SUTRON CORP
Form 10QSB
November 12, 2004

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

FORM 10-QSB

Quarterly Report Pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934

For the quarterly period ended: September 30, 2004

Commission file number 0-12227

Sutron Corporation
(Exact name of registrant as specified in its charter.)

Virginia	54-1006352
(State or other jurisdiction of incorporation organization)	(I.R.S. Employer Identification No.)

21300 Ridgetop Circle, Sterling Virginia	20166
(Address of principal executive offices)	(Zip Code)

(703) 406-2800
(Registrant's telephone number, including area code)

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 [X]

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

Common Stock, $.01 Par Value - 4,289,551 shares of as of September 30, 2004.

SUTRON CORPORATION
FORM 10-QSB QUARTERLY REPORT
FOR THE QUARTER ENDED SEPTEMBER 30, 2004
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PART I. CONDENSED FINANCIAL INFORMATION

Item 1. Financial Statements

SUTRON CORPORATION
BALANCE SHEETS
(Unaudited)

	September 30, 2004	December 31, 2003
Assets		
Current Assets:		
Cash	$1,212,341	$ 388,612
Accounts receivables	3,900,490	3,062,205
Inventory	2,279,386	2,438,275
Prepaid items and other	53,650	122,150
Deferred income taxes	211,658	120,000
Total Current Asset	$7,657,525	$6,131,242
Property, Plant, and Equipment Cost	2,912,654	2,723,107
Accumulated depreciation	(2,287,624)	(2,125,624)
Net Property, Plant and Equipment	625,030	597,483
Income taxes receivable	0	129,000
Other	23,986	22,986
TOTAL ASSETS	$8,306,541	$6,880,711

LIABILITIES AND STOCKHOLDERS' EQUITY

	September 30, 2004	December 31, 2003
Current Liabilities:		
Accounts payable	$1,022,495	$1,043,805
Accrued payroll	236,640	50,142
Accrued expenses	1,099,443	850,726
Accrued income taxes	179,726	-
Current maturities of long-term notes:		
Line of credit	-	399,454
Notes payable-stockholders	-	330,000
Notes payable	105,121	49,936
Total Current Liabilities	$2,643,425	$2,724,063

Long-term liabilities:		
Long-term notes payable	40,362	100,129
Deferred income taxes	142,000	111,000
Total liabilities	2,825,787	2,935,192
Stockholders' Equity:		
Common stock, $.01 par value,	42,896	42,896
Additional paid in capital	2,306,655	2,306,655
Retained Earnings	3,131,203	1,595,968
Total Stockholders' Equity	5,480,754	3,945,519
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$8,306,541	$6,880,711

See Accompanying Notes to Financial Statements

SUTRON CORPORTION
STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended September 30, 2004	2003
Revenues	$4,813,906	$2,230,638
Cost of Goods Sold	2,984,614	1,654,141
Gross Profit	1,829,292	576,497
Research and Development Expenses	241,871	276,463
Selling, General, and Administrative Expenses	596,308	480,574
Income (Loss) from Operations	991,113	(180,540)
Interest Expense	4,154	4,976
Income (Loss) before Provision for Income Taxes	986,959	(185,516)
Provisions for Income Taxes	354,000	(82,000)
Net Income	$ 632,959	$(103,516)
Net Income per Common Share	$ .15	$(.02)
Weighted Average Number of Common Shares	4,289,551	4,289,551

See Accompanying Notes to Financial Statements

SUTRON CORPORTION
STATEMENTS OF OPERATIONS

(Unaudited)

	Nine Months Ended September 30, 2004	2003
Revenues	$12,614,975	$7,309,235
Cost of Goods Sold	7,739,421	5,247,548
Gross Profit	4,875,554	2,061,687
Research and Development Expenses	741,769	860,477
Selling, General, and Administrative Expenses	1,717,217	1,673,724
Income (Loss) from Operations	2,416,568	(472,514)
Interest Expense	28,333	13,599
Income (Loss) before Provision for Income Taxes	2,388,235	(486,113)
Provisions for Income Taxes	853,000	(228,000)
Net Income	$1,535,235	$(258,113)
Net Income per Common Share	$ .36	$(.06)
Weighted Average Number of Common Shares	4,289,551	4,289,551

See Accompanying Notes to Financial Statements

SUTRON CORPORTION
STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30, 2004	2003
Cash Flows from Operating Activities:		
Net income (loss)	$1,535,235	$(258,113)
Depreciation and amortization	162,000	161,100
(Increase) Decrease in:		
Accounts receivables	(838,285)	(477,567)
Inventory	158,889	(352,600)
Prepaid items and other	67,500	56,151
Deferred income taxes	(91,658)	(206,173)
Income tax receivable	129,000	-
Increase (Decrease) in:		
Accounts payable	(21,310)	290,210
Accrued expenses	435,215	381,904
Accrued income taxes	179,726	-
Deferred income taxes	31,000	-

Net Cash Provided by Operating Activities	1,747,312	(405,090)
Cash Flows from Investing Activities:		
Capital expenditures	(189,547)	(111,918)
Net Cash Used in Investing Activities	(189,547)	(111,918)
Cash Flows from Financing Activities:		
Proceeds from advances on line of credit	-	424,454
Proceeds from shareholder notes	-	330,000
Payments on line of credit	(399,454)	-
Payments on term notes payable	(4,582)	(47,242)
Payments on shareholder notes payable	(330,000)	-
Net Cash (Used) by Financing Activities	(734,036)	707,212
Net Increase (Decrease) in Cash	823,729	190,204
Cash and Cash Equivalents, January 1	388,612	401,740
Cash and Cash Equivalents, September 30	$1,212,341	$ 591,944

See Accompanying Notes to Financial Statements

SUTRON CORPORATION

NOTES TO FINANCIAL STATEMENTS

September 30, 2004

1. Basis of Presentation

The accompanying financial statements, which should be read in conjunction with the financial statements of Sutron Corporation ("the Company") included in the 2003 Annual Report filed on Form 10-KSB, are unaudited but have been prepared in the ordinary course of business for the purpose of providing information with respect to the interim period. The Company believes that all adjustments (none of which were other than normal recurring accruals) necessary for a fair presentation for such periods have been included.

2. Earnings Per Share

The Company has adopted Statement of Financial Accounting Standards ("SFAS") No. 128 which establishes standards for computing and presenting earnings per share (EPS) for entities with publicly held common stock. The standard requires presentation of two categories of earning per share, basic EPS and diluted EPS. Basic EPS excludes dilution and is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding for the year. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Company.

Computation of Per Share Earnings

	Three Months Ended September 30, 2004	2003
Basic EPS		
Average shares outstanding	4,289,551	4,289,551
Net Income	$ 632,959	$(103,516)
Net Income per common share	$.15	$(.02)
Dilutive EPS		
Average shares outstanding	4,289,551	4,289,551
Effect of dilutive securities	582,256	142,750
Total average shares outstanding	4,871,807	4,432,301
Net earnings	$ 632,959	$(103,516)
Net income per diluted share	$.13	$(.02)

	Nine Months Ended September 30, 2004	2003
Basic EPS		
Average shares outstanding	4,289,551	4,289,551
Net Income	$1,535,235	$(258,113)
Net Income per common share	$.36	$(.06)
Dilutive EPS		
Average shares outstanding	4,289,551	4,289,551
Effect of dilutive securities	582,256	286,688
Total average shares outstanding	4,871,807	4,576,239
Net earnings	$1,535,235	$(258,113)
Net income per diluted share	$.33	$(.06)

3. Cash and Cash Equivalents

The Company has entered into certain international contracts that require provision of letters of guarantee to the customer until acceptance of the system by the customer. Standby irrevocable letters of credit were issued by the Companys previous bank that do not expire until March 2005. As of September 30, 2004, $277,454 of the cash and cash equivalents balance is restricted and is held as security by M&T Bank for these standby letters of credit.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Statements made in this Report on Form 10-QSB, including without limitation this Management's Discussion and Analysis of Financial Condition and Operations, other than statements of historical information, are forward looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements may sometimes be identified by such words as "may," "will," "expect," "anticipate," "believe," "estimate" and "continue" or similar words. We believe that it is important to communicate our future expectations to investors. However, these forward-looking statements involve many risks and uncertainties. Our actual results could differ materially from those indicated in such forward-looking statements as a result of certain factors. We are under no duty to update any of the forward-looking statements after the date of this Report on Form 10-QSB to conform these statements to actual results.

Sutron Corporation (the Company) was incorporated on December 30, 1975 under the General Laws of the Commonwealth of Virginia. The Company's headquarters is located at 21300 Ridgetop Circle, Sterling, Virginia 20166, and the Company's telephone number at that location is (703) 406-2800. The Company maintains a worldwide web address at www.sutron.com. The Company designs, manufactures and markets products and solutions that enable government and commercial entities to monitor and collect hydrological and meteorological data for the management of critical water resources, for early warning of potentially disasterous floods or storms and for the optimization of hydropower plants.

The Company is focused on providing real-time solutions and services to our customers in three areas of the hydrological and meteorological markets. First, we provide realtime data collection and control products consisting primarily of dataloggers, satellite transmitters and sensors. Second, we provide turnkey integrated systems for hydrological and meteorological networks and airport weather systems. Third, we provide services consisting of equipment installation, maintenance of hydrological and meteorological systems, and other related engineering services. The Companys customers include a diversified base of federal, state, local and foreign governments, engineering companies, universities, and hydropower companies.

The Company utilizes the accrual method of accounting for both financial statement and tax return reporting purposes. The Company recognizes revenue from product sales upon shipment and from services upon completion of services and billing. Selling, general and administrative expenses are charged against periodic income as incurred. Revenue from fixed-price contracts is recognized on the percentage-of-completion method based on costs incurred in relation to total estimated costs. Revenue from time-and-materials contracts is recognized to the extent of billable rates, times hours delivered, plus materials costs incurred. Contract costs include allocated indirect costs and anticipated losses on contracts are recognized as soon as they become known.

Our revenue and operating results are subject to substantial variations based on our customers' expenditures and the frequency with which we are chosen to perform services for our customers. Revenue from any given customer will vary from period to period based upon the size and the complexity of the project. Our gross margins are affected by the product mix and can vary substantially based on quantities, project requirements and the amount and type of services provided.

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our financial statements and notes thereto and the other financial information included elsewhere in this Report on Form 10-QSB.

Results of Operations

The following table sets forth for the periods indicated the percentage of total revenues represented by certain items reflected in our statements of operations:

Three months ended September 30, 2004 Compared to 2003

	2004	2003
Revenues	100.0%	100.0%
Cost of sales	62.0	74.2
Gross profit	38.0	25.8
Research and Development expenses	5.0	12.4
Selling, general and administrative expenses	12.4	21.5
Operating income	20.6	(8.1)
Interest expense	.1	.2
Income before income taxes	20.5	(8.3)
Income taxes (benefit)	7.4	(3.7)
Net income	13.1%	(4.6)%

Net Revenues. The Company's revenues for the three months ended September 30, 2004 increased 115% to $4,813,906 from $2,230,638 in 2003. Domestic revenues increased to $3,661,670 in the third quarter of 2004 versus $1,784,172 in 2003. International revenues were $1,152,236 in 2004 versus $446,466 in 2003. Revenues from domestic sales of standard products and systems increased significantly in the third quarter due to shipments to Hanscom Air Force Base of FMQ-13(v)2 Wind Sensor Systems. The Hydrological Services Division also contributed significantly to the increase in domestic revenues as hydrological and engineering services revenues were approximately $446,000 higher than 2003 revenues. The international sales increase was primarily due to the shipment of XLite dataloggers and bubblers and water level sensors to a Canadian consortium for the Emergency Flood Recovery Project in Poland.

Bookings for the third quarter of 2004 were $6,112,134 as compared to $4,593,124 in the third quarter of 2003.

Gross Profit. Gross profit for 2004 increased to $1,829,292 from $576,497 in 2003. Gross margin as a percentage of revenues for 2004 increased to 38% as compared to 25.8% in 2003. The increase in the Company's gross margin is due to increased sales volume and to the product mix. Sales of 9210 XLites for the Emergency Flood Recovery Project in Poland significantly improved margins as well as FMQ-13(v)2 Wind Sensor Systems that shipped to Hanscom Air Force Base.

Selling, General And Administrative. Selling, general and administrative expenses increased to $596,308 in 2004 from $480,574 in 2003, an increase of $115,734 or 24%. The increase is due to increases in international agent commissions, sales and marketing expenses related to Sutron's new Airport Weather Systems division and increased audit and tax fees.

Research And Development. Research and development expenses decreased to $241,871 in 2004 from $276,463 in 2003, a decrease of $34,592 or 13%. This decrease is due to work performed on the Emergency Flood Recovery Project of Poland and work performed on a contract with the Hydrologic Instrumentation Facility of the US Geological Survey to develop a GOES DCP Test Set. These projects required significant engineering effort which was direct billable work versus indirect engineering work.

Interest Expenses. Interest expenses decreased to $4,154 in 2004 from $4,976 in 2003 due to less borrowings on the bank line of credit and the repayment of shareholder notes in the amount of $330,000.

The following table sets forth for the periods indicated the percentage of total revenues represented by certain items reflected in our statements of operations:

Nine months ended September 30, 2004 Compared to 2003

	2004	2003
Revenues	100.0%	100.0%
Cost of sales	61.4	71.8
Gross profit	38.6	28.2
Research and Development expenses	5.9	11.8
Selling, general and administrative expenses	13.6	22.9
Operating income	19.2	(6.5)
Interest expense	.2	.2
Income before income taxes	19.0	(6.7)
Income taxes (benefit)	6.8	(3.1)
Net income	12.2%	(3.6)%

Net Revenues. The Company's revenues for the nine months ended September 30, 2004 increased 72% to $12,614,975 from $7,309,235 in 2003. Domestic revenues increased to $8,196,668 in the first nine months of 2004 versus $5,051,492 in 2003. International revenues were $4,418,308 in 2004 versus $2,257,743 in 2003. The domestic revenues increase was primarily due to approximately $1,189,000 of sales of FMQ-13(v)2 Wind Sensor Systems to Hanscom Air Force Base and increased services revenues of approximately $1,095,000 by the Hydrological Services Division on contracts with the South Florida Water Management District. The international sales increase was primarily due to the shipment of XLite dataloggers and bubblers and water level sensors to a Canadian consortium for the Emergency Flood Recovery Project in Poland.

Bookings for the first nine months of 2004 were $15,023,747 as compared to $9,805,317 in 2003. As a result to the Company's strong bookings, the Company's backlog of orders at September 30, 2004 was $6,837,725 as compared to $5,200,614 as of September 30, 2003. The Company anticipates that 60% of its backlog as of September 30, 2004 will be shipped in 2004.

Gross Profit. Gross profit for 2004 increased to $4,875,554 from $2,061,687 in 2003. Gross margin as a percentage of revenues for 2004 increased to 39% as compared to 28% in 2003. The increase in the Company's gross margin is due to increased sales volume and to the product mix. Sales of 9210 XLites for the Emergency Flood Recovery Project in Poland significantly improved margins as well as FMQ-13(v)2 Wind Sensor Systems that shipped to Hanscom Air Force Base.

Selling, General And Administrative. Selling, general and administrative expenses increased to $1,717,218 in 2004 from $1,673,724 in 2003, an increase of $43,494 or 3%. The primary cause of the increase was increased sales and marketing activity by Sutron's new Airport Weather Systems division.

Research And Development. Research and development expenses decreased to $741,769 in 2004 from $860,477 in 2003, a decrease of $118,708 or 14%. This decrease is due to engineering services provided on the Hanscom Air Force Base FMQ-13(V)2 Wind Sensor System contract and work performed on a contract with the Hydrologic Instrumentation Facility of the US Geological Survey to develop a GOES DCP Test Set that required significant engineering effort which is direct billable work versus indirect engineering work.

Interest Expenses. Interest expenses increased to $28,333 in 2004 from $13,599 in 2003 due to borrowings from shareholders to supplement the bank line of credit in order to finance inventory and project requirements.

Liquidity and Capital Resources

Cash and cash equivalents increased to $1,212,341 at September 30, 2004, compared to $388,612 at December 31, 2003.

The ratio of current assets to current liabilities was 2.9:1 as of September 30, 2004, compared to 2.25:1 as of December 31, 2003. Working capital at September 30, 2004 increased to $5,014,101 compared to $3,407,179 at the end of fiscal 2003. Free cash flow, which is the net of cash provided or used by operations and capital expenditures, improved to $1,557,765 in 2004 compared with a loss of $235,158 in 2003.

The Company has a revolving credit facility of $1,625,000 with BB&T Bank that expires on August 5, 2005. Borrowings on the line of credit are based on a percentage of billed receivables and finished goods inventory. In addition to the revolving credit facility, the Company borrowed $330,000 from three shareholders in 2003 in order to finance inventory growth and project requirements. In April 2004, the Company paid one of these notes in full in the amount of $200,000. The remaining notes were due and payable to Raul S. McQuivey, President, and Thomas N. Keefer, Vice President and were paid in full in August and September 2004.

Management believes that its existing cash resources, cash flow from operations and short-term borrowings on the existing line of credit will provide adequate financial resources for supporting operations during the remainder of fiscal 2004.

Item 3. Controls and Procedures

Based on their evaluation of the Companys disclosure controls and procedures (as defined in Rules 13a-14(c) and 15d-14(c) under the Securities Exchange Act of 1934) as of a date within 90 days of the filing date of this Quarterly Report on Form 10-QSB the Companys chief executive officer and chief financial officer have concluded that the Companys disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and are operating in an effective manner.

There were no significant changes in the Companys internal controls or in other factors that could significantly affect these controls subsequent to the date of their most recent evaluation.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

In 2003, the Company filed a claim with the Advance Tax Court of India seeking a ruling on a decision by the Government of Andhra Pradesh (GoAP) of India to assess a 48% income tax on the Company's contract of approximately $1,606,000. The GoAP believed that the Company had established a branch office in India and was therefore subject to Indian income tax. Although the Company did file an application for branch office status and received approval to open a branch office, the Company did not complete the registration and approval process with the Government of India and had not opened a branch office in India. The income tax amount that is at issue was approximatly $770,000.

The Advance Tax Court of India heard the case in September 2004 and ruled that Sutron Corporation has a Permanent Establishment in India by virtue of its Country Manager who maintains an office in New Delhi. The Country Manager has the authority to sign contracts and perform other duties on behalf of the Company that fulfills the requirements of Indian tax law and as defined in Double Taxation Avoidance Agreement with the United States of America.

As a result of this ruling, Sutron Corporation entered into an agreement with Ernst & Young, New Delhi, India to file tax returns for the tax periods April 1, 2002 to March 31, 2003 and April 1, 2003 to March 31, 2004. The returns for both tax periods were filed on October 29, 2004. A refund in the amount of approximately $141,500 will be issued to Sutron for the tax period ending March 31, 2003 resulting from excess withholdings by the Government of Andhra Pradesh in excess of the tax amount of approximately $5,250. A tax payment of approximately $5,400 was made for the tax period ending March 31, 2004. All taxes paid in India will be applied as income tax credits on the Company's U.S. tax returns in accordance with the Double Taxation Avoidance Agreement with the United States of America and will therefore offset federal taxes.

Item 6. Exhibits and Reports on Form 8-K

B. Reports on Form 8-K

No reports have been filed on Form 8-K during this quarter.

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SUTRON CORPORATION

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

Sutron Corporation
(Registrant)

November 12, 2004 /s/Raul S. McQuivey
Date Raul S. McQuviey
Principal Executive Officer

November 12, 2004 /s/Sidney C. Hooper
Date Sidney C. Hooper
Principal Accounting Officer

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