SONO TEK CORP
Form 10-Q
January 14, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: **November 30, 2013**

OR

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

Commission File No.: **0-16035**

(Exact name of registrant as specified in its charter)

New York	**14-1568099**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

2012 Rt. 9W, Milton, NY 12547

(Address of Principal Executive Offices) (Zip Code)

Issuer's telephone no., including area code: **(845) 795-2020**

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 |X| NO |_|

Indicate by checkmark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (section 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). |X | 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 |_| Smaller reporting company |X|

Non Accelerated Filer |_| (Do not check if a 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 |X|

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Class	Outstanding as of January 9, 2014
Common Stock, par value $.01 per share	14,698,312

SONO-TEK CORPORATION

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SONO-TEK CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

	November 30, 2013 (Unaudited)	**February 28, 2013**
ASSETS		
Current Assets:		
Cash and cash equivalents	$2,976,334	$1,940,906
Marketable Securities	955,933	975,910
Accounts receivable (less allowance of $29,00 and $20,000 at November 30 and February 28, respectively)	923,413	941,032
Inventories, net	2,046,574	1,829,171
Prepaid expenses and other current assets	77,757	79,605
Total current assets	6,980,011	5,766,624
Land	250,000	250,000
Buildings, net	2,081,160	2,170,409
Equipment, furnishings and building improvements, net	561,236	683,368
Intangible and other assets, net	115,725	106,022
Deferred tax asset	90,021	90,021
TOTAL ASSETS	$10,078,153	$9,066,444
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	$529,201	$408,738
Accrued expenses	602,429	477,027
Customer deposits	390,879	68,846
Current maturities of long term debt	128,794	125,999
Income taxes payable	179,398	6,331
Total current liabilities	1,830,701	1,086,941
Long term debt, less current maturities	1,890,424	1,987,236
Total liabilities	3,721,125	3,074,177
Commitments and Contingencies	—	—
Stockholders' Equity		
Common stock, $.01 par value; 25,000,000 shares authorized, 14,508,632 and 14,503,010 shares issued and outstanding, at November 30 and February 28, respectively	145,086	145,030
Additional paid-in capital	8,723,882	8,709,601
Accumulated deficit	(2,511,940)	(2,862,364)

Total stockholders' equity	6,357,028	5,992,267
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$10,078,153	$9,066,444

See notes to condensed consolidated financial statements.

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SONO-TEK CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

	Nine Months Ended November 30 Unaudited		**Three Months Ended November 30 Unaudited**	
	2013	**2012**	**2013**	**2012**
Net Sales	$ 7,561,998	$ 7,433,215	$ 2,650,225	$ 2,202,406
Cost of Goods Sold	3,963,181	3,836,511	1,435,055	1,120,772
Gross Profit	3,598,817	3,596,704	1,215,170	1,081,634
Operating Expenses				
Research and product development costs	661,975	699,780	204,738	212,993
Marketing and selling expenses	1,451,310	1,709,342	462,685	503,619
General and administrative costs	747,896	963,242	225,301	288,854
Rental operations expense	118,890	86,437	48,791	28,807
Total Operating Expenses	2,980,071	3,458,801	941,515	1,034,273
Operating Income	618,746	137,903	273,655	47,361
Interest Expense	(82,396)	(86,012)	(27,152)	(28,364)
Other (expense) income	(5,405)	18,168	18,169	19,873
Income from Operations Before Income Taxes	530,945	70,059	264,672	38,870
Income Tax (Benefit) Expense	180,521	(26,042)	93,425	13,605
Net Income	$ 350,424	$ 96,101	$ 171,247	$ 25,265
Basic Earnings Per Share	$ 0.02	$ 0.01	$ 0.01	$ 0.00
Diluted Earnings Per Share	$ 0.02	$ 0.01	$ 0.01	$ 0.00
Weighted Average Shares - Basic	14,504,836	14,478,044	14,508,507	14,500,592
Weighted Average Shares - Diluted	14,710,838	14,581,386	14,775,422	14,576,211

See notes to condensed consolidated financial statements.

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SONO-TEK CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended November 30, Unaudited	
	2013	**2012**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	$ 350,424	$ 96,101
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	243,869	265,428
Stock based compensation expense	14,127	48,934
Allowance for doubtful accounts	9,000	(6,620)
Inventory reserve	63,343	48,000
Write off of impaired acquisition costs	15,020	—
Decrease (Increase) in:		
Accounts receivable	8,619	(312,190)
Inventories	(280,746)	215,694
Prepaid expenses and other current assets	1,848	47,867
(Decrease) Increase in:		
Accounts payable and accrued expenses	245,865	(54,387)
Customer Deposits	322,033	(193,415)
Income Taxes Payable	173,067	12,002
Net Cash Provided by Operating Activities	1,166,469	167,414
CASH FLOW FROM INVESTING ACTIVITIES:		
Patent application and other asset costs	(18,421)	(32,218)
Purchase of equipment and furnishings	(77,321)	(142,833)
Proceeds from sale of equipment	38,531	—
Sale (Purchase) of marketable securities	19,977	(721,679)
Net Cash (Used in) Investing Activities	(37,234)	(896,730)
CASH FLOW FROM FINANCING ACTIVITIES:		
Proceeds from exercise of stock options	210	25,346
Repayments of notes payable and loans	(94,017)	(90,416)
Net Cash (Used In) Financing Activities	(93,807)	(65,070)
NET INCREASE (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	1,035,428	(794,386)
CASH AND CASH EQUIVALENTS		
Beginning of period	1,940,906	2,531,689
End of period	$ 2,976,334	$ 1,737,303

SUPPLEMENTAL DISCLOSURE:		
Interest paid	$ 82,396	$ 86,012
Taxes Paid	$ —	$ —

See notes to condensed consolidated financial statements.

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SONO-TEK CORPORATION

Notes to Condensed Consolidated Financial Statements

Six Months Ended November 30, 2013 and 2012

NOTE 1: SIGNIFICANT ACCOUNTING POLICIES

Consolidation - The accompanying condensed consolidated financial statements of Sono-Tek Corporation, a New York corporation (the "Company"), include the accounts of the Company and its wholly owned subsidiaries, Sono-Tek Cleaning Systems Inc. and Sono-Tek Industrial Park, LLC. Sono-Tek Cleaning Systems, Inc., a New Jersey Corporation, ceased operations during the Fiscal Year Ended February 28, 2002. Sono-Tek Industrial Park, LLC operates as a real estate holding company for the Company's real estate operations.

***Cash and Cash Equivalents* –** Cash and cash equivalents consist of money market mutual funds, short term commercial paper and short-term certificates of deposit with original maturities of 90 days or less.

***Fair Value of Financial Instruments* -** The Company adopted the guidance in the Fair Value Measurements and Disclosure Topic of the Accounting Standards Codification for assets and liabilities measured at fair value on a recurring basis. This guidance establishes a common definition for fair value to be applied to existing generally accepted accounting principles that require the use of fair value measurements, establishes a framework for measuring fair value and expands disclosure about such fair value measurements. The adoption of this guidance did not have an impact on the Company's financial position or operating results, but did expand certain disclosures. The guidance defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Additionally, the guidance requires the use of valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. These inputs are prioritized below:

Level 1: Quoted prices in active markets.

Level 2: Observable market-based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs for which there is little or no market data, which require the use of the reporting entity's own assumptions.

The fair values of financial assets of the Company were determined using the following categories at November 30, 2013:

	Quoted Prices in Active Markets (Level 1)	
	November 30, 2013	**February 28, 2013**
Marketable Securities	$955,933	$975,910

Marketable Securities include mutual funds of $955,933, that are considered to be highly liquid and easily tradeable as of November 30, 2013. These securities are valued using inputs observable in active markets for identical securities and are therefore classified as Level 1 within the Company’s fair value hierarchy.

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Interim Reporting - The attached summary condensed consolidated financial information does not include all disclosures required to be included in a complete set of financial statements prepared in conformity with accounting principles generally accepted in the United States of America. Such disclosures were included with the financial statements of the Company at February 28, 2013, and included in its report on Form 10-K. Such statements should be read in conjunction with the data herein.

The financial information reflects all adjustments, normal and recurring, which, in the opinion of management, are necessary for a fair presentation of the results for the interim periods presented. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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. Actual results could differ from those estimates. The results for such interim periods are not necessarily indicative of the results to be expected for the year.

Intangible Assets – Include cost of patent applications that are deferred and charged to operations over seventeen years for domestic patents and twelve years for foreign patents. The accumulated amortization is $103,203 and $95,634 at November 30, 2013 and February 28, 2013, respectively. Annual amortization expense of such intangible assets is expected to be $9,600 per year for the next five years.

Reclassifications – Certain reclassifications have been made to the prior period to conform to the presentations of the current period.

Impact of New Accounting Pronouncements - All new accounting pronouncements issued but not yet effective have been deemed to be not applicable to the Company. Hence, the adoption of these new accounting pronouncements once effective are not expected to have any impact on the Company.

In July 2013, the FASB issued Accounting Standards Update “ASU” 2013-11 on “Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists”. The amendments in this ASU are to improve the current U.S. GAAP because they are expected to reduce diversity in practice by providing guidance on the presentation of unrecognized tax benefits and will better reflect the manner in which an entity would settle at the reporting date any additional income taxes that would result from the disallowance of a tax position when net operating loss carryforwards, similar tax losses, or tax credit carryforwards exist. The amendments in this Update are effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. For nonpublic entities, the amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2014. Early adoption is permitted. The amendments should be applied prospectively to all unrecognized tax benefits that exist at the effective date. Retrospective application is permitted.

NOTE 2: INVENTORIES

Inventories consist of the following:

	November 30, 2013	**February 28, 2013**
Finished goods	$673,780	$561,298
Work in process	516,795	385,092
Consignment	8,943	9,728
Raw materials and subassemblies	1,110,838	1,073,492
Total	2,310,356	2,029,610
Less: Allowance	(263,782)	(200,439)
Net inventories	$2,046,574	$1,829,171

NOTE 3: STOCK OPTIONS AND WARRANTS

Stock Options - Under the 2003 Stock Incentive Plan, as amended ("2003 Plan"), until May 2013, options were available to be granted to officers, directors, consultants and employees of the Company and its subsidiaries to purchase up to 1,500,000 of the Company's common shares. As of November 30, 2013, there were 1,298,436 options outstanding under the 2003 plan, under which no additional options may be granted.

In August 2013, the Company’s shareholders approved the 2013 Stock Incentive Plan under which 2,500,000 options may be granted. No options have been granted to date.

NOTE 4: STOCK BASED COMPENSATION

The weighted-average fair value of options has been estimated on the date of grant using the Black-Scholes options-pricing model. For the nine months ended November 30, 2013 no options were issued.

In computing the impact, the fair value of each option is estimated on the date of grant based on the Black-Scholes options-pricing model utilizing certain assumptions for a risk free interest rate; volatility; and expected remaining lives of the awards. The assumptions used in calculating the fair value of share-based payment awards represent management's best estimates, but these estimates involve inherent uncertainties and the application of management judgment. As a result, if factors change and the Company uses different assumptions, the Company's stock-based compensation expense could be materially different in the future. In addition, the Company is required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. In estimating the Company's forfeiture rate, the Company analyzed its historical forfeiture rate, the remaining lives of unvested options, and the number of vested options as a percentage of total options outstanding. If the Company's actual forfeiture rate is materially different from its estimate, or if the Company reevaluates the forfeiture rate in the future, the stock-based compensation expense could be significantly different from what the Company has recorded in the current period.

For the nine months ended November 30, 2013 and 2012, net income and earnings per share reflect the actual deduction for stock-based compensation expense. The impact of applying ASC 718 approximated $14,127 and $48,934 in additional compensation expense during the nine months ended November 30, 2013 and 2012, respectively. Such amounts are included in general and administrative expenses on the statement of operations. The expense for stock-based compensation is a non-cash expense item.

NOTE 5: EARNINGS PER SHARE

The denominator for the calculation of diluted earnings per share at November 30, 2013 and 2012 are calculated as follows:

	Nine Months Ended November 30,		**Three Months Ended November 30,**	
	2013	**2012**	**2013**	**2012**
Denominator for basic earnings per share	14,504,836	14,478,044	14,508,507	14,500,592
Dilutive effect of stock options	206,003	103,342	266,915	75,618
Denominator for diluted earnings per share	14,710,838	14,581,386	14,775,422	14,576,211

NOTE 6: LONG TERM DEBT

Long-term debt consists of the following:

	November 30, 2013	**February 28,**
Note payable, individual, collateralized by land and buildings, payable in monthly installments of principal and interest of $14,446 through January 2031. Interest rate 5.5%. 20 year term.	$1,923,075	$1,972,617
Equipment loan, bank, collateralized by related office equipment, payable in monthly installments of principal and interest of $5,154 through June 2015. Interest rate 2.12%. 48 month term.	96,143	140,618
Total long term debt	2,019,218	2,113,235
Due within one year	128,794	125,999
Due after one year	$1,890,424	$1,987,236

NOTE 7: REVOLVING LINE OF CREDIT

The Company has a $750,000 revolving line of credit at prime which was 3.25% at November 30, 2013. The loan is collateralized by all of the assets of the Company, except for the land and buildings. The line of credit is payable on demand and must be retired for a 30 day period once annually. If the Company fails to perform the 30 day annual pay down or if the bank elects to terminate the credit line, the bank may at its option convert the outstanding balance to a 36 month term note with payments including interest in 36 equal installments. As of November 30, 2013, the Company’s outstanding balance was $0, and the unused credit line was $750,000.

NOTE 8: SEGMENT INFORMATION

The Company operates in two segments: ultrasonic spraying systems and rental real estate operations.