

BUTLER NATIONAL CORP  
Form 10-Q  
December 13, 2012

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

FORM 10-Q

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

For the quarterly period ended October 31, 2012

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 0-1678

BUTLER NATIONAL CORPORATION  
(Exact name of registrant as specified in its charter)

Kansas  
(State or other jurisdiction of incorporation or organization)

41-0834293  
(I.R.S. Employer Identification No.)

19920 West 161st Street, Olathe, Kansas 66062  
(Address of principal executive offices)(Zip Code)

Registrant's telephone number, including area code: (913) 780-9595

Former name, former address and former fiscal year if changed since last report:  
Not Applicable

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 twelve 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 Regulation 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 definition of "large accelerated filer," "accelerated filer" and "smaller reporting

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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

The number of shares outstanding of the Registrant's Common Stock, \$0.01 par value, as of December 3, 2012 was 58,142,914 shares.

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BUTLER NATIONAL CORPORATION AND SUBSIDIARIES

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BUTLER NATIONAL CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS  
As of October 31, 2012 and April 30, 2012  
(in thousands except per share data)  
(unaudited)

	October 31, 2012	April 30, 2012
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash	\$ 7,031	\$ 7,431
Accounts receivable	2,847	3,589
Inventories		
Raw materials	6,211	6,305
Work in process	1,085	982
Finished goods	292	424
Total inventory	7,588	7,711
Prepaid expenses and other current assets	2,050	1,493
Total current assets	19,516	20,224
<b>PROPERTY, PLANT AND EQUIPMENT:</b>		
Land and building	3,946	3,946
Aircraft	6,673	6,288
Machinery and equipment	3,714	3,714
Office furniture and fixtures	3,068	3,217
Construction in progress	6,711	-
	24,112	17,165
Accumulated depreciation	(7,880)	(6,688)
Total property, plant and equipment	16,232	10,477
<b>SUPPLEMENTAL TYPE CERTIFICATES (net of amortization of \$2,562 at</b>		
<b>October 31, 2012 and \$2,500 at April 30, 2012)</b>	<b>1,621</b>	<b>1,677</b>
<b>OTHER ASSETS:</b>		
Deferred tax asset	1,167	1,167
Other assets (net of accumulated amortization of \$803 at October 31, 2012 and \$538 at April 30, 2012)	6,752	7,017
Total other assets	7,919	8,184
Total Assets	\$ 45,288	\$ 40,562
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Line of credit	\$ 902	\$ 462
Current maturities of long-term debt and capital lease obligations	4,958	3,757
Accounts payable	1,760	1,169
Customer deposits	444	1,015
Gaming facility mandated payment	1,463	1,281
Compensation and compensated absences	963	1,342
Accrued income tax	-	47

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Other	291	207
Total current liabilities	10,781	9,280
<b>LONG-TERM DEBT AND CAPITAL LEASE OBLIGATIONS, NET OF CURRENT MATURITIES:</b>		
	10,624	8,678
Total liabilities	21,405	17,958
<b>COMMITMENTS AND CONTINGENCIES</b>		
<b>STOCKHOLDERS' EQUITY:</b>		
Preferred stock, par value \$5:		
Authorized 50,000,000 shares, all classes		
Designated Classes A and B 200,000 shares		
\$1,000 Class A, 9.8%, cumulative if earned liquidation and redemption value \$100, no shares issued and outstanding	-	-
\$1,000 Class B, 6%, convertible cumulative, liquidation and redemption value \$1,000, no shares issued and outstanding	-	-
Common stock, par value \$.01: Authorized 100,000,000 shares issued and outstanding 58,142,914 shares at October 31, 2012 and 57,907,564 shares at April 30, 2012	581	579
Common stock, owed but not issued 278,573 shares at October 31, 2012 and at April 30, 2012	3	3
Capital contributed in excess of par	12,736	12,568
Treasury stock at cost, 600,000 shares	(732)	(732)
Retained Earnings	8,553	8,170
Total stockholders' equity Butler National Corporation	21,141	20,588
Noncontrolling Interest in BHCMC, LLC	2,742	2,016
Total stockholders' equity	23,883	22,604
Total Liabilities and Stockholders' Equity	\$ 45,288	\$ 40,562

The accompanying notes are an integral part of these financial statements

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BUTLER NATIONAL CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE THREE MONTHS ENDED OCTOBER 31, 2012 AND 2011  
(in thousands, except per share data)  
(unaudited)

	THREE MONTHS ENDED October 31,	
	2012	2011
<b>REVENUES:</b>		
Professional services	\$ 9,170	\$ 9,139
Aerospace products	4,367	5,002
Total revenues	13,537	14,141
<b>COSTS AND EXPENSES:</b>		
Cost of professional services	5,370	5,015
Cost of aerospace products	3,177	2,577
Marketing and advertising	997	2,192
Employee benefits	522	751
Depreciation and amortization	745	473
General, administrative and other	2,027	1,754
Total costs and expenses	12,838	12,762
<b>OPERATING INCOME</b>	<b>699</b>	<b>1,379</b>
<b>OTHER INCOME (EXPENSE):</b>		
Interest expense	(332)	(93)
Other income (expense), net	1	-
Total other income (expense)	(331)	(93)
<b>INCOME BEFORE INCOME TAXES</b>	<b>368</b>	<b>1,286</b>
<b>PROVISION FOR INCOME TAXES</b>	<b>68</b>	<b>306</b>
<b>NET INCOME</b>	<b>300</b>	<b>980</b>
Net income attributable to noncontrolling interest in BHCMC, LLC	(186)	(522)
<b>NET INCOME ATTRIBUTABLE TO BUTLER NATIONAL CORPORATION</b>	<b>\$ 114</b>	<b>\$ 458</b>
<b>BASIC EARNINGS PER COMMON SHARE</b>	<b>\$ .00</b>	<b>\$ .01</b>
<b>WEIGHTED AVERAGE SHARES USED IN PER SHARE CALCULATION</b>	<b>57,546,314</b>	<b>56,594,262</b>
<b>DILUTED EARNINGS PER COMMON SHARE</b>	<b>\$ .00</b>	<b>\$ .01</b>
<b>WEIGHTED AVERAGE SHARES USED IN PER SHARE CALCULATION</b>	<b>57,546,314</b>	<b>56,594,262</b>

The accompanying notes are an integral part of these financial statements



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BUTLER NATIONAL CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE SIX MONTHS ENDED OCTOBER 31, 2012 AND 2011  
(in thousands, except per share data)  
(unaudited)

	SIX MONTHS ENDED	
	October 31,	
	2012	2011
<b>REVENUES:</b>		
Professional services	\$ 18,977	\$ 17,737
Aerospace products	8,028	8,550
Total revenues	27,005	26,287
<b>COSTS AND EXPENSES:</b>		
Cost of professional services	10,507	9,992
Cost of aerospace products	6,101	5,513
Marketing and advertising	2,117	3,137
Employee benefits	1,004	1,509
Depreciation and amortization	1,456	936
General, administrative and other	3,836	3,147
Total costs and expenses	25,021	24,234
<b>OPERATING INCOME</b>	<b>1,984</b>	<b>2,053</b>
<b>OTHER INCOME (EXPENSE):</b>		
Interest expense	(678)	(181)
Other income (expense), net	10	2
Total other income (expense),	(668)	(179)
<b>INCOME BEFORE INCOME TAXES</b>	<b>1,316</b>	<b>1,874</b>
<b>PROVISION FOR INCOME TAXES</b>	<b>208</b>	<b>388</b>
<b>NET INCOME</b>	<b>1,108</b>	<b>1,486</b>
Net income attributable to noncontrolling interest in BHCMC, LLC	(726)	(920)
<b>NET INCOME ATTRIBUTABLE TO BUTLER NATIONAL CORPORATION</b>	<b>\$ 382</b>	<b>\$ 566</b>
<b>BASIC EARNINGS PER COMMON SHARE</b>	<b>\$ .01</b>	<b>\$ .01</b>
<b>WEIGHTED AVERAGE SHARES USED IN PER SHARE CALCULATION</b>	<b>57,546,314</b>	<b>56,594,262</b>
<b>DILUTED EARNINGS PER COMMON SHARE</b>	<b>\$ .01</b>	<b>\$ .01</b>
<b>WEIGHTED AVERAGE SHARES USED IN PER SHARE CALCULATION</b>	<b>57,546,314</b>	<b>56,594,262</b>

The accompanying notes are an integral part of these financial statements





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BUTLER NATIONAL CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE SIX MONTHS ENDING OCTOBER 31, 2012 AND 2011  
(dollars in thousands)  
(unaudited)

	SIX MONTHS ENDED	
	October 31,	
	2012	2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 1,108	\$ 1,486
Adjustments to reconcile cash flows from operating activities		
Depreciation and amortization	1,520	980
Stock issued for services	91	-
Stock options issued to employees and directors	74	251
Changes in assets and liabilities		
Accounts receivable	742	(51)
Inventories	123	(319)
Prepaid expenses and other current assets	(557)	(376)
Accounts payable	591	259
Customer deposits	(571)	(421)
Accrued liabilities	(426)	(888)
Gaming facility mandated payment	182	(666)
Other liabilities	88	42
Cash flows from operating activities	2,965	297
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Capital expenditures	(6,952)	(1,211)
Cash flows from investing activities	(6,952)	(1,211)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Borrowings line of credit, net	440	115
Contributed capital	-	5
Borrowings of promissory notes, long-term debt and capital lease obligations	4,598	728
Repayments of promissory notes, long-term debt and capital lease obligations	(1,451)	(974)
Cash flows from financing activities	3,587	(126)
<b>NET INCREASE (DECREASE) IN CASH</b>	<b>(400)</b>	<b>(1,040)</b>
CASH, beginning of period	7,431	8,475
CASH, end of period	\$ 7,031	\$ 7,435
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>		
Interest paid	\$ 677	\$ 181
Income taxes paid	\$ 783	\$ 634
<b>NON CASH OPERATING ACTIVITY</b>		

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Non cash stock issued for services	\$	91	\$	-
Non cash stock options issued to employees and directors	\$	74	\$	251

The accompanying notes are an integral part of these financial statements

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BUTLER NATIONAL CORPORATION AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(in thousands)  
(unaudited)

1. The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X and do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. Therefore, these financial statements should be read in conjunction with the annual report on Form 10-K for the fiscal year ended April 30, 2012. In our opinion, all adjustments (consisting of normal recurring accruals) necessary for a fair presentation have been included. Operating results for the three and six months ended October 31, 2012 are not indicative of the results of operations that may be expected for the fiscal year ended April 30, 2013.

Certain reclassifications within the condensed financial statement captions have been made to maintain consistency in presentation between years.

2. Net Income (Loss) Per Share: The Company follows ASC 260 that requires the reporting of both basic and diluted earnings (loss) per share. Basic earnings (loss) per share is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings (loss) per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. In accordance with ASC 260, any anti-dilutive effects on net earnings (loss) per share are excluded. Potential common shares as of October 31, 2012 are 65,683,551.

3. Research and Development: We invested in research and development activities. The amount invested in the six months ended October 31, 2012 and 2011 was approximately \$797 and \$779 respectively.

4. Borrowings: At October 31, 2012, the Company had one line of credit totaling \$1 million. The unused line at October 31, 2012 was \$98. During the current year these funds were primarily used for the purchase of inventory for the modifications and avionics operations.

At October 31, 2012, there were several notes collateralized by aircraft security agreements totaling \$2,303. These notes were used for the purchase and modifications of these collateralized aircraft.

There are three notes at a bank totaling \$1,812 for real estate located in Olathe, Kansas and Tempe, Arizona. The due date for these notes is in March 2013, and August 2016.

One note totaling \$339 remains for real estate purchased in June 2009 in Dodge City, Kansas.

One note with a balance of \$330 is collateralized by the first and second position on all assets of the company. There are several other notes collateralized by automobiles and equipment totaling an additional \$169.

One note was entered into with Konami Gaming, Inc. effective August 1, 2012, in the amount of \$1,733. The purchase of the gaming system was installed at Boot Hill Casino in mid-August and has a current remaining balance of \$1,593.

5. Leases: BHCMC, LLC (“BHCMC”) as tenant entered into a lease dated May 1, 2011, and amended via an addendum dated January 1, 2012 (collectively, the “Lease”), with BHC Investment Company, L.C. (“BHCI”) as landlord for a total obligation of \$7,423. BHCI provided funds to BHCMC for the purchase of certain intangible items and gaming related items related to the Boot Hill Casino and Resort. Commencing on January 1, 2012, BHCMC is obligated to make a

minimum payment to BHCI of \$177 per month until September 30, 2017. The remaining balance on the obligation is \$6,536.

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On August 24, 2012, BHCMC and BHCI entered into a second lease (“Second Lease”) of \$2,500 for tenant improvements related to expansion of the Boot Hill Casino and Resort. Commencing on November 1, 2012, BHCMC is obligated to make a minimum payment to BHCI of approximately \$55 per month until November 30, 2017.

6. Other Assets: Other assets include an intangible asset of \$5,500 related to the Kansas Expanded Lottery Act Management Contract privilege fee and JET autopilot intellectual property of \$2,055. BHCMC, LLC expects the intangible assets for the Kansas Expanded Lottery Act contract privilege fee of \$5,500 to have value over the remaining life of the Management Contract with the State of Kansas which will end in December 2024. There is no assurance of Management Contract renewal. The privilege fee will be fully amortized by the projected end of the Management Contract. Based on the projected sales of the Legacy line of “JET” products it was determined that it would be fully amortized within 15 years.

7. Stockholders’ Equity: On May 8, 2012, the Company issued 238,750 shares of Company common stock to Reign Strategy & Investment Group, LLC (“Reign”). The expense will be amortized over the term of the agreement for a total amount of \$91 thousand based on market value at date of issue. These shares were issued in consideration for Reign’s marketing and consulting services related to increasing public awareness and shareholder interest in the Company.

The issuance of stock by the Company to Reign is exempt from registration pursuant to Rule 506 of Regulation D promulgated under the Securities Act of 1933, as amended. Reign has represented to the Company and the Company believes that Reign is an “accredited investor” as defined in Rule 501(a) of Regulation D.

8. Stock Options: Approximately 7.2 million stock options were issued on December 31, 2010. Previously issued stock options were time-vesting and did not include share price performance targets. All of the newly issued stock options expire December 31, 2015.

The exercise price for the incentive stock options is \$0.49 (closing price as of December 31, 2010). The Board of Directors approved the issuance of incentive stock options on December 31, 2010 with the goals of increasing shareholder value, expanding the number of managers participating in the program, and increasing the percentage of compensation tied to share price performance.

The incentive stock options are allocated in three groups with two conditions for vesting. The first condition is stock price and the second condition is time:

Year 1: Target \$0.92

2,420,688 options that can be exercised on or after December 31, 2011 if and when the share price reaches \$0.92

Year 2: Target \$1.41

2,420,688 options that can be exercised on or after December 31, 2012 if and when the share price reaches \$1.41

Year 3: Target \$1.90

2,420,688 options that can be exercised on or after December 31, 2013 if and when the share price reaches \$1.90

At October 31, 2012 we had 7,262,064 outstanding stock options with an average exercise price of \$1.42.

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ITEM MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
2. OPERATIONS

THROUGHOUT THIS ITEM 2 ALL NON TABULAR FINANCIAL RESULTS ARE PRESENTED IN THOUSANDS OF U.S. DOLLARS EXCEPT WHERE MILLIONS OF DOLLARS IS INDICATED.

REFERENCE TO EXHIBIT 99 OF THE COMPANY'S ANNUAL REPORT ON FORM 10-K

Statements made in this report, filed with the Securities and Exchange Commission, communications to stockholders, press releases, and oral statements made by representatives of the Company that are not historical in nature, or that state the Company or management intentions, hopes, beliefs, expectations or predictions of the future, may constitute "forward-looking statements" within the meaning of Section 21E of the Securities and Exchange Act of 1934, as amended (the "Exchange Act"). Forward-looking statements can often be identified by the use of forward-looking terminology, such as "could," "should," "will," "intended," "continue," "believe," "may," "expect," "hope," "anticipate," "goal," "forecast," "plan," "guidance" or "estimate" or the negative of these words, variations thereof or similar expressions. Forward-looking statements are not guarantees of future performance or results. They involve risks, uncertainties, and assumptions. It is important to note that any such performance and actual results, financial condition or business, could differ materially from those expressed in such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in the Cautionary Statements and Risk Factors, filed as Exhibit 99 and Item 1A. Risk Factors to the Company's Annual Report on Form 10-K for the fiscal year ended April 30, 2012 are incorporated herein by reference. Other unforeseen factors not identified herein could also have such an effect. We undertake no obligation to update or revise forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or changes in future operating results, financial condition or business over time.

Management Overview

Management is focused on increasing long-term shareholder value from increased cash generation, earnings growth, and prudently managing capital expenditures. We plan to do this by continuing to drive increased revenue from product and service innovations, strategic acquisitions, and targeted marketing programs.

Our revenue is primarily derived from two very different business segments; aerospace products and professional services. These segments operate through various Butler National Corporation subsidiaries and affiliates listed in the Company's fiscal year 2012 annual report on form 10K.

Aerospace products derives its revenue by designing, engineering, manufacturing, installing, servicing, and repairing products for classic and current production aircraft. These products include JET autopilot service and repairs, AVCON provisions for special mission equipment installations, KINGS avionics equipment sales, service, and installation, and BUTLER National electronic controls and safety equipment manufacture and sales. Aerospace customers range in size from owners and operators of small single engine airplanes to owners and operators of large commercial and military aircraft. Aerospace products are sold to and serviced for customers located in many countries of the world.

Aerospace is the legacy part of the Butler National business. Organized over 50 years ago, this business is based upon design engineering and installation innovations to enhance and support products related to airplanes and ground support equipment. These new products included: in the 1960's, aircraft electronic load sharing and system switching equipment, a number of airplane electronic navigation instruments, radios and transponders; in the 1970's, ground based VOR navigation equipment sold worldwide and GPS equipment as we know it today in civilian use; in the 1980's, special mission modifications to business jets for aerial surveillance and conversion of passenger configurations to cargo; in the 1990's, classic aviation support of aging airplanes with enhanced protection of electrical

systems through transient suppression devices (TSD), control electronics for military weapon systems and improved aerodynamic control products (Avcon Fins) allowing stability at higher gross weights for additional special mission applications; in the 2000's, improved accuracy of the airspeed and altimeter systems to allow less vertical separation between flying airplanes (RVSM) and acquisition of the JET autopilot product line to support and replace aged electronic equipment in the classic fleet of Learjet airplanes; and in the 2010's, the acquisition of Kings Avionics to provide additional classic airplane support by retrofit of avionics from the past 40 years to modern state of the art equipment for sale worldwide using FAA supplemental type certification to make the installations (STC) acceptable to foreign governments for installation abroad.



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Aerospace continues to be a focus for new product design and development. We expect this segment will continue to grow in the future. To address the three to five year business cycles related to the aerospace industry, in the 1990's, we began providing professional services to markets outside the aerospace industry.

Professional services derives its revenue from (a) professional management services in the gaming industry through Butler National Service Corporation ("BNSC") and BHCMC, LLC ("BHCMC"), (b) licensed architectural services to the business community through BCS Design, and (c) monitoring services to owners and operators of intelligence gathering systems through Butler National Services, Inc. ("BNSI").

Professional services grew from the experiences gained from the BNSI monitoring products and services of the 1980's including SCADA systems and products including digital voice technology for the telephone industry and nuclear plant and civil defense warning systems. BNSI sold these professional services and products to utilities and municipalities resulting in relatively stable revenue streams. The defense warning products were sold in the 1980's to a third party leaving only the current BNSI service business in Florida.

In the early 1990's, management determined that more revenue stable business units were needed to sustain the Company. Members of the Board of Directors had contacts with several American Indian tribes, others members were associated with gaming operators in Las Vegas and the 1988 Indian Gaming Regulatory Act (IGRA) which was relatively new to the industry. We reached out to various Indian tribes with land in the area to explore the opportunities for operations under IGRA. This resulted in the "Stables" an Indian owned casino on Modoc Indian land opened in September 1988 developed and managed by BNSC. The Stables Management Agreement has been available on the website maintained by the National Indian Gaming Commission ("NIGC"). The Stables Management Agreement was subsequently amended by various amendments dated April 30, 2003 (the "First Amendment"), November 30, 2006 (the "Second Amendment"), October 19, 2009 (the "Third Amendment") and September 22, 2011 (the "Fourth Amendment"). The result of the First Amendment, Second Amendment, Third Amendment and Fourth Amendment is to provide that twenty (20%) of Net Profits from The Stables are distributed to BNSC, to end per the management agreement the participation of the Miami Indian tribe from the business and to extend the duration of the Stables Management Agreement through September 30, 2018. BCS Design has also assisted with the design, construction and continued refurbishment of this venture.

From this experience with IGRA and the success of the Indian gaming industry, we determined that the IGRA model may be applicable for state owned gaming. We spent Butler National Corporation innovation, legal and market development funds to design and encourage the use of an Indian owned gaming model in the State of Kansas. From these efforts, Kansas enacted the Kansas Expanded Lottery Act (KELA) in 2007 allowing four state owned casinos to be developed in Kansas. In 2007, BNSC made application to manage a state owned casino. In 2008, BNSC was awarded a fifteen year term to manage the Boot Hill Casino and Resort in Dodge City, Kansas pursuant to a Lottery Gaming Facility Management Contract (the "Boot Hill Casino Management Contract"). The Boot Hill Casino Management Contract was amended on December 29, 2009 (the "First Amendment to the Boot Hill Casino Management Contract") to bring the definition of "Fiscal Year" in line with the fiscal year of BNSC (May 1 to April 30). BHCMC was organized to be the manager of the casino in Dodge City. The casino opened in December 2009.

By 2009, Butler National Corporation was clearly established into two segments; the professional services and aerospace products business segments.

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## Results Overview

The six months ending October 31, 2012 revenue increased 3% to \$27.0 million compared to \$26.3 million in the six months ending October 31, 2011. The six month increase in revenue reflects additional professional services revenue (up 7%) driven by increased revenue from gaming activities and a decrease in aerospace products revenue (down 6%). We anticipate future domestic military spending reductions and continued slow growth of the United States economy.

The six months ending October 31, 2012 net income decreased 32.5% to \$382 compared to \$566 in the six months ending October 31, 2011. Diluted earnings per share remained the same at \$0.01 for the six months ending October 31, 2012 and October 31, 2011. We continue focusing on our margin expansion initiatives, including efficiencies in our implementation and operational processes and controlling general and administrative expenses. The six months ending October 31, 2012, operating margin was 7%, a decrease of one percentage point from our margin of 8% in the six months ending October 31, 2011.

## RESULTS OF OPERATIONS

## SIX MONTHS ENDING OCTOBER 31, 2012 COMPARED TO SIX MONTHS ENDING OCTOBER 31, 2011

(dollars in thousands)	Six Months Ended Oct. 31, 2012	Percent of total revenue	Six Months Ended Oct. 31, 2011	Percent of total revenue	Percent Change 2011-2012
Revenues:					
Professional services	\$ 18,977	70%	\$ 17,737	67%	7%
Aerospace products	8,028	30%	8,550	33%	(6)%
<b>Total revenues</b>	<b>27,055</b>	<b>100%</b>	<b>26,287</b>	<b>100%</b>	<b>3%</b>
Costs and expenses:					
Cost of professional services	10,507	39%	9,992	38%	5%
Cost of aerospace products	6,101	23%	5,513	21%	11%
Marketing and advertising	2,117	8%	3,137	12%	(33)%
Employee benefits	1,004	4%	1,509	6%	(33)%
Depreciation and amortization	1,456	5%	936	4%	56%
General, administrative and other	3,836	14%	3,147	12%	22%
<b>Total costs and expenses</b>	<b>25,021</b>	<b>93%</b>	<b>24,234</b>	<b>92%</b>	<b>3%</b>
<b>Operating income</b>	<b>\$ 1,984</b>	<b>7%</b>	<b>\$ 2,053</b>	<b>8%</b>	<b>(3)%</b>

## Revenues:

Revenue increased 3% to \$27.0 million in the six months ended October 31, 2012, as compared to \$26.3 million in the six months ended October 31, 2011.

- Professional services derives its revenue from professional management services in the gaming industry through BNSC and BHCMC, licensed architectural services to the business community through BCS Design and monitoring services to owners and operators of SCADA through BNSI. Revenue from professional services increased 7% to \$19.0 million in the six months ended October 31, 2012 from \$17.7 million in the six months ended October 31, 2011. The increase in professional services revenue was driven by increased revenue from gaming activities.

- Aerospace products derives its revenue by designing, engineering, manufacturing, installing, servicing and repairing products for classic and current production aircraft. Aerospace products revenue decreased 6% for the six months to \$8.0 million at October 31, 2012 compared to \$8.6 million at October 31, 2011. We anticipate future domestic military spending reductions and continued slow growth of the United States economy.

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Costs and expenses:

Costs and expenses related to Professional services and Aerospace products include the cost of engineering, labor, materials, equipment utilization, control systems, security and occupancy.

Costs and expenses increased 3% in the six months ended October 31, 2012 to \$25.0 million compared to \$24.2 million in the six months ended October 31, 2011. Costs and expenses were 93% of total revenue in the six months ended October 31, 2012, as compared to 92% of total revenue in the six months ended October 31, 2011. The increased costs and expenses as a percent of total revenue in the six months ended October 31, 2012 were primarily driven by an increase in labor and material costs.

Marketing and advertising expenses as a percent of total revenue was 8% in the six months ended October 31, 2012, as compared to 12% in six months ended October 31, 2011. These expenses decreased 33% to \$2.1 million in the six months ended October 31, 2012, from \$3.1 million in the six months ended October 31, 2011. Marketing and advertising expenses include advertising, sales and marketing labor, gaming development costs, and casino and product promotions. Boot Hill Casino marketing expenses increased \$405 thousand, however other gaming development expenses decreased. The Boot Hill Casino increase was primarily attributable to growth in the professional services business reflecting a marketing plan to target specific marketing sectors in the Wild West market to increase destination casino revenue. The Boot Hill Casino and Resort definition of the Wild West market includes the area east from the Rocky Mountains to the Mississippi River and the southern Canadian border to the northern border of Mexico.

Employee benefits expenses as a percent of total revenue was 4% in the six months ended October 31, 2012, compared to 6% in the six months ended October 31, 2011. These expenses decreased 33% to \$1.0 million in the six months ended October 31, 2012, from \$1.5 million in the six months ended October 31, 2011. These expenses include the employers' share of all federal, state and local taxes, paid time off for vacation, holidays and illness, employee health and life insurance programs and employer matching contributions to retirement plans. The decreased expenses are related to a decrease in the number of employees in professional services.

Depreciation and amortization expenses as a percent of total revenue was 5% in the six months ended October 31, 2012, compared to 4% in the six months ended October 31, 2011. These expenses increased 56% to \$1.5 million in the six months ended October 31, 2012, from \$936 thousand in the six months ended October 31, 2011. These expenses include depreciation related to owned assets being depreciated over various useful lives and amortization of intangible items including the Kansas privilege fee related to the Boot Hill Casino and Resort being expensed over the term of the gaming contract with the State of Kansas. BHCMC, LLC depreciation and amortization expense for the six months ended October 31, 2012 was \$487 compared to \$20 at October 31, 2011.

General, administrative and other expenses as a percent of total revenue was 14% in the six months ended October 31, 2012, compared to 12% in the six months ended October 31, 2011. These expenses increased 22% to \$3.8 million in fiscal 2012, from \$3.1 million in fiscal 2011. The increase reflects the increase in the number of administrative personnel in professional services, the increased legal fees and expenses and the outside professional consulting fees related to working within the Kansas gaming regulations.

Other income (expense):

Interest and other expenses were \$678 thousand in the six months ended October 31, 2012 compared with interest and other expenses of \$181 thousand in the six months ended October 31, 2011, an increase of \$497 thousand, 275%, from the six months ended October 31, 2011 to the six months ended October 31, 2012. Interest of \$524 thousand was related to obligations of BHCMC, LLC.



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## Operations by Segment

We have two operating segments, professional services and aerospace products. The professional services segment includes revenue contributions and expenditures associated with monitoring services for SCADA systems owned by others, professional architectural services and casino management services. Aerospace products derives its revenue by designing, engineering, manufacturing, installing, servicing and repairing products for classic and current production aircraft.

The following table presents a summary of our operating segment information for the six months ended October 31, 2012 and October 31, 2011:

(dollars in thousands)	Six Months Ended Oct. 31, 2012	Percent of Revenue	Six Months Ended Oct. 31, 2011	Percent of Revenue	Percent Change 2011-2012
Professional Services					
Revenues					
Boot Hill Casino and Resort	\$ 16,584	87%	\$ 15,555	88%	7%
Management/Professional Services	2,393	13%	2,182	12%	10%
Net Revenue	18,977	100%	17,737	100%	7%
Costs of professional services	10,507	55%	9,992	56%	5%
Expenses	6,464	34%	6,622	37%	(2)%
Total costs and expenses	16,971	89%	16,614	94%	2%
Professional services operating income (loss) before noncontrolling interest in BHCMC, LLC	2,006	11%	1,123	6	