

NORTECH SYSTEMS INC
Form 10-Q
August 12, 2010
[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 June 30, 2010

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

Edgar Filing: NORTECH SYSTEMS INC - Form 10-Q

Commission file number **0-13257**

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 July 29, 2010 - 2,742,992

(The remainder of this page was intentionally left blank.)

Table of Contents

TABLE OF CONTENTS

	PAGE
<u>PART I FINANCIAL INFORMATION</u>	
<u>Item 1 Financial Statements</u>	
<u>Consolidated Balance Sheets</u>	3 - 4
<u>Consolidated Statements of Income</u>	5 - 6
<u>Consolidated Statements of Cash Flows</u>	7
<u>Condensed Notes to Consolidated Financial Statements</u>	8-13
<u>Item 2 Management's Discussion and Analysis of Financial Condition And Results of Operations</u>	13-18
<u>Item 4 Controls and Procedures</u>	18
<u>PART II OTHER INFORMATION</u>	
<u>Item 1 Legal Proceedings</u>	19
<u>Item 6 Exhibits</u>	19
<u>SIGNATURES</u>	20
Exhibit 10.6	
Exhibit 31.1	
Exhibit 31.2	
Exhibit 32.1	
Exhibit 32.2	

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

ASSETS	JUNE 30 2010 (Unaudited)	DECEMBER 31 2009
Current Assets		
Cash and Cash Equivalents	\$ 722,314	\$ 245,381
Accounts Receivable, Less Allowance for Uncollectible Accounts	14,352,640	12,021,378
Inventories	17,970,715	15,806,669
Prepaid Expenses	449,756	542,643
Income Taxes Receivable	2,338,435	2,515,906
Deferred Income Taxes	867,000	753,000
Total Current Assets	36,700,860	31,884,977
Property and Equipment, Net	7,776,376	8,239,161
Finite Life Intangible Assets, Net of Accumulated Amortization	272,452	343,549
Deferred Income Taxes	210,000	348,000
Other Assets	313,518	313,518
Total Assets	\$ 45,273,206	\$ 41,129,205

See Accompanying Condensed Notes to Consolidated Financial Statements

Table of Contents

NORTECH SYSTEMS INCORPORATED AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

LIABILITIES AND SHAREHOLDERS EQUITY	JUNE 30 2010 (Unaudited)	DECEMBER 31 2009
Current Liabilities		
Line of Credit	\$ 6,792,610	\$ 5,490,607
Current Maturities of Long-Term Debt	1,077,081	1,013,920
Accounts Payable	10,975,877	9,050,684
Accrued Payroll and Commissions	3,029,637	1,449,528
Accrued Health and Dental Claims	375,000	310,000
Other Accrued Liabilities	966,993	1,354,438
Total Current Liabilities	23,217,198	18,669,177
Long-Term Liabilities		
Long-Term Debt, Net of Current Maturities	2,930,945	3,572,264
Other Long-Term Liabilities	129,008	160,912
Total Long-Term Liabilities	3,059,953	3,733,176
Total Liabilities	26,277,151	22,402,353
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 and 2,738,992 Shares Issued and Outstanding at June 30, 2010 and December 31, 2009, respectively	27,430	27,390
Additional Paid-In Capital	15,682,484	15,654,160
Accumulated Other Comprehensive Loss	(75,466)	(73,909)
Retained Earnings	3,111,607	2,869,211
Total Shareholders Equity	18,996,055	18,726,852
Total Liabilities and Shareholders Equity	\$ 45,273,206	\$ 41,129,205

See Accompanying Condensed Notes to Consolidated Financial Statements

Table of Contents

NORTECH SYSTEMS INCORPORATED AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

	THREE MONTHS ENDED	
	2010	2009
	JUNE 30	
Net Sales	\$ 24,694,506	\$ 19,891,110
Cost of Goods Sold	21,583,889	18,790,455
Gross Profit	3,110,617	1,100,655
Operating Expenses:		
Selling Expenses	765,502	1,125,744
General and Administrative Expenses	1,860,145	1,549,943
Restructuring and Impairment Charges		645,118
Total Operating Expenses	2,625,647	3,320,805
Income (Loss) From Operations	484,970	(2,220,150)
Other Income (Expense)		
Interest Expense	(100,550)	(140,170)
Miscellaneous Income (Expense), net	7,692	(53,462)
Total Other Expense	(92,858)	(193,632)
Income (Loss) Before Income Taxes	392,112	(2,413,782)
Income Tax Expense (Benefit)	245,000	(867,000)
Net Income (Loss)	\$ 147,112	\$ (1,546,782)
Earnings (Loss) Per Common Share:		
Basic and Diluted	\$ 0.05	\$ (0.56)
Weighted Average Number of Common Shares Outstanding Used for Basic and Diluted		
Earnings (Loss) Per Common Share	2,742,992	2,738,989

See Accompanying Condensed Notes to Consolidated Financial Statements

Table of Contents

NORTECH SYSTEMS INCORPORATED AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

	SIX MONTHS ENDED JUNE 30	
	2010	2009
Net Sales	\$ 46,435,947	\$ 41,441,746
Cost of Goods Sold	40,685,662	39,510,527
Gross Profit	5,750,285	1,931,219
Operating Expenses:		
Selling Expenses	1,520,924	2,538,335
General and Administrative Expenses	3,418,609	3,090,956
Restructuring and Impairment Charges		645,118
Total Operating Expenses	4,939,533	6,274,409
Income (Loss) From Operations	810,752	(4,343,190)
Other Income (Expense)		
Interest Expense	(226,075)	(235,276)
Miscellaneous Expense, net	(37,281)	(43,534)
Total Other Expense	(263,356)	(278,810)
Income (Loss) Before Income Taxes	547,396	(4,622,000)
Income Tax Expense (Benefit)	305,000	(1,786,000)
Net Income (Loss)	\$ 242,396	\$ (2,836,000)
Earnings (Loss) Per Common Share:		
Basic and Diluted	\$ 0.09	\$ (1.04)
Weighted Average Number of Common Shares Outstanding Used for Basic and Diluted		
Earnings (Loss) Per Common Share	2,741,777	2,738,972

See Accompanying Condensed Notes to Consolidated Financial Statements

Table of Contents

NORTECH SYSTEMS INCORPORATED AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	SIX MONTHS ENDED	
	2010	2009
	JUNE 30	
Cash Flows From Operating Activities		
Net Income (Loss)	\$ 242,396	\$ (2,836,000)
Adjustments to Reconcile Net Income (Loss) to Net Cash Provided by (Used in) Operating Activities:		
Depreciation	797,061	954,088
Amortization	71,097	75,061
Stock-Based Compensation	15,864	62,592
Interest on Swap Valuation	(12,404)	(7,875)
Restructuring Charges		103,307
Property and Equipment Impairment Charges		541,811
Deferred Income Taxes	24,000	(173,000)
Loss on Disposal of Property and Equipment	876	5,733
Foreign Currency Gain	(3,458)	(31,495)
Changes in Current Operating Items, Net of Effects of Business Acquisition		
Accounts Receivable	(2,330,092)	1,159,907
Inventories	(1,861,077)	3,818,667
Prepaid Expenses and Other Assets	93,034	321,483
Income Taxes Receivable	177,501	(1,624,323)
Accounts Payable	1,925,180	(2,932,660)
Accrued Payroll and Commissions	1,579,335	(701,661)
Accrued Health and Dental Claims	65,000	13,898
Other Accrued Liabilities	(407,140)	(522,870)
Net Cash Provided by (Used in) Operating Activities	377,173	(1,773,337)
Cash Flows from Investing Activities:		
Proceeds from Sale of Property and Equipment		100
Business Acquisition	(402,969)	
Purchase of Property and Equipment	(233,651)	(204,266)
Net Cash Used in Investing Activities	(636,620)	(204,166)
Cash Flows from Financing Activities:		
Net Borrowings on Line of Credit	1,302,003	1,992,045
Proceeds from Long-Term Debt		616,397
Principal Payments on Long-Term Debt	(578,158)	(620,339)
Proceeds from Issuance of Common Stock	12,500	132
Net Cash Provided by Financing Activities	736,345	1,988,235
Effect of Exchange Rate Changes on Cash	35	4,657
Net Increase in Cash and Cash Equivalents	476,933	15,389
Cash and Cash Equivalents - Beginning	245,381	803,041
Cash and Cash Equivalents - Ending	\$ 722,314	\$ 818,430
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the period for interest	\$ 237,425	\$ 250,032
Cash paid during the period for income taxes	151,615	502

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. 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 as of June 30, 2010, including changes during the six-month period then ended:

	Shares	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Outstanding - January 1, 2010	736,750	\$ 7.20		
Exercised	(4,000)	\$ 3.13		
Forfeited	(67,500)	\$ 6.27		
Outstanding - June 30, 2010	665,250	\$ 7.32	6.05	\$ 997
Exercisable - June 30, 2010	291,250	\$ 7.37	4.67	\$

The total intrinsic value of options exercised during the three and six months ended June 30, 2010 was \$0 and \$20, respectively. Cash received from option exercises during the three and six months ended June 30, 2010 was \$0 and \$12,500, respectively. There were no options exercised during the three and six months ended June 30, 2009.

Stock Options with Time-Based Vesting

Total compensation expense related to stock options with time-based vesting for the three months ended June 30, 2010 and 2009 was \$7,931 and \$31,296, respectively. Total compensation expense related to stock options with time-based vesting for the six months ended June 30, 2010 and 2009 was \$15,864 and \$62,592, respectively. At June 30, 2010 we had 315,250 time-based options outstanding.

As of June 30, 2010 there was approximately \$43,000 of unrecognized compensation expense related to unvested option awards that we expect to recognize over a weighted-average period of 1.36 years.

Segment Reporting Information

For the three and six months ended June 30, 2010 and 2009 all of our operations fall under the Contract Manufacturing segment within the Electronic Manufacturing Services industry. We strategically direct production between our various manufacturing facilities based on a number of considerations to best meet our customers' requirements. We share resources for sales, marketing, cash and risk management, banking, credit and collections, human resources, payroll, internal control, audit, taxes, SEC reporting and corporate accounting. Consolidated financial information is available that is evaluated regularly by the chief operating decision maker in assessing performance and allocating resources. Export sales represented 5% of consolidated net sales for the three and six months ended June 30, 2010, and 4% of consolidated net sales for the three and six months ended June 30, 2009.

Inventories

Edgar Filing: NORTECH SYSTEMS INC - Form 10-Q

Inventories are stated at the lower of cost (first-in, first-out method) or market (based on the lower of replacement cost or net realizable value). Costs include material, labor, and overhead required in the warehousing and production of our products. Inventory reserves are maintained for the estimated value of the inventories that may have a lower value than stated or quantities in excess of future production needs.

Table of Contents

Inventories are as follows:

	June 30 2010		December 31 2009
Raw materials	\$ 12,510,214	\$	11,137,853
Work in process	3,890,988		3,304,725
Finish goods	2,768,372		2,459,521
Reserve	(1,198,859)		(1,095,430)
Total	\$ 17,970,715	\$	15,806,669

Finite Life Intangible Assets

Finite life intangible assets at June 30, 2010 and December 31, 2009 are as follows:

	June 30, 2010			
	Remaining Lives (Years)	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Bond Issue Costs	11	\$ 79,373	\$ 21,168	\$ 58,205
Customer Base	2	676,557	462,310	214,247
Other Intangibles	0	28,560	28,560	
Totals		\$ 784,490	\$ 512,038	\$ 272,452

December 31, 2009

Remaining Gross