the Settlement.

A person having beneficial interest in shares of Common Stock held of record in the name of another person, such as a broker, bank or other nominee, must act promptly to cause the record holder to follow the steps summarized in this proxy statement and in a timely manner to perfect appraisal rights. **In view of the complexity of Section 262, stockholders who may wish to pursue appraisal rights should consult their legal and financial advisors**.

ADJOURNMENTS AND POSTPONEMENTS

Although it is not currently expected, the special meeting may be adjourned or postponed for the purpose of soliciting additional proxies. In the event that there is present, in person or by proxy, sufficient favorable voting power to secure the vote of the stockholders of the Company necessary to approve the proposal to adopt the Merger Agreement, the Company does not anticipate that it will adjourn or postpone the special meeting unless it is advised by counsel that such adjournment or postponement is necessary under applicable law to allow additional time for any disclosure. Any signed proxies received by the Company in which no voting instructions are provided on such matter will be voted in favor of an adjournment in these circumstances. The time and place of the adjourned meeting will be announced at the time the adjournment is taken, and no other notice need be given, unless the adjournment is for more than 30 days. Any adjournment or postponement of the special meeting for the purpose of soliciting additional proxies will allow

the Company s stockholders who have already sent in their proxies to revoke them at any time prior to their use at the special meeting as adjourned or postponed.

SOLICITATION OF PROXIES

The Company will bear all costs of this proxy solicitation. Proxies may be solicited by mail, in person, by telephone, or by facsimile or by electronic means by officers, directors and regular employees of the Company. In addition, the Company will utilize the services of Georgeson Inc., an independent proxy solicitation firm, and will pay a customary fee, plus reimbursement of out-of-pocket expenses. The Company may also reimburse brokerage firms, custodians, nominees and fiduciaries for their expenses to forward proxy materials to beneficial owners.

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ADDITIONAL ASSISTANCE

If you have more questions about the special meeting, or require assistance in submitting your proxy or voting your shares or need additional copies of the proxy statement or the enclosed proxy card, please contact Georgeson Inc., which is acting as the Company s proxy solicitation agent:

Call Toll-Free 1-866-391-7007

Email: hallwood@georgeson.com

If your broker, bank or other nominee holds your shares, you should also call your broker, bank or other nominee for additional information.

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THE MERGER AGREEMENT

The following is a summary of the material provisions of the Merger Agreement, a copy of which is attached to this proxy statement as Annex A, and which we incorporate by reference into this proxy statement. This summary may not contain all of the information about the Merger Agreement that is important to you. We encourage you to read carefully the Merger Agreement in its entirety, as the rights and obligations of the parties thereto are governed by the express terms of the Merger Agreement and not by this summary or any other information contained in this proxy statement.

EXPLANATORY NOTE REGARDING THE MERGER AGREEMENT

The following summary of the Merger Agreement, and the copy of the Merger Agreement attached as Annex A to this proxy statement, are intended as public disclosure under federal securities laws to provide information regarding the terms of the Merger Agreement and are not intended to modify or supplement any factual disclosures about the Company in its public reports filed with the SEC. In particular, the Merger Agreement and the following summary are not intended to be, and should not be relied upon independently as, disclosures regarding any facts and circumstances relating to the Company or any of its subsidiaries or affiliates. Please refer to the Company s complete filings with the SEC for such information. The Merger Agreement contains representations and warranties by the Company, Parent and Merger Sub that were made only for purposes of the Merger Agreement and as of specified dates. The representations, warranties and covenants in the Merger Agreement were made solely for the benefit of the parties to the Merger Agreement; may be subject to limitations agreed upon by the contracting parties, including being qualified by confidential disclosures made for the purposes of allocating contractual risk between the parties to the Merger Agreement instead of establishing these matters as facts; and may apply contractual standards of materiality or material adverse effect that generally differ from those applicable to investors. In addition, information concerning the subject matter of the representations, warranties and covenants may change after the date of the Merger Agreement, which subsequent information may or may not be fully reflected in the Company s public disclosures. Moreover, the description of the Merger Agreement below does not purport to describe all of the terms of such agreement, and is qualified in its entirety by reference to the full text of such agreement, a copy of which is attached hereto as Annex A and is incorporated herein by reference.

Additional information about the Company may be found elsewhere in this proxy statement and the Company s other public filings. See the section entitled *Where You Can Find Additional Information* beginning on page 83.

STRUCTURE OF THE MERGER

At the Effective Time, Merger Sub will merge with and into the Company and the separate corporate existence of Merger Sub will cease. The Company will be the Surviving Corporation in the Merger, a wholly owned subsidiary of Parent and will continue to be a Delaware corporation after the Merger. The certificate of incorporation of the Surviving Corporation in effect immediately prior to the Effective Time will be amended and restated in its entirety to be in the form of the certificate of incorporation attached as Exhibit A to the Merger Agreement, until amended in accordance with its terms and as provided in the DGCL. The bylaws of the Surviving Corporation will be amended to be the same as the bylaws of Merger Sub in effect immediately prior to the Effective Time, except that the bylaws shall include the name of the Surviving Corporation in the title thereof, and as so amended will be the bylaws of the Surviving Corporation, until thereafter amended in accordance with their terms and as provided in the DGCL. The directors of Merger Sub immediately prior to the Effective Time will be the directors of the Surviving Corporation and will hold office until their respective successors are duly elected and qualified, or their earlier death, incapacitation, resignation or removal. The officers of the Company immediately prior to the date on which the Closing occurs will be the officers of the Surviving Corporation and will hold office until their respective successors

are duly elected and qualified, or their earlier death, resignation or removal.

WHEN THE MERGER BECOMES EFFECTIVE

The Merger will become effective when the Company files a certificate of merger with the Secretary of State of the State of Delaware or at such later date or time as Parent and the Company may agree in writing and specify in the certificate of merger in accordance with the DGCL (which we refer to herein as the Effective Time).

The Closing will take place on a date which will be no later than the fifth business day after the satisfaction or waiver (to the extent permitted by applicable law and the terms of the Merger Agreement) of the closing conditions stated in the Merger

Agreement (other than those conditions that by their nature are to be satisfied at the Closing, but subject to the satisfaction or waiver of such conditions) or at such other time and date as the Company and Parent may agree in writing.

The Company currently expects the Closing to occur soon after the special meeting. The Company, however, can provide no assurance that the Closing will occur by any particular date, if at all. Because the Closing is subject to a number of conditions, the exact timing of the Merger cannot be determined at this time.

EFFECT OF THE MERGER ON OUR COMMON STOCK

At the Effective Time, each share of Common Stock, par value $0.10 per share, of the Company issued and outstanding immediately prior to the Effective Time (other than Excluded Shares and any Dissenting Shares) will be converted automatically into the right to receive the Merger Consideration, whereupon all such shares will be automatically cancelled upon the conversion thereof and will cease to exist, and the holders of such shares will cease to have any rights with respect thereto other than the right to receive the Merger Consideration, without interest, upon surrender of such shares.

At the Effective Time, each Excluded Share will be automatically cancelled and will cease to exist and no consideration will be delivered in exchange for such cancellation. At the Effective Time, each Dissenting Share will be not be converted into, or represent the right to receive, the Merger Consideration and any holder thereof will be entitled to receive payment of the appraised value of the Dissenting Shares in accordance with Section 262, except that all Dissenting Shares held by stockholders who have failed to perfect or who effectively have withdrawn or lost their rights to appraisal of such Dissenting Shares pursuant to Section 262 will thereupon be deemed to have been converted into, and represent the right to receive, the Merger Consideration in the manner provided in the Merger Agreement and will no longer be Dissenting Shares. At the Effective Time, each share of common stock of Merger Sub will be converted into and become one validly issued, fully paid and nonassessable share of common stock of the Surviving Corporation, and will constitute the only outstanding shares of capital stock of the Surviving Corporation.

PAYMENT PROCEDURES AND EXCHANGE OF CERTIFICATES

At or prior to the Effective Time, Parent will deposit, or will cause to be deposited, with a U.S. bank or trust company that will be appointed by Parent (that is reasonably acceptable to the Company) to act as a paying agent under the Merger Agreement, in trust for the benefit of the holders of Common Stock, sufficient cash to pay to the holders of Common Stock (other than the holders of the Excluded Shares and Dissenting Shares) the aggregate Merger Consideration. In the event any Dissenting Shares cease to be Dissenting Shares, Parent will deposit, or cause to be deposited, with the Paying Agent sufficient cash to pay to the holders of such Common Stock the Merger Consideration. As soon as reasonably practicable after the Effective Time and in any event no later than the fifth business day following the Effective Time, the Paying Agent will mail to each record holder of shares of Common Stock that were converted into the Merger Consideration a letter of transmittal and instructions for use in effecting the surrender of certificates that formerly represented shares of the Common Stock or non-certificated shares represented by book-entry in exchange for the Merger Consideration.

Upon surrender of certificates (or effective affidavits of loss in lieu thereof) or book-entry shares to the Paying Agent together with such letter of transmittal, duly completed and validly executed in accordance with the instructions thereto, and such other documents as may customarily be required by the Paying Agent, the holder of such certificates or book-entry shares will be entitled to receive in exchange therefor a check in an amount equal to the product of (x) the number of shares formerly represented by such holder s properly surrendered certificates (or effective affidavits of loss in lieu thereof) or book-entry shares multiplied by (y) the Merger Consideration. No interest will be paid or

accrued on any amount payable upon due surrender of certificates or book-entry shares. In the event of a transfer of ownership of shares that is not registered in the transfer or stock records of the Company, a check for any cash to be paid upon due surrender of the certificate formerly representing such shares may be paid to such a transferee if such certificate is presented to the Paying Agent, accompanied by all documents required to evidence and effect such transfer and to evidence that any applicable stock transfer or other taxes have been paid or are not applicable.

The Surviving Corporation, Parent and the Paying Agent will be entitled to deduct and withhold from the consideration otherwise payable under the Merger Agreement to any holder of shares, such amounts as are required to be withheld or deducted under the Code, or any provision of U.S., state, local or foreign tax law with respect to the making of such payment. To the extent that amounts are so withheld or deducted and paid over to the applicable governmental entity, such withheld or deducted amounts shall be treated for all purposes of the Merger Agreement as having been paid to the holder of the shares in respect of which such deduction and withholding were made.

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REPRESENTATION AND WARRANTIES

The Merger Agreement contains representations and warranties of the Company as to, among other things:

- organization, existence, good standing, and power and authority, including with respect to its subsidiaries;
- corporate power and authority to enter into the Merger Agreement and, subject to receipt of required stockholder approvals, to consummate the transactions contemplated thereby;
- its SEC filings since January 1, 2011, including financial statements contained therein, internal controls and compliance with the Sarbanes-Oxley Act of 2002 and applicable securities laws;
- the absence of certain conflicts, violations, defaults or consent requirements under certain contracts, organizational documents and applicable laws, in each case arising out of the execution and delivery, and consummation of the transactions contemplated by and compliance with the provisions, of the Merger Agreement;
- the absence of certain undisclosed liabilities for the Company and its subsidiaries;
- its and its subsidiaries compliance with applicable legal requirements since January 1, 2011 and possession of necessary permits;
- environmental matters;
- employee benefit matters;
- the absence of certain changes or events since December 31, 2012;
- the absence of certain investigations and litigation;
- this proxy statement and certain information supplied or to be supplied by the Company in connection herewith;
- tax matters;

labor matters;

real and personal property matters;

intellectual property matters;

insurance matters;

receipt by the Special Committee of the opinion of Southwest Securities;

required vote of the Company s stockholders;

material contracts;

the absence of undisclosed fees to finders or brokers; and

state takeover statutes.

The Merger Agreement also contains representations and warranties of Parent and Merger Sub as to, among other matters:

qualification; organization;

corporate power and authority to enter into the Merger Agreement and to consummate the transactions contemplated thereby;

the absence of certain conflicts, violations, defaults or consent requirements under certain contracts, organizational documents and applicable laws, in each case arising out of the execution and delivery of, and consummation of the transactions contemplated by and compliance with the provisions of, the Merger Agreement;

this proxy statement and certain information supplied or to be supplied by Parent or Merger Sub in connection herewith;

Parent s ownership of Merger Sub and the absence of any previous conduct of business by Merger Sub other than incident to its formation and in connection with the Merger Agreement and the transactions contemplated by the Merger Agreement;

the absence of fees to finders or brokers; and

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financial capability of Parent and Merger Sub to consummate the Merger.

Some of the representations and warranties in the Merger Agreement are qualified by materiality qualifications or a Company Material Adverse Effect clause. As used in the Merger Agreement, a Company Material Adverse Effect means any fact, circumstance, event, change, effect or occurrence that (A) has had or is reasonably likely to have a material adverse effect on the assets, properties, liabilities, business, results of operation or financial condition of the Company and its Subsidiaries, taken as a whole, but shall not include facts, circumstances, events, changes, effects or occurrences to the extent (i) generally affecting the industries in which the Company and its subsidiaries operate, (ii) generally affecting the economy or the financial or securities markets in the United States or elsewhere in the world, including changes in interest or exchange rates, (iii) generally affecting regulatory and political conditions or developments, except, in the case of each of (i), (ii) and (iii), to the extent any fact, circumstance, event, change, effect or occurrence disproportionately impacts the assets, properties, business, results of operation or financial condition of the Company and its subsidiaries, taken as a whole, relative to other participants in the industries in which the Company and its subsidiaries operate, (iv) resulting from the announcement of the Merger Agreement and the transactions contemplated thereby, including, but not limited to, the loss of any employees, customers, suppliers or any other third party with whom the Company has a material relationship, (v) resulting from any action taken at the written request of Parent, (vi) resulting from any change in the market price or trading volume of securities of the Company in and of itself; provided, that a fact, circumstance, event, change, effect or occurrence causing or contributing to the change in market price or volume shall not be disregarded from the determination of Company Material Adverse Effect, (vii) resulting from the notice of delisting from the NYSE MKT received by the Company with respect to Common Stock or resulting from any such delisting, or (viii) resulting from acts of war (whether or not declared), sabotage or terrorism (or any escalation or worsening of any such acts of war (whether or not declared), sabotage or terrorism), pandemics, earthquakes, hurricanes, tornados or other natural disasters, (B) that would be reasonably likely to prevent or materially delay or materially impair the ability of the Company or Parent to perform its obligations under the Merger Agreement or to consummate the transactions contemplated herein, or (C) that constitutes an Event of Default under that certain Loan Agreement among Branch Banking and Trust Company, Brookwood, the Company and certain other subsidiaries of the Company dated as of March 30, 2012.

CONDUCT OF BUSINESS PENDING THE MERGER

The Merger Agreement provides that from and after the date of the Merger Agreement and prior to the Effective Time or the date, if any, on which the Merger Agreement is earlier terminated, subject to certain exceptions in the Merger Agreement and disclosure schedules delivered by the Company in connection with the Merger Agreement, the Company will, and will cause each of its subsidiaries to, (A) conduct its business in the ordinary course of business consistent with past practice, (B) use commercially reasonable efforts to maintain and preserve intact its business organization and advantageous business relationships and to retain the services of its key officers and key employees and (C) take no action that would adversely affect or delay the ability of any of the parties to the Merger Agreement from obtaining any necessary approvals of any regulatory agency or other governmental entity required for the transactions contemplated thereby or otherwise materially delay or prohibit consummation of the Merger or other transactions contemplated by the Merger Agreement. The Merger Agreement also provides that between the date of the Merger Agreement and the Effective Time, subject to certain exceptions in the Merger Agreement and disclosure schedules delivered by the Company, the Company will not, and will not permit any of its subsidiaries to, without the prior written consent of Parent (which will not be unreasonably withheld, delayed or conditioned), take any of the following actions:

adjust, split, combine or reclassify any capital stock or otherwise amend the terms of its capital stock;

make, declare or pay any dividend, or make any other distribution on, or directly or indirectly redeem, purchase or otherwise acquire or encumber, any shares of its capital stock; provided, however, that no wholly owned subsidiary will be prohibited under the Merger Agreement from (A) paying any dividend, or making any other distribution, on any shares of its capital stock held by the Company or any other wholly owned subsidiary or (B) directly or indirectly redeeming, purchasing or otherwise acquiring any shares of its capital stock held by the Company;

issue, deliver, pledge or encumber any shares of its capital stock or other equity interests, or rights, warrants or options to acquire, any such shares of capital stock or other equity interests, or grant any person any right to any of the foregoing;

except as is both in the ordinary course of business consistent with past practice and as would not reasonably be expected to delay, adversely affect or impede the Merger, purchase, sell, transfer, mortgage, encumber or otherwise dispose of any properties or assets having a value in excess of $500,000 in the aggregate to any person (other than to a wholly owned subsidiary); provided, however, that no wholly owned subsidiary shall be prohibited under the Merger Agreement from transferring any of its properties or assets to the Company or any other wholly owned subsidiary;

incur, assume, guarantee, prepay, or become obligated with respect to any indebtedness for borrowed money or offer, place or arrange any issue of debt securities, other than any of the foregoing that is both in the ordinary course of business consistent with past practice and would not reasonably be expected to delay, adversely affect or impede the Merger in any material respect; provided, however, that no wholly owned subsidiary will be prohibited under the Merger Agreement from repaying any indebtedness for borrowed money owing by it to the Company or any other wholly owned subsidiary or making any loans or advances to the Company or any other wholly owned subsidiary;

except as is both in the ordinary course of business consistent with past practice and as would not reasonably be expected to delay, adversely affect or impede the Merger in any material respect, make any investment in excess of $500,000 in the aggregate, whether by purchase of stock or securities of, contributions to capital to, property transfers to, or purchase of any property or assets of any other person other than a wholly owned subsidiary of the Company or any wholly owned subsidiary thereof or as permitted under the immediately preceding bullet;

make any acquisition of another person or business, whether by purchase of stock or securities, contributions to capital or property transfers;

except in the ordinary course of business consistent with past practice, enter into, renew, extend, amend or terminate (A) any material contract or contract that if entered into prior to the date of the Merger Agreement would be a material contract, or (B) any contracts not in the ordinary course, involving the commitment or transfer of value in excess of $500,000 in the aggregate in any year or $1 million over the term of the contract;

except to the extent required by law or any Company benefit plan in effect as of the date of the Merger Agreement, (A) increase in any manner the compensation or benefits of any directors, officers, employees, consultants, independent contractors or other service providers of the Company or any of its subsidiaries, except immaterial increases payable to employees, consultants, independent contractors or other service providers (in each case that are not affiliates of any directors or officers of the Company or its subsidiaries) in the ordinary course of business consistent with past practice (including, for this purpose, the normal employee salary, bonus and equity compensation review process conducted each year), (B) pay any pension, severance or retirement benefits to any directors, officers, employees, consultants, independent contractors or other service providers, (C) accelerate the vesting of, or the lapsing of forfeiture restrictions or conditions with respect to, any incentive compensation or establish or cause the funding of any rabbi trust or similar arrangement, (D) establish, adopt, amend or terminate any Company benefit plan or (E) enter into, amend, alter, adopt, implement or otherwise make any commitment to do any of the foregoing;

waive, release, assign, settle or compromise any claim, action or proceeding, other than waivers, releases, assignments, settlements or compromises that involve only the payment of monetary damages not in excess of $100,000 in the aggregate;

amend or waive any provision of its certificate of incorporation or its bylaws or other equivalent organizational documents;

take any action that is intended or would reasonably be expected to result in any of its representations and warranties set forth in the Merger Agreement being or becoming untrue in any material respect (or in any respect in the case of representations and warranties qualified by Company Material Adverse Effect) at any time prior to the Effective Time, or in any of the conditions to the Merger set forth in the Merger Agreement not being satisfied or satisfaction of those conditions being materially delayed in violation of any provision of the Merger Agreement;

enter into any non-compete or similar agreement that would restrict the businesses of the Surviving Corporation or its subsidiaries following the Effective Time or that would in any way restrict the businesses of Parent or its affiliates or take any action that may impose any new or additional regulatory requirement on any affiliate of Parent;

adopt a plan of complete or partial liquidation, dissolution, merger, consolidation, restructuring, recapitalization or other reorganization of such entity;

implement or adopt any change in its tax or financial accounting principles, practices or methods, other than as consistent with or as may be required by U.S. generally accepted accounting principles, law or regulatory guidelines;

(A) make, change or revoke any material tax election, (B) change any material method of reporting for tax purposes, (C) settle or compromise any material tax claim, audit or dispute or (D) make or surrender any claim for a material refund of taxes;

enter into any new, or materially amend or otherwise materially alter any current, agreement or obligations with any affiliate of the Company; or

agree to take, make any commitment to take, or adopt any resolutions of the Board in support of, any of the actions prohibited by any of the foregoing bullets.

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NON-SOLICITATION

Until the Effective Time, the Company, its subsidiaries and their respective representatives are subject to customary no shop restrictions on their ability to initiate, solicit, knowingly encourage (including by providing information) or knowingly facilitate any inquiries, proposals or offers with respect to, or the making or completion of, an Alternative Proposal (as defined below). However, if following the date of the Merger Agreement and prior to the Company obtaining the required stockholder approvals, (i) the Company receives an unsolicited written Alternative Proposal, (ii) the Company has not breached the no shop provision, (iii) the Board (acting through the Special Committee, if then in existence) determines, in good faith, after consultation with its outside counsel and financial advisors, that such Alternative Proposal constitutes or is reasonably likely to result in a Superior Proposal (as defined below) and (iv) after consultation with its outside counsel, the Board of Directors (acting through the Special Committee, if then in existence) determines in good faith that failure to take such action could reasonably be expected to be inconsistent with its fiduciary duties under applicable law, then the Company may (A) furnish information with respect to the Company and its subsidiaries to the person making such Alternative Proposal and its representatives pursuant to a customary confidentiality agreement with a standstill provision and (B) participate in discussions or negotiations with such person and its representatives regarding such Alternative Proposal. As used in the Merger Agreement, Alternative Proposal means any inquiry, proposal or offer from any person or group of persons other than Parent or one of its subsidiaries (1) for a merger, reorganization, consolidation, recapitalization or other business combination, liquidation, dissolution or similar transaction involving the Company or any of its subsidiaries, (2) for the issuance by the Company of over 20% of its equity securities as consideration for the assets or securities of another person or (3) to acquire in any manner, directly or indirectly, over 20% of the equity securities or consolidated total assets of the Company and its subsidiaries, in each case, other than the Merger.

As used in the Merger Agreement, Superior Proposal means a bona fide, unsolicited, written Alternative Proposal (except that references to 20% in the definition of such term will be deemed to be references to 50%) made in writing and not solicited in violation of the no shop provision that the Board (acting through the Special Committee, if then in existence) determines in good faith, after consultation with outside legal counsel and financial advisors, (i) is reasonably likely to be consummated in accordance with its terms, taking into account all legal, financial and regulatory aspects of the proposal and the person making the proposal (including any conditions relating to financing, regulatory approvals or other events or circumstances beyond the control of the party invoking the condition), (ii) for which financing, if a cash transaction (whether in whole or in part), is then fully committed, and (iii) if consummated, would result in a transaction more favorable to the holders of Common Stock in their sole capacity as such (other than Parent and Merger Sub) from a financial point of view (including the effect of any termination fee or provision relating to the reimbursement of expenses) than the transaction contemplated by the Merger Agreement (after taking into account any revisions to the terms of the transaction contemplated by the no shop provision and the time likely to be required to consummate such Alternative Proposal).

Additionally, neither the Board nor any committee thereof may withdraw or modify in a manner adverse to Parent or Merger Sub, or publicly propose to withdraw or modify in a manner adverse to Parent or Merger Sub or fail to publicly reaffirm as promptly as practicable (but in any event within five business days after written receipt of any written request to do so from Parent), its recommendation (a Recommendation Change). Notwithstanding the foregoing, with respect to (aa) an event, fact, circumstance, development or occurrence that affects the business, assets or operations of the Company that is unknown to the Board or any committee thereof as of the date of the Merger Agreement and becomes known to the Board or any committee thereof (an Intervening Event) or (bb) an Alternative Proposal, the Board (acting through the Special Committee, if then in existence) may at any time prior to receipt of the required stockholder approvals, make a Recommendation Change and/or terminate the Merger Agreement if (and only if):

in the case of an Alternative Proposal, the Alternative Proposal (that did not result from a breach of the no shop provision) is made to the Company by a third party, and such Alternative Proposal is not withdrawn, the Board (acting through the Special Committee, if then in existence) determines in good faith after consultation with its financial advisors and outside legal counsel that such Alternative Proposal constitutes a Superior Proposal and the Board (acting through the Special Committee, if then in existence) determines to terminate the Merger Agreement; and

in the case of an Intervening Event, following consultation with outside legal counsel, the Board (acting through the Special Committee, if then in existence) determines that the failure to make a Recommendation Change could reasonably be expected to be inconsistent with the fiduciary duties of the Board (acting through the Special Committee, if then in existence) under applicable laws.

In either case, (x) the Company must provide Parent three business days prior written notice of its intention to take such action, which notice must include the information with respect to such Superior Proposal (if applicable) that is specified in the no shop provision or a description of such Intervening Event (if applicable) and must otherwise specify the basis for the Recommendation Change or proposed termination, (y) after providing such notice and prior to making such Recommendation Change in connection with an Intervening Event or a Superior Proposal, or taking any action to terminate the Merger Agreement with respect to a Superior Proposal, as applicable, the Company must negotiate in good faith with Parent during such three business day period (to the extent that Parent desires to negotiate) to make such revisions to the terms of the Merger Agreement as would permit the Board and the Special Committee not to effect a Recommendation Change in connection with an Intervening Event or a Superior Proposal or to take such action to terminate the Merger Agreement in response to a Superior Proposal, and (z) the Board and the Special Committee must have considered in good faith any changes to the Merger Agreement offered in writing by Parent and must have determined in good faith, after consultation with its outside legal counsel and financial advisors, that the event continues to constitute an Intervening Event or that the Superior Proposal would continue to constitute a Superior Proposal, in each case, if such changes offered in writing by Parent were to be given effect. However, neither the Board nor any committee thereof may effect a Recommendation Change in connection with an Intervening Event or a Superior Proposal or take any action to terminate the Merger Agreement with respect to a Superior Proposal prior to the time that is three business days after it has provided the required written notice; provided, further, that in the event that the Alternative Proposal is modified subsequently by the party making such Alternative Proposal, the Company must provide written notice of such modified Alternative Proposal and must again comply with the no shop provision.

OTHER COVENANTS AND AGREEMENTS

The Merger Agreement contains additional customary agreements between the Company, Parent and Merger Sub relating to, among other matters:

- filings and other actions related to this proxy statement;
- employee matters;
- commercially reasonable efforts;
- state takeover statute;
- public announcements;
- indemnification and insurance;
- participation in any stockholder litigation;

- resignation of directors of the Company;
- notification of certain matters;
- dispositions of Company equity securities under Rule 16b-3; and
- ownership; no acquisition of capital stock of the Company.

CONDITIONS TO THE MERGER

The respective obligations of each party to effect the Merger are subject to the fulfillment (or waiver by all parties (other than the first bullet below, which may not be waived)) at or prior to the Effective Time of the following conditions:

- The required stockholder approvals must have been obtained (including the Majority of the Minority Approval).
- No restraining order, preliminary or permanent injunction or other order issued by any court of competent jurisdiction or other legal restraint or prohibition preventing the consummation of the Merger and/or the other transactions contemplated by the Merger Agreement may be in effect.

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The obligation of the Company to effect the Merger is further subject to the fulfillment (or waiver in writing by the Company) of the following conditions:

(i) The representations and warranties of Parent and Merger Sub contained in the Merger Agreement relating to corporate power and authority to enter into the Merger Agreement must be true and correct in all respects at and as of the Closing Date as though made at and as of the Closing Date, and (ii) the representations and warranties of Parent and Merger Sub set forth in the Merger Agreement (other than in clause (i) above) must be true and correct at and as of the Closing Date as though made at and as of the Closing Date except, in the case of this clause (ii), where the failure of such representations and warranties to be so true and correct (without giving effect to any limitation as to materiality or Material Adverse Effect qualification set forth therein) does not have, and would not reasonably be expected to have, individually or in the aggregate, a material adverse effect on Parent or Merger Sub; provided, however, that, with respect to clauses (i) and (ii) hereof, representations and warranties that are made as of a particular date or period must be true and correct (in the manner set forth in clauses (i) or (ii), as applicable) only as of such date or period.

Parent must have in all material respects performed all obligations and complied with all covenants required by the Merger Agreement to be performed or complied with by it prior to the Effective Time.

Parent must have delivered to the Company a certificate, dated the Effective Time and signed by its chief executive officer or another senior executive officer, certifying to the effect that the conditions set forth in the foregoing two bullets have been satisfied.

The obligation of Parent and Merger Sub to effect the Merger is further subject to the fulfillment (or waiver in writing by Parent and Merger Sub) of the following conditions:

(i) The representations and warranties of the Company contained in the Merger Agreement relating to capitalization, corporate power and authority to enter into the Merger Agreement, absence of certain conflicts, violations, defaults or consent requirements, receipt by the Special Committee of the opinion of Southwest Securities, required vote of the Company s stockholders, absences of undisclosed fees to finders and brokers and state takeover statutes must be true and correct in all respects (except, in the case of the representations and warranties of the Company contained in the Merger Agreement relating to capitalization, for such inaccuracies as are de minimis in the aggregate), in each case at and as of the date of the Merger Agreement and at and as of the Closing Date as though made at and as of the Closing Date, and (ii) the representations and warranties of the Company set forth in this Agreement (other than in clause (i) above) shall be true and correct at and as of the date of this Agreement and at and as of the Closing Date as though made at and as of the Closing Date, except, in the case of this clause (ii), where the failure of such representations and warranties to be so true and correct (without giving effect to any limitation as to materiality or Material Adverse Effect qualification set forth therein) does not have, and would not reasonably be expected to have, individually or in the aggregate, a Company Material Adverse Effect; provided, however, that, with respect to clauses (i) and (ii) hereof, representations and warranties that are made as of a particular date or period must be true and correct (in the manner set forth in clauses (i) or (ii), as applicable) only as of such date or period.

The Company must have in all material respects performed all obligations and complied with all covenants required by the Merger Agreement to be performed or complied with by it prior to the Effective Time.

The Company must have delivered to Parent a certificate, dated the Effective Time and signed by a senior executive officer of the Company (other than any affiliate of Parent), certifying to the effect that the conditions set forth in the foregoing two bullets have been satisfied.

Since the date of the Merger Agreement there must not have been any Company Material Adverse Effect.

Since the date of the Merger Agreement, (i) the Company and each of its subsidiaries must not have violated any applicable environmental laws, and (ii) to the Company s knowledge, there must not have been any release of any hazardous substance by the Company or any of its subsidiaries in any manner that, in the case of either clause (i) or clause (ii) could reasonably be expected to give rise to any remedial obligation, corrective action requirement, penalty, fine, judgment, or other liability of any kind that would result in a Company Material Adverse Effect, or subject the Company or any of its subsidiaries to any obligation in excess of $200,000.

Since the date of the Merger Agreement, there must not have been any recommendation, report, judgment or order, issued by any court of competent jurisdiction, subjecting or proposing to subject the Company or any of its subsidiaries to any obligation exceeding by more than $200,000 the amount of the litigation reserve reflected in the consolidated balance sheet of the Company and its subsidiaries as of December 31, 2012 contained in any filing made by the Company with the SEC since January 1, 2011.

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TERMINATION

The Merger Agreement may be terminated and abandoned at any time prior to the Effective Time, whether before or (subject to the terms of the Merger Agreement) after any approval of the matters presented in connection with the Merger by the stockholders of the Company:

- by the mutual written consent of the Company and Parent;
- by either the Company or Parent, if:
  - the Effective Time has not occurred on or before the End Date and the party seeking to terminate the Merger Agreement must not have breached its obligations under the Merger Agreement in any manner that has proximately caused the failure to consummate the Merger on or before such date;
  - an injunction, other legal restraint or order has been entered permanently restraining, enjoining or otherwise prohibiting the consummation of the Merger and such injunction, other legal restraint or order has become final and nonappealable; provided, that the party seeking to terminate the Merger Agreement must have used its commercially reasonable efforts to remove such injunction, other legal restraint or order in accordance with the Merger Agreement; or
  - the special meeting (including any adjournments thereof) has concluded and the required stockholder approvals contemplated by the Merger Agreement have not been obtained;
- by the Company:
  - if there has been a breach of any of the covenants or agreements or failure to be true of any of the representations or warranties on the part of Parent, which breach or failure to be true, either individually or in the aggregate (A) would result in a failure of a closing condition of Parent and Merger Sub set forth in the Merger Agreement which cannot be cured by the End Date; provided, that the Company must have given Parent written notice, delivered at least thirty days prior to such termination, stating the Company s intention to terminate the Merger Agreement and the basis for such termination; provided, further, that the Company will not have the right to terminate the Merger Agreement if the Company is then in material breach of any of its representations, warranties, covenants or agreements contained in the Merger Agreement; or
  - prior to obtaining the required stockholder approvals, in order to enter into a definitive agreement with respect to a Superior Proposal, but only if the Company has complied in all material respects with its obligations under the no shop provision.

by Parent:

if there has been a breach of any of the covenants or agreements or failure to be true of any of the representations or warranties on the part of the Company which breach or failure to be true, either individually or in the aggregate (A) would result in a failure of a closing condition of the Company set forth in the Merger Agreement and (B) which is not cured within the earlier of (I) the End Date; and (II) thirty days following written notice to the Company; provided, that Parent must have given the Company written notice, delivered at least thirty days prior to such termination, stating Parent s intention to terminate the Agreement and the basis for such termination; provided, further, that Parent will not have the right to terminate the Merger Agreement if Parent is then in material breach of any of its representations, warranties, covenants or agreements contained in the Merger Agreement;

prior to obtaining the required stockholder approvals, if the Board or the Special Committee withdraws or modifies, in a manner adverse to Parent or Merger Sub, or publicly proposes to withdraw or modify, in a manner adverse to Parent or Merger Sub, its recommendation, fails to use commercially reasonable efforts to obtain the required stockholder approvals in accordance with the Merger Agreement or approves or recommends, or publicly proposes to approve or recommend, any Alternative Proposal; or

prior to obtaining the required stockholder approvals, if the Company or any of its subsidiaries or representatives materially breaches its obligations under the no shop provision or its obligations under the Merger Agreement concerning filings and other actions related to this proxy statement or the Company gives Parent notification that it intends to make a Recommendation Change and/or terminate the Merger Agreement due to an Alternative Proposal or Intervening Event as contemplated by the Merger Agreement.

In the event that the Court does not approve the Settlement, the parties to the Merger Agreement have agreed to proceed with the consummation of the Merger based on the original Merger Consideration of $10.00 per share, without the $3.00 per share increase to the Merger Consideration contemplated by the Second Amendment, which would involve the solicitation of stockholder approval at such $10.00 price per share. The Second Amendment further allows for the extension of the End Date to provide reasonably sufficient time for stockholder approval.

FEES AND EXPENSES

If the Merger is not consummated, all costs and expenses incurred in connection with the Merger, the Merger Agreement and the transactions contemplated thereby will be paid by the party incurring or required to incur such expenses. If the Merger is consummated, all costs and expenses incurred by Parent or Merger Sub in connection with the Merger, the Merger Agreement and the transactions contemplated thereby will be paid by the Surviving Corporation and/or, to the extent applicable, reimbursed to Parent by the Surviving Corporation.

SPECIFIC PERFORMANCE

Pursuant to the Merger Agreement, the parties agreed that irreparable damage would occur in the event that any of the provisions of the Merger Agreement were not performed in accordance with their specific terms or were otherwise breached. Each party agreed that, subject to two paragraphs below, in the event of any breach or threatened breach by any other party of any covenant or obligation contained in the Merger Agreement, the non-breaching party will be entitled (in addition to any other remedy that may be available to it whether in law or equity, including monetary damages) to seek to obtain (a) a decree or order of specific performance to enforce the observance and performance of such covenant or obligation, and (b) an injunction restraining such breach or threatened breach.

Each party further agreed that, subject to the immediately following paragraph, (x) it will not oppose the granting of an injunction, specific performance and other equitable relief as provided in the Merger Agreement on the basis that the other party has an adequate remedy at law or an award of specific performance is not an appropriate remedy for any reason at law or equity and (y) no other party or any other Person shall be required to obtain, furnish or post any bond or similar instrument in connection with or as a condition to obtaining any remedy referred to in this paragraph, and each party irrevocably waives any right it may have to require the obtaining, furnishing or posting of any such bond or similar instrument.

Pursuant to the Merger Agreement, under no circumstances will either party be permitted or entitled to receive both (i) a grant of specific performance that permits the consummation of the transactions contemplated by the Merger Agreement, including the Merger, in accordance with the terms of the Merger Agreement and (ii) monetary damages in connection with the Merger Agreement or any termination of the Merger Agreement.

AMENDMENTS AND WAIVERS

At any time prior to the Effective Time, any provision of the Merger Agreement (other than the closing condition relating to the obtainment of required stockholder approvals, including the Majority of the Minority Approval, and its relevant definitions) may be amended or waived if, and only if, such amendment of waiver is in writing and signed, in the case of an amendment, by the Company, Parent and Merger Sub, or, in the case of a waiver, by the party against whom the waive is to be effective; provided, however, that, after receipt of the required stockholder approvals, if any such amendment or waiver shall, by applicable law or in accordance with the rules and regulations of the NYSE MKT exchange, require further approval of the stockholders of the Company, the effectiveness of such amendment or waiver shall be subject to the approval of the stockholders of the Company. Notwithstanding the foregoing, no knowledge, investigation or inquiry, or failure or delay by the Company or Parent in exercising any right under the

Merger Agreement will operate as a waiver thereof nor shall any single or partial exercise thereof preclude any other or further exercise of any other right thereunder.

GOVERNING LAW; JURISDICTION

The Merger Agreement is governed by and construed in accordance with the laws of the State of Delaware, without giving effect to any choice or conflict of law provision or rule (whether of the State of Delaware or any other jurisdiction) that would cause the application of the laws of any jurisdiction other than the State of Delaware. Any legal action or proceeding with respect to the Merger Agreement and the rights and obligations arising thereunder, or for recognition and enforcement of any judgment in

respect of the Merger Agreement and the rights and obligations arising thereunder brought by the other party thereto or its successors or assigns, must be brought and determined exclusively in any federal or state court located in the State of Delaware.

PROVISIONS FOR UNAFFILIATED STOCKHOLDERS

No provision has been made (i) to grant the Company s unaffiliated stockholders access to the corporate files of the Company, any other party to the Merger or any of their respective affiliates, or (ii) to obtain counsel or appraisal services at the expense of the Company, any other such party or affiliate.

IMPORTANT INFORMATION REGARDING THE COMPANY

DIRECTORS AND EXECUTIVE OFFICERS

Directors

The Board presently consists of four members:

Charles A. Crocco, Jr., age 75, has served as a director of the Company since 1981. He is an attorney, and was Counsel to Crocco & De Maio, P.C. through March 2003. He is a Securities Arbitrator in proceedings brought under the auspices of the Financial Industry Regulatory Authority (formerly National Association of Securities Dealers). Mr. Crocco also served as a director of First Banks America, Inc., a bank holding company, from 1989 until December 2002.

Amy H. Feldman, age 61, has served as a director of the Company since 2012. She has been a Realtor representing Timbers Resorts properties in Snowmass Village, Colorado, and Tuscany, Italy since 2002. From 1990 to 2001, Ms. Feldman was an owner or co-owner of Jorden Communications, Inc., a Miami-based public relations and event management agency with specialties in retail communication and marketing, real estate media relations, as well as sports-related event management and media relations. From 1983 to 1988, she was a Certified Public Accountant with Coopers & Lybrand.

Michael R. Powers, age 62, has served as a director of the Company since 2012. He has also been a director of Ankor Holdings Limited, an international commodities trading company with offices in Hong Kong, Monaco and Qatar specializing in the physical and electronic trading of natural resources, since 2011. Since 1998, Mr. Powers has also served as a director of Monte Carlo Entertainment, SAM, a sports management company owning and promoting professional sports events, including ATP pro tennis tournaments and annual PGA senior golf events. Since 2003, Mr. Powers has served as a principal of Monaco Powers SC, a consulting firm working as an advisor primarily to companies in the oil and gas, real estate and sports entertainment industries, including Sotheby s France, Royal Riviera Royalty and Emotion Sports Management Group Austria.

Anthony J. Gumbiner, age 68, has served as a director and Chairman of the Board of the Company since 1981 and Chief Executive Officer of the Company since 1984. He also served as President and Chief Operating Officer from December 1999 to March 2005. He also served as a director and Chairman of the board of directors of Hallwood Energy Management, LLC, the general partner of Hallwood Energy, L.P. and each of the constituent entities of Hallwood Energy, L.P. from their inception until February 2009. Hallwood Energy Management, LLC, Hallwood Energy and its subsidiaries filed petitions for relief under Chapter 11 of the United States Bankruptcy Code on March 1, 2009. He served as a director of Hallwood Realty, LLC, the general partner of Hallwood Realty Partners, L.P. (HRP) and its predecessor until HRP was sold in July 2004. Mr. Gumbiner was a director and officer of

Hallwood Energy Corporation until its sale in December 2004 and of Hallwood Energy III, L.P. until its sale in July 2005. He has served as a director of The Local Radio Company PLC since November 2008. Mr. Gumbiner is also a solicitor of the Supreme Court of Judicature of England. Mr. Gumbiner is a citizen of the United Kingdom.

Executive Officers

In addition to Anthony J. Gumbiner, age 68, who serves as Director, Chairman and Chief Executive Officer of the Company, the following individuals also serve as executive officers:

William L. Guzzetti, age 70, has served as President and Chief Operating Officer of the Company since March 9, 2005. He also served as President, Chief Operating Officer and a director of Hallwood Energy Management, LLC, the general partner of Hallwood Energy, L.P. and each of the constituent entities of Hallwood Energy, L.P. from their inception until February 2009. Mr. Guzzetti served as President, Chief Operating Officer, and Director of the former Hallwood Energy Corporation from December 1998 until May 2001. He was President, Chief Operating Officer, and Director of the general partner of Hallwood Energy Partners, L.P. from February 1985 until June 1999 and President, Chief Operating Officer, and Director of Hallwood

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Consolidated Resources Corporation from May 1991 until June 1999. Mr. Guzzetti served as the President, Chief Operating Officer, and Director of Hallwood Realty, LLC from November 1990 until July 2004. He served as the President, Chief Operating Officer, and Director of the new Hallwood Energy Corporation from December 2002 until December 2004. He is a member of the Florida Bar and the State Bar of Texas. Mr. Guzzetti received a B.A. from Harvard University in 1964 and holds a Juris Doctor from the University of Florida.

Amber M. Brookman, age 70, has been the Chief Executive Officer and President of Brookwood, a wholly owned subsidiary of the Company, since 1989. Ms. Brookman manages the activities of five divisions of Brookwood, as well as its wholly owned subsidiaries Brookwood Laminating, Kenyon Industries, Inc., XtraMile, and Solutions 4. Ms. Brookman served as a Director of Brookwood since 1989. She served as a Director of Syms Corp. from 2004 to 2007.

Richard Kelley, age 53, has been the Chief Financial Officer, Vice President, and Secretary of Company since December 15, 2008. Prior to his appointment, Mr. Kelley had served as the Company s Director of Human Resources since July 2004. He served as the Manager of Financial & SEC Reporting for Hallwood Realty from May 1990 to July 2004. Mr. Kelley served as the Financial Reporting Accountant from June 1985 to March 1987 and as the Manager of Financial & SEC Reporting from March 1987 to May 1990 for Hallwood Energy Corporation.

The address for each director and executive officer is: The Hallwood Group Incorporated, 3710 Rawlins, Suite 1500, Dallas, Texas 75219.

During the past ten years, neither the Company nor any of the Company directors or executive officers listed above has been convicted in a criminal proceeding (excluding traffic violations or similar misdemeanors). In addition, neither the Company nor any of the Company directors or executive officers listed above has been a party to any judicial or administrative proceeding (except for matters that were dismissed without sanction or settlement) that resulted in a judgment, decree or final order enjoining the person from future violations of, or prohibiting activities subject to, federal or state securities laws, or a finding of any violation of federal or state securities laws. Except as indicated above, each of the individuals listed above is a citizen of the United States.

PRIOR PUBLIC OFFERINGS

There have been no underwritten public offerings of the Company s Common Stock during the past three years.

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HISTORICAL SELECTED FINANCIAL INFORMATION

Set forth below is unaudited summarized financial data for the Company as of nine months ended September 30, 2013 and 2012 and audited summarized financial data for the years ended December 31, 2012, 2011, 2010, 2009 and 2008. The financial data for years ended December 31, 2012, 2011 and 2010, has been derived from the audited financial statements contained in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2012 (the 2012 10-K). The financial data for nine months ended September 30, 2013 and 2012 has been derived from the unaudited financial statements contained in the Company s Quarterly Report on Form 10-Q for the quarter ended September 30, 2013 (the 2013 10-Q and together with the 2012 10-K, the Periodic Reports). This data should be read in conjunction with the consolidated financial statements and other financial information contained in the Periodic Reports, including the notes thereto, which are incorporated by reference into this proxy statement. More comprehensive financial information is included in the Periodic Reports, including management s discussion and analysis of financial condition and results of operations, and other documents we file with the SEC. The following summary is qualified in its entirety by reference to the full text of the Periodic Reports and all of the financial information and notes contained in those documents and their exhibits and annexes. See the section entitled *Where You Can Find Additional Information* on page 83.

	Nine months ended September 30,		**Years Ended December 31,**				
	2013	**2012**	**2012**	**2011**	**2010**	**2009**	**2008**
			(in thousands, except per share data)				
Revenues	$ 94,040	$ 100,207	$ 130,524	$ 139,499	$ 168,354	$ 179,554	$ 162,237
Expenses (a)	94,363	117,858	148,934	148,508	152,198	153,922	146,470
Operating income (loss)	(323)	(17,651)	(18,410)	(9,009)	16,156	25,632	15,767
Other income (expense):							
Interest expense	(461)	(315)	(517)	(105)	(301)	(252)	(688)
Other, net	67	2	2	10	36	144	399
Equity loss from investments in Hallwood Energy (b)							(12,120)
	(394)	(313)	(515)	(68)	(291)	(216)	(12,664)
Income (loss) before income taxes	(717)	(17,964)	(18,925)	(9,077)	15,865	25,416	3,103
Income tax expense (benefit)	351	(6,126)	(982)	(2,746)	5,985	8,361	1,705
Net Income (Loss)	$ (1,068)	$ (11,838)	$ (17,943)	$ (6,331)	$ 9,880	$ 17,055	$ 1,398
Net Income (Loss) Per Common Share							
Basic	$ (0.70)	$ (7.76)	$ (11.76)	$ (4.15)	$ 6.48	$ 11.18	$ 0.92
Diluted	(0.70)	(7.76)	(11.76)	(4.15)	6.48	11.18	0.92
Dividends Per Common Share							$ 7.89

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	Nine months ended September 30, 2013	2012	Years Ended December 31, 2012	2011	2010	2009	2008
			(in thousands, except per share data)				
Weighted Average Shares Outstanding							
Basic	1,525	1,525	1,525	1,525	1,525	1,525	1,521
Diluted	1,525	1,525	1,525	1,525	1,525	1,525	1,525
Financial Condition							
Total assets	$ 65,877	$ 81,557	$ 70,906	$ 88,905	$ 85,277	$ 88,440	$ 69,395
Loans payable	6,561	13,034	14,182	2,000	2,000	6,450	10,438
Redeemable preferred stock (c)						1,000	1,000
Common stockholders equity	40,129	47,302	41,197	59,140	65,471	55,591	38,261

(a) The Company recorded charges of $13,200,000 and $9,300,000 in 2012 and 2011, respectively, related to various Hallwood Energy litigation matters. The company recorded a litigation charge credit of $1,082,000 in the 2013 third quarter.

(b) In 2008, Hallwood Energy reported a net loss of $60,941,000, which included an impairment of $32,731,000 associated with its oil and gas properties. The Company recorded an equity loss to the extent of loans it made and a contingent commitment to invest additional funds in Hallwood Energy.

(c) In July 2010, the Company completed a mandatory redemption of the Company s Series B Preferred Stock, at $4.00 per share, in the total amount of $1,000,000. The Series B Preferred Stock was cancelled on the stock records of the Company, and the holders of the Series B Preferred Stock have no continuing rights as stockholders of the Company, other than the right to receive payment of the redemption value.

Computation of Ratio of Earnings to Fixed Charges

The ratio of earnings to fixed charges, the ratio of earnings to combined fixed charges and preferred stock dividends, as well as any deficiency of earnings are determined using the following applicable factors:

Earnings available for Fixed Charges are calculated first, by determining the sum of: (a) income from continuing operations before income taxes and equity income, (b) distributed equity income, (c) fixed charges, as defined below and (d) amortization of capitalized interest, if any. From this total, we added equity loss of an investment in Hallwood Energy accounted for under the equity method.

Fixed Charges are calculated as the sum of (a) interest costs (both expensed and capitalized), (b) amortization of debt expense and discount or premium relating to any indebtedness and (c) that portion of rental expense that is representative of the interest factor.

	9 month periods 2013	2012	Years Ended December 31, 2012	2011	2010	2009	2008
			(in thousands)				
Fixed Charges:							
Interest expense	461	315	517	105	301	252	688

Capitalized interest							
Portion of rental expense which represents interest factor	151	149	199	206	220	316	303(1)

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	9 month periods		Years Ended December 31,				
	2013	2012	2012	2011	2010	2009	2008
	(in thousands)						
Total Fixed Charges	612	464	716	311	521	568	991
Earnings available for Fixed Charges:							
Pre-tax income (loss)	(717)	(17,964)	(18,925)	(9,077)	15,865	25,416	3,103
Add: Distributed equity income of affiliated companies							
Add: Fixed charges	612	464	716	311	521	568	991
Less Capitalized interest							
Add: Equity loss of investment accounted for under the equity method (Hallwood Energy)							12,120
Total Earnings available for Fixed Charges	(105)	(17,500)	(18,209)	(8,766)	16,386	25,984	16,214
Ratio of Earnings to Fixed Charges	*	*	*	*	$ 31.45	$ 45.75	$ 16.36