TAYLOR DEVICES INC
Form 10-Q
October 14, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

[X] **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended August 31, 2009

OR

[ ] **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 0-3498

TAYLOR DEVICES, INC.

(Exact name of registrant as specified in its charter)

NEW YORK	16-0797789
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
90 Taylor Drive, North Tonawanda, New York	14120-0748
(Address of Principal Executive Offices)	(Zip Code)

716-694-0800

(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 [X] No [ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer [ ]	Accelerated filer [ ]	Non-accelerated filer [ ] (Do not check if a smaller reporting company)	Smaller reporting company [X]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes [ ] No [X]

As of October 14, 2009, there were outstanding 3,223,174 shares of the registrant's common stock, par value $.025 per share.

TAYLOR DEVICES, INC.

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TAYLOR DEVICES, INC. AND SUBSIDIARY

Condensed Consolidated Balance Sheets	**(Unaudited) August 31, 2009**	May 31, 2009
Assets		
Current assets:		
Cash and cash equivalents	**$ 33,257**	$ 45,297
Accounts receivable, net	**2,552,683**	2,691,032
Inventory	**6,587,117**	6,721,821
Costs and estimated earnings in excess of billings	**3,253,418**	1,957,149
Other current assets	**1,250,924**	1,382,907
Total current assets	**13,677,399**	12,798,206
Maintenance and other inventory, net	**732,279**	808,537
Property and equipment, net	**3,656,362**	3,687,637
Other assets	**138,097**	136,747
	$ 18,204,137	$ 17,431,127
Liabilities and Stockholders' Equity		
Current liabilities:		
Short-term borrowings and current portion of long-term debt	**$ 578,381**	$ 1,094,151
Payables - trade	**1,236,029**	886,963
Accrued commissions	**736,864**	598,287
Billings in excess of costs and estimated earnings	**200,901**	126,017
Other current liabilities	**1,603,590**	1,146,631
Total current liabilities	**4,355,765**	3,852,049

Long-term liabilities	**320,540**	395,245
Stockholders' Equity:		
Common stock and additional paid-in capital	**6,517,699**	6,494,497
Retained earnings	**9,241,354**	8,920,557
	15,759,053	15,415,054
Treasury stock - at cost	**(2,231,221)**	(2,231,221)
Total stockholders' equity	**13,527,832**	13,183,833
	$ 18,204,137	$ 17,431,127

See notes to condensed consolidated financial statements.

TAYLOR DEVICES, INC. AND SUBSIDIARY

Condensed Consolidated Statements of Income **(Unaudited)**

	For the three months ended	
	August 31, 2009	August 31 2008
Sales, net	**$ 5,013,673**	$ 4,803,502
Cost of goods sold	**3,281,827**	3,523,715
Gross profit	**1,731,846**	1,279,787
Selling, general and administrative expenses	**1,180,338**	1,042,982
Operating income	**551,508**	236,805

Other expense, net	**4,711**	253
Income before provision for income taxes	**546,797**	236,552
Provision for income taxes	**226,000**	87,900
Net income	**$ 320,797**	$ 148,652
Basic and diluted earnings per common share	**$ 0.10**	$ 0.05

See notes to condensed consolidated financial statements.

TAYLOR DEVICES, INC. AND SUBSIDIARY

Condensed Consolidated Statements of Cash Flows

	(Unaudited)	
For the three months ended	**August 31, 2009**	August 31, 2008
Cash flows from operating activities:		
Net income	**$ 320,797**	$ 148,652
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation and amortization	**110,556**	98,920
Gain of sale of equipment	**-**	(320)
Stock options issued for services	**19,851**	28,114
Changes in other assets and liabilities:		
Accounts receivable	**138,349**	(1,303,687)
Inventory	**210,962**	(71,148)
Costs and estimated earnings in excess of billings	**(1,296,269)**	(1,003,586)
Other current assets	**94,052**	260,254
Payables - trade	**349,066**	(59,824)

Accrued commissions	**138,577**	134,481
Billings in excess of costs and estimated earnings	**74,884**	-
Other current liabilities	**456,959**	32,322
Net cash flows from (for) operating activities	**617,784**	(1,735,822)
Cash flows from investing activities:		
Acquisition of property and equipment	**(79,281)**	(123,462)
Other investing activities	**36,581**	25,185
Net cash flows for investing activities	**(42,700)**	(98,277)
Cash flows from financing activities:		
Net short-term borrowings and repayments on long-term debt	**(590,475)**	1,852,934
Proceeds from issuance of common stock	**3,351**	3,591
Net cash flows from (for) financing activities	**(587,124)**	1,856,525
Net increase (decrease) in cash and cash equivalents	**(12,040)**	22,426
Cash and cash equivalents - beginning	**45,297**	110,720
Cash and cash equivalents - ending	**$ 33,257**	$ 133,146

See notes to condensed consolidated financial statements.

TAYLOR DEVICES, INC.

Notes to Condensed Consolidated Financial Statements

1. 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-Q. 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. In the opinion of the Company, the accompanying unaudited condensed consolidated financial statements contain all adjustments (consisting of only normal recurring accruals) necessary to present fairly the financial position as of August 31, 2009 and May 31, 2009, the results of operations for the three months ended August 31, 2009 and August 31, 2008, and cash flows for the three months ended August 31, 2009 and August 31, 2008. These financial statements should be read in conjunction with the audited financial statements and notes thereto contained in the Company's Annual Report to Shareholders for the year ended May 31, 2009. There have been no updates or changes to our audited financial statements for the year ended May 31, 2009.

2. The Company has evaluated events and transactions for potential recognition or disclosure in the financial statements through October 14, 2009 (the date on which the financial statements were issued).

3. There is no provision nor shall there be any provisions for profit sharing, dividends, or any other benefits of any nature at any time for this fiscal year.

4. For the three month periods ended August 31, 2009 and August 31, 2008 the net income was divided by 3,222,327 and 3,219,490, respectively, which is net of the Treasury shares, to calculate the net income per share.

5. The results of operations for the three month period ended August 31, 2009 are not necessarily indicative of the results to be expected for the full year.

6. In September 2006, the FASB issued SFAS No. 157 "Fair Value Measurements," to define fair value, establish a framework for measuring fair value in accordance with generally accepted accounting principles, and expand disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and for interim periods within those years. The FASB issued FASB Staff Positions (FSP) 157-1 and 157-2 and 157-3. FSP 157-1 amends SFAS 157 to exclude SFAS No. 13, "Accounting for Leases," and its related interpretive accounting pronouncements that address leasing transactions, while FSP 157-2 delays the effective date of the application for SFAS No. 157 to fiscal years beginning after November 15, 2008 for all nonfinancial assets that are recognized or disclosed at fair value in the consolidated financial statements on a nonrecurring basis. FSP 157-3 addresses considerations in determining fair value of a financial asset when the market for that asset is not active. The Company adopted SFAS No. 157 as of June 1, 2008 with the exception of the application of the statement to nonfinancial assets and liabilities. The Company's adoption of SFAS No. 157 does not have a material impact on its consolidated financial statements.

   In February 2007, the FASB issued SFAS No. 159 "The Fair Value Option for Financial Assets and Financial Liabilities -- an Amendment of SFAS No. 115." This statement permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by mitigating volatility in reporting earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007 and interim periods within those years. The Company adopted SFAS No. 159 as of June 1, 2008 and elected not to measure any additional financial instruments and other items at fair value, therefore, the adoption of SFAS No. 159 had no effect on our consolidated financial statements.

   Other recently issued FASB Statements or Interpretations, SEC Staff Accounting Bulletins, and AICPA Emerging Issue Task Force Consensuses have either been implemented or are not significant to the Company.

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

Cautionary Statement

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements. Information in this Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations," and elsewhere in this 10-Q that does not consist of historical facts, are "forward-looking statements." Statements accompanied or qualified by, or containing, words such as "may," "will," "should," "believes," "expects," "intends," "plans," "projects," "estimates," "predicts," "potential," "outlook," "forecast," "anticipates," "presume," and "assume" constitute forward-looking statements and, as such, are not a guarantee of future performance. The statements involve factors, risks and uncertainties, the impact or occurrence of which can cause actual results to differ materially from the expected results described in such statements. Risks and uncertainties can include, among others, uncertainty regarding how long the worldwide economic

recession will continue and whether the recession will deepen; reductions in capital budgets by our customers and potential customers; changing product demand and industry capacity; increased competition and pricing pressures; advances in technology that can reduce the demand for the Company's products; and other factors, many or all of which are beyond the Company's control. Consequently, investors should not place undue reliance on forward-looking statements as predictive of future results. The Company disclaims any obligation to release publicly any updates or revisions to the forward-looking statements herein to reflect any change in the Company's expectations with regard thereto, or any changes in events, conditions or circumstances on which any such statement is based.

Results of Operations

A summary of the period to period changes in the principal items included in the condensed consolidated statements of income is shown below:

Summary comparison of the three months ended August 31, 2009 and August 31, 2008

	Increase / (Decrease)
Sales, net	$ 210,000
Cost of goods sold	$ (242,000)
Selling, general and administrative expenses	$ 137,000
Income before provision for income taxes	$ 310,000
Provision for income taxes	$ 138,000
Net income	$ 172,000

Sales under certain fixed-price contracts, requiring substantial performance over several periods prior to commencement of deliveries, are accounted for under the percentage-of-completion method of accounting whereby revenues are recognized based on estimates of completion prepared on a ratio of cost to total estimated cost basis. Costs include all material and direct and indirect charges related to specific contracts.

Adjustments to cost estimates are made periodically and any losses expected to be incurred on contracts in progress are charged to operations in the period such losses are determined. However, any profits expected on contracts in progress are recognized over the life of the contract.

For financial statement presentation purposes, the Company nets progress billings against the total costs incurred on uncompleted contracts. The asset, "costs and estimated earnings in excess of billings," represents revenues recognized in excess of amounts billed. The liability, "billings in excess of costs and estimated earnings," represents billings in excess of revenues recognized.

For the three months ended August 31, 2009 (All figures discussed are for the three months ended August 31, 2009 as compared to the three months ended August 31, 2008.)

	Three months ended		**Change**	
	August 31, 2009	**August 31, 2008**	**Increase / (Decrease)**	**Percent Change**
Net Revenue	$ 5,014,000	$ 4,804,000	$ 210,000	*4%*
Cost of sales	3,282,000	3,524,000	(242,000)	*-7%*
Gross profit	$ 1,732,000	$ 1,280,000	$ 452,000	*35%*
...as a percentage of net revenues	*35%*	*27%*		

The Company's consolidated results of operations showed a 4% increase in net revenues and an increase in net income of 116%. Revenues recorded in the current period for long-term construction projects were 66% higher than the level recorded in the prior year. Revenues recorded in the current period for other-than long-term construction projects (non-projects) were down 37% from the level recorded in the prior year. The gross profit as a percentage of net revenues for the current and prior year periods was 35% and 27%. This fluctuation is attributable primarily to a.) one large, domestic project in process last year that had a very low margin, b.) a few of the bigger non-project shipments in the first quarter last year had low margins, and c.) three large export projects have higher than average margins.

While the overall sales figures showed only a modest gain over the prior year, the mix of customers buying our products changed. Sales of the Company's products are made to three general groups of customers: industrial, construction and aerospace / defense. The negative effect of the continued slow global construction market has been offset by an increase in our global sales to customers in the aerospace and defense markets. A breakdown of sales to the three general groups of customers is as follows:

First Quarter - Fiscal 2010		First Quarter - Fiscal 2009	
Industrial	6%	Industrial	13%
Construction	40%	Construction	50%
Aerospace / Defense	54%	Aerospace / Defense	37%

At August 31, 2008, we had 119 open sales orders in our backlog with a total sales value of $9.5 million. At August 31, 2009, we have 8% fewer open sales orders in our backlog (110 orders) but the total sales value is $11.3 million or approximately 19% higher than the prior year.

The Company's revenues and net income fluctuate from period to period. The fluctuations in comparing the current period to the prior period are not necessarily representative of future results.

Selling, General and Administrative Expenses

	Three months ended			Change
	August 31, 2009	August 31, 2008	Increase / (Decrease)	Percent Change
Outside Commissions	$ 276,000	$ 202,000	$ 74,000	*37%*
Other SG&A	904,000	841,000	63,000	*7%*
Total SG&A	$1,180,000	$1,043,000	$ 137,000	*13%*
...as a percentage of net revenues	*24%*	*22%*		

Selling, general and administrative expenses increased by 13% from the prior year. Outside commission expense increased by 37% from last year's level. As a percentage of sales, outside commissions were 5.5% compared with 4.2% last year. This fluctuation was primarily due to a single, high value, non-project, commissionable sales order recorded during the quarter as well as a higher level of Project sales in the current year. As noted above, a few of the Projects have high gross margins. These projects also have higher than average commissions. Other selling, general and administrative expenses increased only slightly from last year to this.

The above factors resulted in operating income of $552,000 for the three months ended August 31, 2009, up 133% from the $237,000 in the same period of the prior year.

Stock Options

The Company has a stock option plan which provides for the granting of nonqualified or incentive stock options to officers, key employees and non-employee directors. Options granted under the plan are exercisable over a ten year term. Options not exercised at the end of the term expire.

The Company applies the stock option expensing rules of Statement of Financial Accounting Standards (SFAS) No. 123R, "Share Based Payment," using the fair value recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation." The Company recognized $20,000 and $28,000 of compensation cost for the three month periods ended August 31, 2009 and August 31, 2008.

The fair value of each stock option grant has been determined using the Black-Scholes model. The model considers assumptions related to exercise price, expected volatility, risk-free interest rate, and the weighted average expected term of the stock option grants. Expected volatility assumptions used in the model were based on volatility of the Company's stock price for the thirty month period ending on the date of grant. The risk-free interest rate is derived from the U.S. treasury yield. The Company used a weighted average expected term. The following assumptions were used in the Black-Scholes model in estimating the fair market value of the Company's stock option grants:

	2009	2008
Risk-free interest rate:	4.875%	5.000%
Expected life of the options:	2.5 years	2.5 years
Expected share price volatility:	57.57%	44.62%
Expected dividends:	zero	zero

These assumptions resulted in:

Estimated fair-market value per stock option:	$1.37	$1.94

The ultimate value of the options will depend on the future price of the Company's common stock, which cannot be forecast with reasonable accuracy.

A summary of changes in the stock options outstanding during the three month period ended August 31, 2009 is presented below:

	Number of Options	Weighted-Average Exercise Price
Options outstanding and exercisable at May 31, 2009:	160,000	$ 4.98
Options granted:	14,500	$ 3.51
Options outstanding and exercisable at August 31, 2009:	174,500	$ 4.86
Closing value per share on NASDAQ at August 31, 2009:		$ 3.59

Capital Resources, Line of Credit and Long-Term Debt

The Company's primary liquidity is dependent upon the working capital needs. These are mainly inventory, accounts receivable, costs and estimated earnings in excess of billings, accounts payable, accrued commissions, billings in excess of costs and estimated earnings, and debt service. The Company's primary sources of liquidity have been operations and bank financing.

Capital expenditures for the three months ended August 31, 2009 were $79,000 compared to $123,000 in the same period of the prior year. As of August 31, 2009, the Company has no commitments for capital expenditures during the next twelve months.

Effective August 7, 2009, the Company replaced its bank credit facility with a $6,000,000 demand line of credit from a bank, with interest payable at the Company's option of 30, 60, 90 or 180 day LIBOR rate plus 2.5% or the bank's prime rate less .25%. There is an interest rate floor of 3.5%. The line is secured by accounts receivable, equipment, inventory, and general intangibles, and a negative pledge of the Company's real property. This line of credit is subject to the usual terms and conditions applied by the bank and is subject to renewal annually. There is a $573,000 principal balance outstanding as of August 31, 2009, compared to the $1,017,000 balance outstanding on the line of credit in place as of May 31, 2009. The outstanding balance on the line of credit will fluctuate as the Company's various long-term projects progress. The Company is in compliance with restrictive covenants under the line of credit. In these covenants, the Company agrees to maintain the following minimum levels of the stated item:

Covenant	Minimum per Covenant	Current Actual	When Measured
Minimum level working capital	$3,000,000	$9,322,000	Quarterly
Minimum debt service coverage ratio	1.5:1	n/a	Fiscal Year-end

All of the $5,427,000 unused portion of our line of credit is available without violating any of our debt covenants.

Principal maturities of long-term debt for the remainder of the current fiscal year and the subsequent five years are as follows: 2010 - $4,000; 2011 - $5,000; 2012 - $6,000; and 2013 - $4,000.

Inventory and Maintenance Inventory

	August 31, 2009		May 31, 2009		Increase / (Decrease)	
Raw Materials	$ 464,000		$ 524,000		$ (60,000)	*-11%*
Work in process	5,448,000		5,688,000		(240,000)	*-4%*
Finished goods	675,000		510,000		165,000	*32%*
Inventory	6,587,000	*90%*	6,722,000	*89%*	(135,000)	*-2%*
Maintenance and other inventory	732,000	*10%*	809,000	*11%*	(77,000)	*-10%*
Total	$7,319,000	*100%*	$7,531,000	*100%*	$ (212,000)	*-3%*
Inventory turnover	1.8		1.6			

NOTE: Inventory turnover is annualized for the three month period ended August 31, 2009.

Inventory, at $6,587,000 as of August 31, 2009, is $135,000 or two percent lower than the prior year-end level of $6,722,000. Of this, approximately 83% is work in process, 10% is finished goods, and 7% is raw materials. While this decrease is not significant, it is one factor in the increase in the inventory turnover rate. The inventory turnover is calculated by dividing the annualized cost of sales by the average inventory level. The annualized cost of sales for the current period is $13,128,000, which is slightly over $1 million more than last year's level for the full year. This is the primary reason for the increase in the inventory turnover rate. The average level of inventory for the three months ended August 31, 2009 was $7,425,000. This is only $97,000 lower than the average level for the fiscal year ended May 31, 2009.

Maintenance and other inventory represent stock that is estimated to have a product life cycle in excess of twelve months. This stock represents certain items the Company is required to maintain for service of products sold and items that are generally subject to spontaneous ordering. This inventory is particularly sensitive to technological obsolescence in the near term due to its use in industries characterized by the continuous introduction of new product lines, rapid technological advances and product obsolescence. The maintenance inventory decreased slightly since May 31, 2009. Management of the Company has recorded an allowance for potential inventory obsolescence. The provision for potential inventory obsolescence was $45,000 for each of the three month periods ended August 31, 2009 and August 31, 2008. The Company continues to rework slow-moving inventory, where applicable, to convert it to product to be used on customer orders.

Accounts Receivable, Costs and Estimated Earnings in Excess of Billings ("CIEB"), and Billings in Excess of Costs