ELECTRO SENSORS INC
Form 10QSB
November 14, 2005
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

Form 10-QSB

x **QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2005

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

FOR THE TRANSITION PERIOD FROM TO

Commission File Number 0-9587

ELECTRO-SENSORS, INC.

(Exact name of small business issuer as specified in its charter)

Minnesota	**41-0943459**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

6111 Blue Circle Drive
Minnetonka, Minnesota 55343-9108
(Address of principal executive offices)

(952) 930-0100
(Issuer s telephone number)

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

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

The number of shares outstanding of the registrant s Common Stock, $0.10 par value, on November 14, 2005 was 3,248,516.

Transitional Small Business Disclosure Format (check one):
Yes o No x

ELECTRO-SENSORS, INC.
Form 10-QSB
For the Period Ended September 30, 2005

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

ELECTRO-SENSORS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET

	September 30, 2005 (unaudited)
ASSETS	
CURRENT ASSETS	
Cash and cash equivalents	$ 6,856,000
Investments	6,662,000
Trade receivables, less allowance for doubtful accounts of $9,000	510,000
Inventories	865,000
Other current assets	68,000
Total current assets	14,961,000
Property and equipment, net	1,362,000
TOTAL ASSETS	$ 16,323,000
LIABILITIES AND STOCKHOLDERS EQUITY	
LIABILITIES	
Accounts payable	$ 109,000
Accrued expenses	253,000
Deferred revenue	50,000
Income taxes payable	110,000
Deferred income tax	2,374,000
TOTAL LIABILITIES	$ 2,896,000
STOCKHOLDERS EQUITY	
Common stock par value $0.10 per share; authorized 10,000,000 shares; issued 3,241,016	324,000
Additional paid-in capital	1,158,000
Retained earnings	7,937,000
Accumulated other comprehensive income	4,008,000
TOTAL STOCKHOLDERS EQUITY	13,427,000

	September 30, 2005 (unaudited)
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 16,323,000

See accompanying notes to consolidated financial statements

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ELECTRO-SENSORS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended September 30, 2005	Three Months Ended September 30, 2004	Nine Months Ended September 30, 2005	Nine Months Ended September 30, 2004
Net sales	$ 1,206,000	$ 1,243,000	$ 3,557,000	$ 3,664,000
Cost of goods sold	470,000	453,000	1,368,000	1,368,000
Gross profit	736,000	790,000	2,189,000	2,296,000
Operating expenses:				
Selling and marketing	318,000	341,000	938,000	968,000
General and administrative	246,000	254,000	833,000	775,000
Research and development	205,000	206,000	624,000	566,000
Total operating expenses	769,000	801,000	2,395,000	2,309,000
Operating loss	(33,000)	(11,000)	(206,000)	(13,000)
Non-operating income (expense):				
Gain (loss) on sale of investment securities	543,000	(1,000)	807,000	425,000
Interest income	52,000	19,000	125,000	43,000
Other income	3,000	2,000	11,000	9,000
Equity in losses of equity method investee	(129,000)	(40,000)	(140,000)	(165,000)
Total non-operating income (loss)	469,000	(20,000)	803,000	312,000
Income (loss) before income taxes	436,000	(31,000)	597,000	299,000
Federal and state income tax provision	175,000	4,000	237,000	187,000

	Three Months Ended September 30,		Nine Months Ended September 30,	
Net income (loss)	$ 261,000	$ (35,000)	$ 360,000	$ 112,000
Net income per share data:				
Basic				
Net income (loss) per share	$ 0.08	$ (0.01)	$ 0.11	$ 0.03
Weighted average shares	3,234,472	3,218,009	3,227,136	3,202,089
Diluted				
Net income (loss) per share	$ 0.08	$ (0.01)	$ 0.11	$ 0.03
Weighted average shares	3,330,726	3,326,575	3,327,822	3,312,835
Dividends paid per share	$ 0.04	$ 0.04	$ 0.12	$ 0.12

See accompanying notes to consolidated financial statements

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ELECTRO-SENSORS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30, 2005	Nine Months Ended September 30, 2004
Cash flows from operating activities		
Net income	$ 360,000	$ 112,000
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation	75,000	68,000
Realized gain on sale of investments	(807,000)	(426,000)
Equity in loss of equity method investee	140,000	165,000
(Increase)/decrease in:		
Trade receivables	49,000	(60,000)
Inventory	(55,000)	(46,000)
Other current assets	0	(2,000)
Prepaid income taxes	127,000	(53,000)
Increase/(decrease) in:		
Accounts payable	(53,000)	54,000
Accrued expenses	5,000	45,000
Deferred revenue	(18,000)	7,000
Prepaid income taxes	110,000	(96,000)
Net cash used in operating activities	(67,000)	(232,000)

	Nine Months Ended September 30,	
Cash flows from investing activities:		
Proceeds from sale of investments	825,000	772,000
Purchase of equity securities	0	(326,000)
Payment for purchase of investments	0	(160,000)
Purchase of property and equipment	(35,000)	(21,000)
Net cash provided by investing activities	790,000	265,000
Cash flows from financing activities:		
Proceeds from issuance of stock	56,000	109,000
Dividends paid	(387,000)	(385,000)
Net cash used in financing activities	(331,000)	(276,000)
Net increase/(decrease) in cash & cash equivalents	392,000	(243,000)
Cash & cash equivalents, beginning	6,464,000	6,862,000
Cash & cash equivalents, ending	6,856,000	6,619,000
Supplemental schedule of non-cash investing and financing activities		
Net change in unrealized loss on investments	$ (654,000)	$ (8,461,000)

See accompanying notes to consolidated financial statements

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ELECTRO-SENSORS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Nature of Business

The accompanying consolidated financial statements include the accounts of Electro-Sensors, Inc. and its wholly owned subsidiaries, ESI Investment Company and Senstar Corporation. Senstar Corporation does not have any business transactions. Intercompany accounts, transactions and earnings have been eliminated in consolidation. The consolidated entity is referred to as the Company.

The Company operates two distinct businesses. The first is the Controls Division, which manufactures and markets a complete line of speed monitoring and motor control systems for industrial machinery. The Controls Division utilizes leading-edge technology to continuously improve its products and make them easier to use. The Controls Division s goal is to manufacture the industry-preferred product for every market served. These products are sold through an internal sales staff, manufacturer s representatives, and distributors to a wide variety of manufacturers, OEM s and processors to monitor process machinery operations. The Controls Division markets its products to a number of different industries located throughout the United States and abroad.

The Company s second primary business is AutoData® Systems (ADS). ADS designs and markets a desktop software based system that reads hand printed characters, checkmarks and bar code information from scanned or faxed forms. ADS products are designed to provide capabilities to automate data collection and are sold by internal sales staff to end users, resellers and developers in the United States, Canada, Europe and Asia.

ESI Investment Company (INV) owns marketable securities which have experienced significant appreciation in value since the IPO of August Technology in 2000. August Technology Corporation designs, manufactures, and sells automated defect inspection systems used in the manufacture of microelectronic devices. The Company has recognized income from the sale of its holdings in August Technology Corporation. See Note 6 for additional information regarding its investments. The Company s investments in marketable securities are subject to normal market risks, and are extremely concentrated in one security.

Note 2. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-QSB. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. It is the opinion of management that the unaudited condensed consolidated financial statements include all adjustments, consisting of normal recurring accruals, necessary to fairly state the financial position and results of operations for the three and nine month periods ended September 30, 2005 and September 30, 2004. The results of interim periods may not be indicative of results to be expected for the year.

This report should be read together with the Company s annual report on Form 10-KSB for the year ended December 31, 2004, including the audited financial statements and footnotes therein.

Note 3. Revenue Recognition

Revenue recognition of production monitoring equipment:

All production monitoring equipment is shipped without an evaluation or acceptance period. Revenues from the sale of the products and any related warranty costs are recognized at the time of shipment. The Company s distributors are not granted any price protection. Sales to all customers, including distributors, are final and no right of return after shipment exists.

Software revenue recognition:

The Company recognizes revenue upon shipment of its character recognition software. The product is sold to the end user and risk of loss is transferred, and the Company has no continuing obligations, once its products are delivered to the shipper. The Company recognizes revenue upon shipment, net of return reserves based on historical experience. To recognize revenue, it must also be probable that the Company will collect the accounts receivable from its customers. In some situations, the Company receives advance payments from its customers. Revenue associated with these advance payments is deferred until the product is shipped.

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Note 4. Stock-Based Compensation

In accordance with Accounting Principles Board (APB) Opinion No. 25 and related interpretations, the Company uses the intrinsic value-based method for measuring stock-based compensation cost which measures compensation cost as the excess, if any, of quoted market price of the Company s common stock at the grant date over the amount the employee must pay for the stock. The Company s general policy is to grant stock options at fair value at the date of grant.

Had compensation cost been recognized based on the fair values of options at the grant dates consistent with the provisions of Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock Based Compensation, the Company s net income and basic and diluted net income per common share would have been changed to the following pro forma amounts:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Net income (loss):				
As reported	$ 261,000	$ (35,000)	$ 360,000	$ 112,000
Pro forma	$ 247,000	$ (68,000)	$ 318,000	$ 67,000

	Three Months Ended September 30,		Nine Months Ended September 30,	
Basic net income (loss) per common share:				
As reported	0.08	(0.01)	0.11	0.03
Pro forma	0.08	(0.02)	0.10	0.02
Diluted net income (loss) per common share:				
As reported	0.08	(0.01)	0.11	0.03
Pro forma	0.07	(0.02)	0.10	0.02
Stock based compensation:				
As reported	0	0	0	0
Pro forma	$ 14,000	$ 33,000	$ 42,000	$ 45,000

The company did not grant any options during the nine months ended September 30, 2005. Please read the information in R