

NORTECH SYSTEMS INC
Form 10-Q
May 07, 2014
[Table of Contents](#)

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2014

OR

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

For the transition period from _____ to _____

NORTECH SYSTEMS INCORPORATED

Commission file number 0-13257

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State of Incorporation: **Minnesota**

IRS Employer Identification No. **41-1681094**

Executive Offices: **1120 Wayzata Blvd E., Suite 201, Wayzata, MN 55391**

Telephone number: **(952) 345-2244**

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

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

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

Large Accelerated Filer

Accelerated Filer

Non-accelerated Filer

Smaller Reporting Company

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

Number of shares of \$.01 par value common stock outstanding at May 1, 2014 - 2,742,992

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Table of Contents

TABLE OF CONTENTS

	PAGE
<u>PART I - FINANCIAL INFORMATION</u>	
<u>Item 1</u> :	<u>Financial Statements</u>
	<u>Consolidated Balance Sheets</u> 3
	<u>Consolidated Statements of Income</u> 4
	<u>Consolidated Statements of Cash Flows</u> 5
	<u>Condensed Notes to Consolidated Financial Statements</u> 6-11
<u>Item 2</u> :	<u>Management's Discussion and Analysis of Financial Condition And Results of Operations</u> 11-16
<u>Item 4</u> :	<u>Controls and Procedures</u> 16
<u>PART II - OTHER INFORMATION</u>	
<u>Item 1</u> :	<u>Legal Proceedings</u> 16
<u>Item 6</u> :	<u>Exhibits</u> 17
<u>INDEX TO EXHIBITS</u>	17
<u>SIGNATURES</u>	17

Table of Contents**PART 1****ITEM 1. FINANCIAL STATEMENTS****NORTECH SYSTEMS INCORPORATED AND SUBSIDIARY****CONSOLIDATED BALANCE SHEETS**

	MARCH 31 2014 (Unaudited)	DECEMBER 31 2013
ASSETS		
Current Assets		
Cash	\$ 336,195	\$ 16,030,848
Accounts Receivable, Less Allowance for Uncollectible Accounts	15,409,447	17,427,470
Inventories	18,794,263	634,350
Prepaid Expenses	800,288	140,174
Income Taxes Receivable	86,807	683,000
Deferred Income Taxes	683,000	34,915,842
Total Current Assets	36,110,000	34,915,842
Property and Equipment, Net	11,015,078	11,037,160
Other Assets	121,096	122,419
Total Assets	\$ 47,246,174	\$ 46,075,421
LIABILITIES AND SHAREHOLDERS EQUITY		
Current Liabilities		
Line of Credit	\$ 7,625,468	\$ 7,234,983
Current Maturities of Long-Term Debt	681,961	632,176
Accounts Payable	8,632,089	8,185,012
Accrued Payroll and Commissions	2,671,549	2,595,393
Other Accrued Liabilities	753,336	718,974
Total Current Liabilities	20,364,403	19,366,538
Long-Term Liabilities		
Long-Term Debt, Net of Current Maturities	4,289,085	4,246,914
Deferred Income Taxes	282,000	282,000
Other Long-Term Liabilities	281,599	244,521
Total Long-Term Liabilities	4,852,684	4,773,435
Total Liabilities	25,217,087	24,139,973
Shareholders Equity		
Preferred Stock, \$1 par value; 1,000,000 Shares Authorized: 250,000 Shares Issued and Outstanding	250,000	250,000
Common Stock - \$0.01 par value; 9,000,000 Shares Authorized: 2,742,992 Shares Issued and Outstanding	27,430	27,430
Additional Paid-In Capital	15,745,715	15,738,233
Accumulated Other Comprehensive Loss	(62,936)	(62,936)
Retained Earnings	6,068,878	5,982,721
Total Shareholders Equity	22,029,087	21,935,448

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Total Liabilities and Shareholders	Equity	\$	47,246,174	\$	46,075,421
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See Accompanying Condensed Notes to Consolidated Financial Statements

Table of Contents

NORTECH SYSTEMS INCORPORATED AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

	THREE MONTHS ENDED MARCH 31	
	2014	2013
Net Sales	\$ 26,149,142	\$ 25,925,401
Cost of Goods Sold	23,075,207	22,687,976
Gross Profit	3,073,935	3,237,425
Operating Expenses		
Selling Expenses	1,120,901	1,196,740
General and Administrative Expenses	1,716,813	1,817,063
Total Operating Expenses	2,837,714	3,013,803
Income From Operations	236,221	223,622
Other Expense		
Interest Expense	(89,980)	(93,526)
Miscellaneous Income (Expense), net	(10,084)	(10,007)
Total Other Expense	(100,064)	(103,533)
Income Before Income Taxes	136,157	120,089
Income Tax Expense (benefit)	50,000	(21,000)
Net Income	\$ 86,157	\$ 141,089
Earnings Per Common Share:		
Basic	\$ 0.03	\$ 0.05
Weighted Average Number of Common Shares Outstanding Used for Basic Earnings Per Common Share	2,742,992	2,742,992
Diluted	\$ 0.03	\$ 0.05
Weighted Average Number of Common Shares Outstanding Plus Effect of Dilutive Common Stock Options	2,747,858	2,742,992

See Accompanying Condensed Notes to Consolidated Financial Statements

Table of Contents

NORTECH SYSTEMS INCORPORATED AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	THREE MONTHS ENDED	
	2014	2013
MARCH 31		
Cash Flows From Operating Activities		
Net Income	\$ 86,157	\$ 141,089
Adjustments to Reconcile Net Income to Net Cash Provided by (Used in) Operating Activities:		
Depreciation	497,350	509,370
Amortization	1,323	1,323
Compensation on Stock-Based Awards	7,482	3,781
Impairment on Assets	1,150	74,003
Deferred Taxes		(65,000)
Changes in Current Operating Items		
Accounts Receivable	621,401	(438,792)
Inventories	(1,366,793)	(1,452,540)
Prepaid Expenses	(165,938)	(115,941)
Income Taxes Receivable	53,367	
Income Taxes Payable		(81,364)
Accounts Payable	640,234	206,112
Accrued Payroll and Commissions	76,156	804,834
Other Accrued Liabilities	71,528	(5,397)
Net Cash Provided by (Used in) Operating Activities	523,417	(418,522)
Cash Flows from Investing Activities:		
Purchases of Property and Equipment	(669,663)	(201,573)
Net Cash Used in Investing Activities	(669,663)	(201,573)
Cash Flows from Financing Activities:		
Net Borrowings (Repayments) on Line of Credit	390,485	(923,508)
Proceeds from Long-Term Debt	230,000	1,674,000
Principal Payments on Long-Term Debt	(138,044)	(111,876)
Net Cash Provided by Financing Activities	482,441	638,616
Net Increase in Cash	336,195	18,521
Cash - Beginning		
Cash - Ending	\$ 336,195	\$ 18,521
Supplemental Disclosure of Cash Flow Information:		
Cash Paid During the Period for Interest	\$ 87,159	\$ 77,848
Cash Paid During the Period for Income Taxes	100	101,000
Supplemental Noncash Investing and Financing Activities		
Capital Expenditures in Accounts Payable	124,749	10,676

See Accompanying Condensed Notes to Consolidated Financial Statements

Table of Contents

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited consolidated financial statements for the interim periods have been prepared in accordance with Generally Accepted Accounting Principles in the United States of America (GAAP) for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the financial information and footnotes required by GAAP for complete financial statements, although we believe the disclosures are adequate to make the information presented not misleading. It is suggested that these consolidated financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in our latest shareholders' annual report on Form 10-K. The operating results for the interim periods presented are not necessarily indicative of the results expected for the full year or for any other interim period. In our opinion, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included.

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. In preparing these consolidated financial statements, we have made our best estimates and judgments of certain amounts included in the consolidated financial statements, giving due consideration to materiality. Changes in the estimates and assumptions used by us could have a significant impact on our financial results, since actual results could differ from those estimates.

Principles of Consolidation

The consolidated financial statements include the accounts of Nortech Systems Incorporated and its wholly owned subsidiary, Manufacturing Assembly Solutions of Monterrey, Inc. All significant intercompany accounts and transactions have been eliminated.

Revenue Recognition

We recognize revenue upon shipment of manufactured products to customers, when title has passed, all contractual obligations have been satisfied and collection of the resulting receivable is reasonably assured. We also provide engineering services separate from the manufacture of a product. Revenue for engineering services is recognized upon completion of the engineering process, providing standalone fair value to our customers. Our engineering services are short-term in nature. In addition, we have another separate source of revenue that comes from short-term repair services, which are recognized upon completion of the repairs and shipment of product back to the customer.

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Shipping and handling costs charged to our customers are included in net sales, while the corresponding shipping expenses are included in cost of goods sold.

Table of Contents**Stock Options**

Following is the status of all stock options outstanding as of March 31, 2014:

	Shares	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Outstanding - December 31, 2013	216,000	\$ 6.46		
Granted				
Cancelled				
Outstanding - March 31, 2014	216,000	\$ 6.46	3.33	\$ 48,953
Exercisable - March 31, 2014	192,918	\$ 6.77	2.65	\$ 16,320

There were no options exercised during the three months ended March 31, 2014 and 2013. The weighted-average fair value of options granted during the three months ended March 31, 2013 was \$1.65 per share. There were no stock options granted during the three months ended March 31, 2014.

Total compensation expense related to stock options for the three months ended March 31, 2014 and 2013 was \$7,482 and \$3,781, respectively. As of March 31, 2014, there was approximately \$39,000 of unrecognized compensation related to unvested option awards that we expect to recognize over a weighted-average period of 1.68 years.

Equity Appreciation Rights Plan

In November 2010, the Board of Directors approved the adoption of the Nortech Systems Incorporated Equity Appreciation Rights Plan (the 2010 Plan). The total number of Equity Appreciation Right Units (Units) the Plan can issue shall not exceed an aggregate of 750,000 Units. The 2010 Plan provides that Units issued shall fully vest three years from the base date as defined in the agreement unless terminated earlier. Units give the holder a right to receive a cash payment equal to the appreciation in book value per share of common stock from the base date, as defined, to the redemption date. Unit redemption payments under this plan shall be paid in cash within 90 days after we determine the value as of the redemption date.

As of March 31, 2014, we had granted all 750,000 Units and 650,000 remain outstanding with vesting dates ranging from December 31, 2014 through December 31, 2019.

Total compensation expense related to these Units based on the estimated appreciation over their remaining terms was approximately \$43,000 and \$14,000 for the three months ended March 31, 2014 and 2013, respectively.

Table of Contents

As of March 31, 2014 and December 31, 2013, approximately \$124,000 and \$81,000 have been accrued under this plan, respectively. As of March 31, 2014, approximately \$35,000 of this balance was included in Other Accrued Liabilities and the remaining \$89,000 balance was included in Other Long-term Liabilities. As of December 31, 2013, approximately \$29,000 of this balance is included in Other Accrued Liabilities and the remaining \$52,000 was included in Other Long-term Liabilities.

Earnings per Common Share

For the three months ended March 31, 2013, the effect of all stock options is antidilutive. Therefore, no outstanding options were included in the computation of per-share amounts. For the three months ended March 31, 2014, 26,750 stock options were included in the computation of diluted per share amounts as their impact is dilutive. For the three months ended March 31, 2014, stock options of 189,250 were excluded because their inclusion would be antidilutive.

Segment Reporting Information