ELECTRO SENSORS INC
Form 10QSB
August 14, 2007
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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 June 30, 2007

o TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE

EXCHANGE ACT

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 (State or other jurisdiction of incorporation or organization)	**41-0943459** (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 during the past 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 August 6, 2007 was 3,362,013.

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

ELECTRO-SENSORS, INC.

Form 10-QSB

For the Period Ended June 30, 2007

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PART I – FINANCIAL INFORMATION

Item 1. Condensed Financial Statements

ELECTRO-SENSORS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEET

(unaudited)

	June 30, 2007
ASSETS	
Current assets	
Cash and cash equivalents	$ 5,475,000
Available for sale securities	5,712,000
Trade receivables, less allowance for doubtful accounts of $13,000	690,000
Inventories	1,016,000
Other current assets	58,000
Total current assets	12,951,000
Property and equipment, net	1,271,000
Total assets	$ 14,222,000
LIABILITIES AND STOCKHOLDERS EQUITY	
Current liabilities	
Accounts payable	$ 127,000
Accrued expenses	215,000
Deferred revenue	77,000
Accrued income tax	995,000
Deferred income tax	1,470,000
Total current liabilities	2,884,000
Commitments and contingencies	
Stockholders equity	
Common stock par value $0.10 per share; authorized 10,000,000 shares; issued and outstanding: 3,361,392 shares	336,000
Additional paid-in capital	1,493,000
Retained earnings	6,054,000
Accumulated other comprehensive income (unrealized gain on available for sale securities, net of income tax	3,455,000
Total stockholders equity	11,338,000
Total liabilities and stockholders equity	$ 14,222,000

See accompanying notes to unaudited condensed consolidated financial statements

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ELECTRO-SENSORS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited)

	Three months Ended June 30, 2007	2006	Six months Ended June 30, 2007	2006
Net Sales	**$1,609,000**	$1,427,000	**$3,169,000**	$2,785,000
Cost of Goods Sold	**571,000**	504,000	**1,152,000**	1,019,000
Gross Profit	**1,038,000**	923,000	**2,017,000**	1,766,000
Operating Expenses:				
Selling and Marketing	**331,000**	332,000	**668,000**	641,000
General and Administrative	**286,000**	349,000	**575,000**	680,000
Research and Development	**136,000**	135,000	**290,000**	272,000
Total Operating Expenses	**753,000**	816,000	**1,533,000**	1,593,000
Operating Income	**285,000**	107,000	**484,000**	173,000
Non-operating Income (Expense):				
Gain on Sale of Investment Securities	**0**	45,000	**0**	1,276,000
Interest Income	**74,000**	99,000	**124,000**	172,000
Other Income/(Expense)	**(7,000)**	5,000	**(5,000)**	9,000
Total Non-operating Income	**67,000**	149,000	**119,000**	1,457,000
Income before Income Taxes	**352,000**	256,000	**603,000**	1,630,000
Federal and State Income Tax Provision	**139,000**	101,000	**238,000**	654,000
Net Income	**$213,000**	$155,000	**$365,000**	$976,000
Other Comprehensive Income/(Loss):				
Change in unrealized value of investments, net of income tax	**$(164,000)**	$(554,000)	**$148,000**	$(6,000)
Reclassification adjustment for gains included in Net Income	**0**	(35,000)	**0**	(769,000)
Total Comprehensive Income/(Loss):	**$49,000**	$(434,000)	**$513,000**	$201,000
Net Income per Share Data:				
Basic				
Net Income per Share	**$0.06**	$0.05	**$0.11**	$0.30
Weighted Average Shares	**3,361,392**	3,306,602	**3,361,042**	3,274,793
Diluted				
Net Income per Share	**$0.06**	$0.05	**$0.11**	$0.29
Weighted Average Shares	**3,402,122**	3,330,527	**3,401,661**	3,315,158
Dividends paid per Share	**$.04**	$1.04	**$.08**	$1.08

See accompanying notes to unaudited condensed consolidated financial statements

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ELECTRO-SENSORS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

	Six months Ended June 30, 2007	2006
Cash Flows From Operating Activities		
Net Income	**$365,000**	$976,000
Adjustments to reconcile Net Income to net cash used in operating activities:		
Compensation recognized for stock option issuance	**9,000**	
Depreciation	**39,000**	39,000
Allowance for doubtful accounts	**4,000**	0
Realized gain on Sale of Marketable Securities	**0**	(1,276,000)
(Increase)/decrease in:		
Trade Receivables	**(97,000)**	(119,000)
Inventories	**(16,000)**	(120,000)
Other Current Assets	**17,000**	18,000
Accounts Payable	**(12,000)**	77,000
Accrued Expenses	**54,000**	48,000
Deferred Revenue	**12,000**	10,000
Accrued Income Taxes	**706,000**	342,000
Deferred Income Taxes	**(783,000)**	0
Net Cash From (Used in) Operating Activities	**298,000**	(5,000)
Cash Flows From Investing Activities		
Proceeds from Sale of Marketable Securities	**0**	1,291,000
Purchase of Property and Equipment	**(36,000)**	0
Net Cash Provided by (Used in) Investing Activities	**(36,000)**	1,291,000
Cash Flows From Financing Activities		
Proceeds from Issuance of Stock	**31,000**	253,000
Dividends Paid	**(269,000)**	(3,607,000)
Net Cash Used in Financing Activities	**(238,000)**	(3,354,000)
Net Increase in Cash & Cash Equivalents	**24,000**	(2,068,000)
Cash & Cash Equivalents, Beginning	**5,451,000**	7,060,000

Cash & Cash Equivalents, Ending	**$5,475,000**	$4,992,000
Supplemental Schedule of Non-Cash Investing and Financing Activities		
Net Change in Unrealized Gain/(Loss) on Investments	**$238,000**	$1,250,000
Cash Paid for:		
Income Taxes	**$325,000**	$312,000

See accompanying notes to unaudited condensed consolidated financial statements

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ELECTRO-SENSORS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

Note 1. Nature of Business

The accompanying condensed consolidated financial statements include the accounts of Electro-Sensors, Inc. and its wholly owned subsidiaries, ESI Investment Company and Senstar Corporation. Senstar has no operations. Intercompany accounts, transactions and earnings have been eliminated in consolidation. The consolidated entity is referred to as the Company .

Electro-Sensors, Inc. 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 second 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.

In addition, through its subsidiary ESI Investment Company (INV), the Company periodically makes strategic investments in other businesses and companies, primarily when the Company believes that such investments will facilitate development of technology complementary to the Company s products. Although ESI, through its subsidiary ESI Investment Company, invests in other businesses or companies, ESI does not intend to become an investment company and intends to remain primarily an operating company. The Company s primary investments are

343,267 shares of Rudolph Technologies, Inc. See Note 7 for additional information regarding its investments. The Company s investments in securities are subject to normal market risks.

Note 2. Basis of Presentation

The accompanying unaudited condensed 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.

This report should be read together with the Company s annual report on Form 10-KSB for the year ended December 31, 2006, including the audited financial statements and footnotes therein.

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 six-months ended June 30, 2007. The results of interim periods may not be indicative of results to be expected for the year.

Note 3. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. These estimates may be adjusted as more information becomes available, and any adjustment could be significant. The impact of any change in estimates is included in the determination of earnings in the period in which the change in estimate is identified. The impact of changes in estimates could materially affect results.

Note 4. Revenue Recognition

In recognizing revenue, the Company applies the provisions of the Securities and Exchange Commission Staff Accounting Bulletin (SAB) No. 101 (as amended by SAB No. 104), Revenue Recognition.

Revenue recognition of production monitoring equipment:

The Company recognizes revenue from the sale of its products when persuasive evidence of an arrangement exists, the product has been delivered, the fee is fixed and determinable and collection of the resulting receivable is reasonably assured.

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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. 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. ADS customers pay an annual maintenance fee for software support, which is recognized as deferred revenue on the balance sheet and on a monthly basis, it is recognized in income over the life of the contract.

Note 5. Stock-Based Compensation

On January 1, 2006, the Company adopted SFAS No. 123 (revised 2004) (SFAS No. 123R), *Share-Based Payment*, which addresses the accounting for stock-based payment transactions in which an enterprise receives employee services in exchange for (a) equity instruments of the enterprise or (b) liabilities that are based on the fair value of the enterprise s equity instruments or that may be settled by the issuance of such equity instruments. In January 2005, the SEC issued SAB No. 107, which provides supplemental implementation guidance for SFAS No. 123R. SFAS No. 123R eliminates the ability to account for stock-based compensation transactions using the intrinsic value method under Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and instead generally requires that such transactions be accounted for using a fair-value-based method. In accordance with the modified-prospective transition method, the Company s financial statements for prior periods have not been restated to reflect the impact of SFAS No. 123R. The Company uses the Black-Scholes-Merton (BSM) option-pricing model to determine the fair-value of stock-based awards.

The Company records compensation expense for employee stock options based on the estimated fair value of the options on the date of grant using the BSM model with the assumptions included in the table below. The Company uses historical data among other factors to estimate the expected price volatility, the expected option life and the expected forfeiture rate. The risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant for the estimated life of the option. At June 30, 2007, the Company had one stock-based employee compensation plan. During the six-months ended June 30, 2007, an executive exercised 15,000 options. On April 25, 2007 the Company granted, newly elected Board member, Robert Heller 5,000 shares of common stock and recognized compensation expense of approximately $9,000 based on the grant date fair value estimated in accordance with the provisions of SFAS 123R.

The assumptions made in estimating the fair value of the options on the grant date based upon the BSM option-pricing model are as follows:

Dividend yield	0.00	%
Expected volatility	36.74	%
Risk free interest rate	4.93	%
Expected lives	10 years	

The Company calculates expected volatility for stock options and awards using historical volatility as the Company believes the expected volatility will approximate historical volatility.

Note 6. Net Income Per Share

All common share equivalents relating to stock options and warrants are included in the diluted weighted average common shares.

Note 7. Available for Sale Securities

INV s investments consist of equity securities, primarily common stocks, government debt securities and money market funds. The estimated fair value of publicly traded equity securities (other than those accounted for based upon the equity method of accounting) is based on quoted market prices, and therefore subject to the inherent risk of market fluctuations. Shares of common stock for which there is no readily determinable value (i.e., no quoted market price) are accounted for on a historical cost method (unless accounted for based upon the equity method of accounting). Management determines the appropriate classification of securities at the date individual investments are acquired, and evaluates the appropriateness of such classification at each balance sheet date.

Since the Company generally does not buy investments in anticipation of short-term fluctuations in market prices, investments in equity securities are classified as available-for-sale (unless accounted for on the equity method of accounting). Available-for-sale securities with readily determinable values are stated at fair value, and unrealized holding gains and losses, net of the related deferred tax effect, are reported as separate component of stockholders equity.

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Realized gains and losses on securities, including losses from declines in value of specific securities determined by management to be other-than-temporary (unless accounted for on the equity method of accounting), are included in income in the period realized.

Prior to February 15, 2006, the Company s significant investment in equity securities consisted of 569,615 shares of common stock of August Technology Corporation (August), which had an approximate cost of $57,000. Rudolph Technologies, Inc. (Rudolph) acquired August on February 15, 2006. As a result of Rudolph s acquisition of August, the Company received 347,224 shares of Rudolph common stock and $1,015,891 in cash. At June 30, 2007, the Company s significant investment in equity securities is 343,267 shares of Rudolph. As of June 30, 2007, the aggregate value of the Company s Rudolph shares as reported on the Nasdaq Stock Exchange was approximately $5,702,000 with an approximate cost of $45,000.

Investment Reported on Equity Method:

At June 30, 2007, the Company owned 551,759 shares of PPT, which is 8.8% of PPT s outstanding common stock. The fair value of its holdings based on the quoted market price at June 30, 2007 was approximately $199,000 with an approximate cost of $2,434,000.

Since the Company owns approximately 8.8% of PPT s outstanding stock, and the Company s Secretary owns a controlling interest, it has been determined that the Company has significant influence over the operations of PPT, and as a result its ownership interest should be reported using the equity method of accounting for investments.

Under the equity method of accounting, the Company s proportionate share of PPT net income or loss through June 30, 2007 is not included in the Company s net income (loss) with a corresponding increase or decrease in the carrying value of its investment. As of 2004, the Company had exhausted it s investment in PPT with its share of the loss. All losses in excess of invested amounts are not recognized in the financial statements, but rather are suspended and applied against future equity in earnings for the investee until exhausted. At June 30, 2007, the Company had approximately $2,235,000 in suspended losses from its investment in PPT that will be used to offset future recognition of equity method earnings from the investment.

Note 8. Segment Information

The Company has three reportable operating segments based on the nature of its product lines: Production Monitoring, Character Recognition, and Investments. The Controls Division manufactures and markets a complete line of production monitoring equipment, in particular speed monitoring and motor control systems for industrial machinery. ADS designs and markets a desktop software-based character recognition system that reads hand printed characters, checkmarks, and bar code information from scanned or faxed forms. Sales of this system include software and can include hardware. INV holds investments in marketable and non-marketable securities.

The accounting policies of the segments are the same as those described in Note 1. In evaluating segment performance, management focuses on sales and income before taxes. The Company has no inter-segment sales.

The following is financial information relating to the continuing operating segments (in thousands):

	Three months Ended June 30, 2007	**2006**	**Six months Ended June 30, 2007**	**2006**
External sales				
Production monitoring	**$1,491,000**	$1,325,000	**$2,914,000**	$2,498,000
Character recognition	**118,000**	102,000	**255,000**	286,000
Investments	**0**	0	**0**	0
Total	**$1,609,000**	$1,427,000	**$3,169,000**	$2,785,000
Net Income/(Loss) before taxes				
Production monitoring	**$371,000**	$304,000	**$621,000**	$420,000
Character recognition	**(16,000)**	(22,000)	**(9,000)**	(8,000)
Investments	**(3,000)**	(26,000)	**(9,000)**	1,218,000
Total	**$352,000**	$256,000	**$603,000**	$1,630,000

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Recent accounting standards:

Management has reviewed recently issued, but not yet effective, accounting pronouncements and does not expect the implementation of these pronouncements to have a significant effect on the Company s financial statements.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (SFAS No. 157) to increase consistency and comparability in fair value measurements by defining fair value, establishing a framework for measuring fair value in generally accepted accounting principles, and expanding disclosures about fair value measurements. SFAS No. 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement and is effective for the fiscal years beginning after November 15, 2007. The Company is in the process of evaluating the effect, if any, that the adoption of SFAS No. 157 will have on its results of operations and financial condition.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS No. 159) which included an amendment of FASB Statement 115. This Statement provides companies with an option to report selected financial assets and liabilities at fair value. This Statement is effective for fiscal years beginning after November 15, 2007 with early adoption permitted. The Company is in the process of evaluating the effect, if any, that the adoption of SFAS No. 159 will have on its results of operations and financial condition.

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Item 2. Management s Discussion and Analysis or Plan of Operation

FORWARD-LOOKING STATEMENTS

This Form 10-QSB contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including statements regarding our expectations, beliefs, intentions or strategies regarding the future. Forward-looking statements include, but are not limited to, statements regarding our intent to develop distribution and independent representative partners domestically and internationally; the timing for release of our products; our expected use of cash on hand; cash requirements; and the sufficiency of our cash flows. Any statement that is not based solely upon historical facts, including strategies for the future and the outcome of events that have not yet occurred, is considered a forward-looking statement.

All forward-looking statements in this document are based on information available to us as of the date hereof, and we assume no obligation to update any such forward-looking statements. It is important to note that our actual results could differ materially from those in such forward-looking statements. The forward-looking statements we make in this Form 10-Q are subject to risks and uncertainties. In addition to the risk factors detailed in our Annual Report on Form 10-KSB for the year ended December 31, 2006, filed with the Securities and Exchange Commission, some of the factors that could cause future results to differ materially from our recent results or those projected in the forward-looking statements are the following: our ability to identify and commence relationships with effective partners; unforeseen delays in our product development process; the extent and timing of future revenues and expenses and customer demand; the market value of our investment securities; changes in worldwide general economic conditions; cyclical capital spending by customers; our ability to keep pace with technological developments and evolving industry standards; worldwide competition; and our ability to protect its existing intellectual property from challenges from third parties and other factors.

CRITICAL ACCOUNTING ESTIMATES

Management uses estimates and assumptions in preparing our financial statements in accordance with generally accepted accounting principles. These estimates affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. There are no significant accounting estimates described in the notes to the financial statements that are critical at this time. A more in-depth description of our accounting estimates can be found in the interim financial statements included in this report and in our Annual Report on Form 10-KSB for the fiscal year ended December 31, 2006.

RESULTS OF OPERATIONS

Net Sales

Net sales for the three-month period ended June 30, 2007 increased $182,000 or 12.7% when compared to net sales for the same period in 2006. Net sales for the six-month period ended June 30, 2007 increased $384,000 or 13.8% when compared to net sales for the same period in 2006.

For the three-months ended June 30, 2007 compared to the same period in 2006, the Controls Division contributed an increase in net sales of $166,000 or 12.5% and ADS contributed an increase in net sales of $16,000 or 15.7%.

For the six-months ended June 30, 2007 compared to the same period in 2006, the Controls Division contributed an increase in net sales of $415,000 or 16.6%, offset by a decrease in ADS net sales of $31,000 or 10.8%.

The Controls Division has experienced an increase in net sales for the second quarter and first half of 2007. The increase in sales is a result of products that are utilized in new plant installations, facility expansions, and to machine engineering. The bulk of our sales volume is derived from the Speed Monitoring product lines to the grain, feed, ethanol and biofuels, power generation, and mining industries, as well as other key industrial markets and equipment builders. Products sold into these markets include shaft speed sensors and switches, ratemeters and counters, motor controllers, vibration switches, and position monitors. In our sales and marketing efforts, we are developing additional channel partners in the form of distributors and independent representatives both domestically and internationally and expect to continue adding sales partners in key locations.

The ADS Division increase in net sales for the second quarter of 2007 is due to an increase in the sales of the ExpertScan product. For the six-months ended June 30, 2007 compared to the same period in 2006, ADS experienced a decrease in net sales due to a reduction in multiple unit orders and scanner bundled systems. ADS is developing an on-line web module for its ExpertScan software product. ExpertScan currently permits automated data collection from surveys and other paper forms. The new web capability will enable ExpertScan to automatically create an electronic version of a new or existing ExpertScan document, thereby allowing a combination of paper and electronic data collection from the same form. Release of the web-enabled version of ExpertScan is expected before the end of this fiscal year and should strengthen sales to both new and existing customers.

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Cost of Goods Sold

Our cost of goods sold increased $67,000 or 13.3% for the three-months ended June 30, 2007 compared to the same period in 2006. For the six-month period ended June 30, 2007, the cost of goods sold increased $133,000 or 13.0% compared to the same period in 2006. This increase is primarily a direct result of increased material costs in direct relation to the favorable sales increase.

Gross Profit

Gross margin for the three-month period ended June 30, 2007 was 64.5% compared to 64.7% for the same period in 2006. For the six-month period ended June 30, 2007, gross margins were 63.7% compared to 63.4% for the same period in 2006. The slight variances are due to sales and expenses rising at nearly the same rates over the three and six-month period ending June 30, 2007 compared to the same period last year.

Operating Expenses

Total operating expenses decreased $63,000 or 7.8% for the three-months ended June 30, 2007 when compared to the same period of the prior year. Of this decrease, the Controls Division contributed a decrease of $77,000 or 11.0% offset by an increase in ADS of $14,000 or 13.5%.

For the six-months ended June 30, 2007 compared to the same period of 2006, operating expenses decreased $60,000 or 3.7%. Of this decrease, the Controls Division contributed a reduction of $75,000 or 5.4%, offset by an increase in ADS of $15,000 or 7.1%.

Selling and marketing costs decreased $1,000 or 0.4% for the three-months ended June 30, 2007 compared to the same period in 2006. For the six-months ended June 30, 2007, selling and marketing costs increased $27,000 or 4.2% compared to the same period in 2006. Of the decrease for the three-months ended June 30, 2007, the Controls Division contributed a minimal increase of 0.1%, which was offset by a decrease from ADS of $2,000 or 3.5%. Of the increase for the six-months ended June 30, 2007, the Controls Division contributed the majority with an increase of $27,000 or 4.8%. Sales representative commissions and advertising are the predominant expenses that increased in the Controls Division. The increase in ADS is due to reduced expenses in website development offset by increased wages due to additional personnel.

General and administrative costs decreased $64,000 or 18.4% for the three-months ended June 30, 2007 compared to the same period in 2006. For the six-months ended June 30, 2007, general and administrative costs decreased $104,000 or 15.4%. Of this decrease for the three-months ended June 30, 2007, the Controls Division contributed a decrease of $77,000 or 22.9% and ADS contributed an increase of $13,000 or 89.5%. The results for the six-months ended June 30, 2007 is driven by a decrease in costs of $113,000 or 17.7% from the Controls Division that was slightly offset by an increase in ADS costs of 19.4%. The overall decrease in general and administrative costs from the Controls Division was due to a one time bonus of $100,000 paid to Peter R. Peterson, Corporate Secretary, in 2006. The increase in ADS is due to contract personnel expenses. Overall, general and administrative costs should remain relatively flat with additional expenses coming from Sarbanes-Oxley compliance.

Research and development costs increased $1,000 or 0.9% for the three-months ended June 30, 2007 compared to the same period in 2006. For the six-months ended June 30, 2007, research and development costs increased $18,000 or 6.6%. Of the increase for the three-months ended June 30, 2006, the Controls Division contributed a decrease of $2,000 or 2.0%, and ADS contributed an increase of $3,000 or 6.4%. Of the increase for the six-months ended June 30, 2007, the Controls Division contributed $11,000 or 6.1%, and ADS contributed $7,000 or 7.5%. The increase in the Controls Division is due to lab testing fees for product certification. The increase in ADS is due to contract engineering fees and salary expenses.

Non-Operating Income

Non-operating income decreased by $82,000 or 55.7% for the three-month period ended June 30, 2007 compared to the same period for 2006. For the six-months ended June 30, 2007, non-operating income decreased $1,338,000 or 91.8%. The decrease for both the three and six-months ended June 30, 2007 is driven by a decrease in interest income, but primarily due to a decrease in the sale of marketable securities, as there were none during the first half of this year.

Interest income decreased $25,000 or 26.1% when comparing the three-months ended June 30, 2007 to the same period in 2006. For the six-months ended June 30, 2007, interest income decreased $48,000 or 27.9%. These decreases are due to fewer of our funds being invested in Treasury Bills for the three and six-months ended June 20, 2007 compared to the same periods in 2006.

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Income Before Income Taxes

Income before income taxes increased $96,000 to an income before tax of $352,000 for the three-month period ended June 30, 2007 compared to the same period in 2006. For the six-month period ended June 30, 2007, income before income tax decreased $1,027,000 when compared to the same period in 2006.

The Controls Division had income before income taxes of $371,000 for the three-months ended June 30, 2007 compared to $203,000 for the same period in 2006, an increase of $168,000. For the six-months ended June 30, 2007, the Controls Division had income before income taxes of $621,000 compared to $322,000 for the same period in 2006, an increase of $299,000. In addition to the increased sales for the Controls Division, our overall efforts to reduce operating expenses contributed to the increase in net income before income taxes.

ADS had a loss before income taxes of $16,000 for the three-months ended June 30, 2007 compared to the net loss before income taxes of $22,000 for same period in 2006. For the six-months ended June 30, 2007, ADS had a loss of $9,000 compared to loss before income taxes of $8,000 for the same period in 2007.

INV s income before taxes increased from a loss of $26,000 for the three-month period ended June 30, 2006 to a loss of $3,000 for the three-month period ended June 30, 2007. INV s income before taxes decreased $1,228,000 to a loss before income taxes of $9,000 for the six-months ended June 30, 2007 compared to the same period in 2006. This decrease is primarily due to no sales of marketable securities in the first half of 2007 and the cash received from Rudolph Technology related to its acquisition of August Technology in February 2006.

LIQUIDITY AND CAPITAL RESOURCES

Our ongoing cash requirements will be primarily for capital expenditures, acquisitions, research and development and working capital. Our primary source of capital is cash provided by operating activities of the Controls Division and ADS.

Cash and cash equivalents were $5,475,000 at June 30, 2007 and $4,992,000 at June 30, 2006. Cash provided by operating activities of $298,000 for the six-months ended June 30, 2007 is primarily a result of our net operating income adjusted for non-cash charges.

Cash used by investing activities was $36,000 for the six-month period ended June 30, 2007 is a result of the purchase of property and equipment.

Cash used in financing activities was $237,000 for the six-months ended June 30, 2007. During the six-months ended June 30, 2007 and 2006, we paid aggregate dividends of $269,000 and $3,607,000, respectively.

Management believes that cash on hand and any cash provided by operations will be sufficient to meet our cash requirements through at least the next 12 months.

INV s primary investments are 343,267 shares of Rudolph Technology Corporation. Rudolph Technology Corporation is listed on the Nasdaq stock market and is subject to fluctuations in price and could have a negative effect on the liquidity of the Company.

Off-balance Sheet Arrangements

As of June 30, 2007, we had no off-balance sheet arrangements or transactions.

Item 3. Controls and Procedures

As of the end of the period covered by this report, the Company conducted an evaluation, under the supervision and with the participation of the person serving as the principal executive officer and principal financial officer, of the Company s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the Exchange Act)). Based on this evaluation, the person serving as the principal executive officer and principal financial officer concluded that the Company s disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms.

There was no change in the Company s internal control over financial reporting during the Company s most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company s internal control over financial reporting.

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PART II OTHER INFORMATION

Item 1. Legal Proceedings

None.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Submission of Matters to a Vote of Security Holders

At our Annual Shareholders meeting held on April 25, 2007, we submitted to a vote of our shareholders the following matters, each of which received the number of votes indicated below:

1. Approving setting the number of members of the Board of Directors at five (5):

For:	2,978,186	Against:	102,731	Abstain:	3,945

2. Election of Directors:

Director	For	Withheld
Bradley D. Slye	2,984,681	100,181
Peter R. Peterson	2,984,081	100,781
Robert W. Heller	2,984,681	100,181
Joseph A. Marino	2,982,667	102,195
Geoffrey W. Miller	2,982,067	102,795

3. Ratification of the selection of Boulay, Heutmaker, Zibell & Co. P.L.L.P. as independent auditors for the Company for the fiscal year ending December 31, 2007:

For:	2,999,741	Against:	63,038	Abstain:	22,083

Item 5. Other Information

None.

Item 6. Exhibits

(a) Exhibits - See Exhibit Index following signature page.

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SIGNATURES

In accordance with the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Electro-Sensors, Inc.

August 14, 2007	/s/ Bradley D. Slye Bradley D. Slye Chief Executive Officer and Chief Financial Officer

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EXHIBIT INDEX

ELECTRO-SENSORS, INC.

FORM 10-QSB FOR QUARTER ENDED JUNE 30, 2007

Exhibit	Description
31.1	Certification of CEO and CFO Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of CEO and CFO Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002